The International Insolvency Review

Third Edition

Editor
Donald S Bernstein

Law Business Research

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EDITOR'S PREFACE

This third edition of *The International Insolvency Review* once again offers an in-depth review of market conditions and insolvency case developments in key countries around the world. As always, a debt of gratitude is owed to the outstanding professionals in geographically diverse locales who have contributed to this book. Their contributions reflect diverse viewpoints and approaches, which in turn reflect the diversity of their respective national commercial cultures and laws.

The preface to the 2014 edition of this book touched upon the challenges faced by large multinational enterprises attempting to restructure under these diverse and potentially conflicting insolvency regimes. These challenges are particularly acute in large corporate insolvencies, because neither UNCITRAL's Model Law on Cross-Border Insolvency nor other enactments, such as the European Union's Regulation on Insolvency,[1] provide the tools necessary for consolidated administration of insolvencies involving multiple legal entities in a corporate group, with operations, assets and stakeholders under different corporate umbrellas in different jurisdictions.[2] Insolvent corporate groups are therefore obliged to cobble together consensual restructurings with local stakeholders in key jurisdictions, or to initiate separate plenary insolvency proceedings for individual companies under multiple local insolvency regimes (as illustrated in the cases of *Nortel*

1 Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, 2000 O.J. (L 160) 1, available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2000:160:0001:0018:en:PDF.

2 On 20 May 2015, the European Parliament and Counsel published the Recast Regulation on Insolvency 2015/848 (the 'Recast Regulation'), which will apply to insolvency proceedings initiated after 26 June 2017. The Recast Regulation contains a provision for voluntary, non-binding group coordination proceedings in the EU. The practical impact of this new tool remains to be seen.

and *Lehman Brothers*, among others), with added costs, dispersed control, legal conflicts and inconsistent judgments.

As discussed in last year's edition, the search for a legislative or treaty-based solution to this problem is ongoing, but any such solutions would necessarily involve some degree of relinquishment of national sovereignty and a ceding of local jurisdiction and control that may be difficult for local interests to accept, especially without substantial convergence in national insolvency laws. Given the lack of statutory tools, for some time it has been common in cross-border cases to implement insolvency protocols designed to address potential procedural, and in some cases substantive, conflicts. These agreements may be limited to providing a general framework for cross-border cooperation and coordination, or they may also include specific procedures for deferral, claims resolution, communication between the courts or other particular needs of an individual case.[3] Since the time of the *Maxwell Communications* case, cross-border protocols have enjoyed widespread support from insolvency practitioners and organisations, including from the American Law Institute, the International Insolvency Institute and INSOL Europe.[4]

However, while cross-border protocols are often valuable tools in multinational corporate group insolvencies, they are inherently limited in important ways. Absent supranational legal regimes, courts can only adjudicate disputes under the laws of their own countries, and parties can only be bound to the extent that the writ of the local court can be enforced against them. Fundamentally, cross-border protocols cannot expand the sovereignty or jurisdiction of the court presiding over an insolvency proceeding, superimpose a single governing substantive law or extend the reach of enforcement of local law against foreign parties. This is especially true if multiple plenary insolvency proceedings have been instituted under divergent national legal regimes with respect to members of a corporate group. Cross-border protocols are not a replacement for the enactment of supervening multi-jurisdictional solutions that bring all of the proceedings under a single controlling legal umbrella.

Some observers believe that the deficiencies in the protocol approach to cross-border insolvencies go beyond their inherent limitations. Questions have been raised about whether the effort to overcome these deficiencies leads to aberrational results, as the parties and the courts try to live up to the cooperative spirit of such protocols. In one such critique, former US bankruptcy court Judge James M Peck, who oversaw a number of cases employing cross-border protocols, most notably the *Lehman Brothers* case, recently addressed this issue in the context of the ongoing fight over distributions in

3 See UNCITRAL Practice Guide on Cross-Border Insolvency Cooperation, New York 2010, available at www.uncitral.org/pdf/english/texts/insolven/Practice_Guide_Ebook_eng.pdf.

4 See Final Supplemental Order Appointing Examiner and Approving Agreement Between Examiner and Joint Administrators, *In re Maxwell Comm. Corp,* Case No. 91-15741 (Bankr. S.D.N.Y. 15 January 1992); see also Guidelines Applicable to Court-to-Court Communications in Cross-Border Cases, published by the American Law Institute (16 May 2000) and adopted by the International Insolvency Institute (10 June 2001); European Communication and Cooperation Guidelines for Cross-Border Insolvency, prepared by INSOL Europe's Academic Wing (2007).

the *Nortel Networks* insolvency cases.[5] As discussed in greater detail in the United States chapter of this review, various Nortel entities initiated plenary insolvency proceedings in the US, UK and Canada. After the sale of substantially all of Nortel's assets, the question remained of how to allocate the resulting US$7.3 billion fund among creditors of the various estates. The parties implemented a cross-border protocol that was designed to promote consistent determinations of legal issues in the various proceedings.[6] After years of legal manoeuvering, the US and Canadian courts did indeed reach consistent decisions, following a trial 'held in two cross-border courtrooms linked by remarkable and effective technology,' on the methodology for distributing the fund to creditors.[7] However, despite the legal wrangling that has so far cost the Nortel and its creditors over US$1 billion in legal fees, as Judge Peck notes, US bondholders have questioned the legitimacy of the rulings under US law, and appeals have been filed.[8] As Judge Peck explains, even the most accomplished commercial judges may have a 'propensity to seek pragmatic resolutions in good faith that may solve the problem presented but that may deviate from a merits based determination'.[9] While judges in multi-jurisdiction insolvency cases should be praised for trying to fit a single irregular peg into both a square and a round hole, it is certainly worth asking whether the integrity of a court's process can be compromised in the struggle to do so.

Judge Peck argues that courts should not overly strive to enhance consistency in decision making across jurisdictions, as 'judges who are performing their jobs faithfully within their home court system are doing all that is required of them.'[10] If parties fear inconsistent outcomes, they may be more willing to enter into binding arbitration or find other means of settling their differences as, Judge Peck suggests, they did in the *Lehman Brothers* case.[11]

While it runs against the grain, after all the efforts of the past 25 years to promote cooperation and coordination in international insolvencies, to suggest that judicial cooperation can sometimes work at cross-purposes with efficient administration of cross-border insolvencies, there is no denying that the likelihood of speedy, clear and accurate (even if inconsistent) substantive adjudication drives settlements in large complex cases. In cross-border cases, striving for judicial decisions that are hard to challenge, even if inconsistent, may be a straighter path to a practical outcome than striving to attain wholly symmetrical results.

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5 James M. Peck, A Cross Border Judicial Dilemma – Conflict and Consistency in Insolvency Cases that Span the Globe, Banking & Financial Services Law Association, Brisbane, Australia (4 September 2015).

6 Id.

7 *In re Nortel Networks, Inc.*, 532 B.R. 494 (Bankr. D. Del. 2015).

8 James M. Peck, A Cross Border Judicial Dilemma – Conflict and Consistency in Insolvency Cases that Span the Globe, *supra* note 4.

9 Id.

10 Id.

11 Id.

Of course, the need for judges to make such pragmatic choices would be reduced if there were clear legal enactments providing for the alignment of insolvency outcomes across jurisdictional lines.

I once again want to thank each of the contributors to this book for their efforts to make *The International Insolvency Review* a valuable resource. As each of our authors, both old and new, knows, this book is a significant undertaking because of our effort to provide truly current coverage of important commercial insolvency developments around the world. My hope is that this year's volume once again will help all of us reflect on the larger picture, keeping our eye on likely, as well as necessary developments on the near and, alas, distant horizon.

Donald S Bernstein
Davis Polk & Wardwell LLP
New York
October 2015

Chapter 26

POLAND

Krzysztof Żyto and Milena Bełczącka[1]

I INSOLVENCY LAW, POLICY AND PROCEDURE

i Statutory framework and substantive law

Polish bankruptcy law (Bankruptcy and Rehabilitation Law Act of 23 February 2003, Dz.U.2012.1112, BRL) provides for two types of bankruptcy proceedings: liquidation bankruptcy and arrangement bankruptcy. Under the former type, a court-appointed trustee liquidates the debtor's estate, usually by selling the debtor's enterprise in whole or in part. The objective of arrangement bankruptcy is to preserve the debtor's enterprise by entering into an arrangement with its creditors. The arrangement scheme provides for restructuring of the debtor's liabilities, primarily through debt reduction and rescheduling. In declaring arrangement bankruptcy, the court may leave the administration of the debtor's assets with the debtor, under court supervision, or may appoint an administrator to administer the debtor's assets. The BRL also provides for separate rehabilitation proceedings if the debtor faces a threat of insolvency. The objective of rehabilitation proceedings is to arrive at an arrangement with creditors while avoiding a declaration of bankruptcy. However, the regulations governing rehabilitation proceedings are imperfect and are seldom used in practice. At present, work has been completed on new legislation related to restructuring proceedings that are set to enter into force in 2016 (more information is provided below).

Order of payments

Bankruptcy proceedings are to be conducted in a manner ensuring the fullest possible repayment of creditors without harm to them or their interests. Under bankruptcy

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proceedings involving the liquidation of the debtor's estate, each claim submitted is assigned to a class. The class assignment affects the order of repayment during the liquidation of the debtor's estate. The highest-ranking class includes, among other items, the costs of the bankruptcy proceedings; liabilities under contracts executed prior to the declaration of bankruptcy whose performance is required by the trustee; liabilities resulting from the actions of the trustee or administrator; and liabilities resulting from actions taken by the debtor after the bankruptcy declaration that do not require the court supervisor's consent or actions taken with his or her consent. The subsequent classes include, among other items, liabilities under employment contracts, alimonies and disability pensions, social insurance premiums, taxes and other public impositions. The fourth class includes other liabilities, including claims under contracts executed by the debtor prior to the bankruptcy declaration.

In the case of arrangement proceedings, some claims are unaffected by the scheme of arrangement and may be pursued according to general principles of law, without bankruptcy proceedings. Such claims primarily include liabilities originating after the bankruptcy declaration, alimonies and disability pensions, social insurance premiums and employment-related liabilities.

Claims secured by property rights over the debtor's estate (e.g., by a mortgage) are repaid separately from all other claims. Secured creditors are to be repaid from the proceeds from the liquidation of the bankruptcy estate. In arrangement bankruptcy, claims secured with property rights are excluded from the arrangement scheme unless the secured creditors consent to inclusion prior to a vote on the arrangement.

Ineffectiveness of legal transactions

The BRL provides for a range of situations in which actions taken by the debtor before filing for bankruptcy are considered ineffective by law or as a result of a court ruling. These measures are designed to protect creditors from the debtor's actions in the period preceding the bankruptcy declaration.[2]

Any actions taken by the debtor in the year preceding the filing of the bankruptcy declaration to dispose of the debtor's assets (including admission of a claim to the assets by the debtor or waiver of such a claim and entry into a court settlement), whether for a consideration or gratuitously with the value of the debtor's performance flagrantly exceeding the value of the mutual performance of the claim, are held to be ineffective by law.

Furthermore, any security or payment by the debtor of debt that is not yet due, if it is made in the two months before the date of submission of the bankruptcy declaration, are also held to be ineffective. A beneficiary of such actions may, however, demand that they be declared effective if, at the time they were made, he or she was unaware that grounds for a bankruptcy declaration existed.

Any security interest established in connection with forward transactions, loans of securities or sales of financial instruments with an obligation to buy back before the date of the bankruptcy declaration may not be deemed ineffective.

2 Articles 127–130 of the BRL.

Any legal transaction for a consideration effected by the debtor in the six months prior to the filing of the bankruptcy declaration will also be deemed ineffective if the counterparty is a spouse or any other 'close person'[3] (or, in the case of companies or partnerships, if the transaction is between the debtor and their partners, shareholders, representatives or their spouses; with affiliates, their partners, shareholders, representatives or their spouses; as well as with a holding or subsidiary company controlled by the debtor).

The court may also declare other legal transactions (or their parts) ineffective if certain conditions stipulated in the BRL are met (this applies, for instance, to consideration paid to the debtor's representatives, the establishment of security interests, etc.). In such cases, only the trustee, court supervisor or administrator are authorised to demand that the transaction be declared ineffective.

ii Policy

Bankruptcy law in Poland is evolving towards an emphasis on company restructuring and reflects the European tendency to pursue the policy of a second chance for entrepreneurs.

The BRL regulates the joint pursuit of claims against debtors who are entrepreneurs and the consequences of declaring bankruptcy, as well as the rules of rehabilitation proceedings that apply to entrepreneurs facing a threat of insolvency. The most recent amendment to the BRL entered into force on 1 January 2015 and concerns consumer bankruptcy.

The regulation concerning consumer bankruptcy underwent a considerable change to the benefit of creditors. Previously the regulation had been ineffective, and only several dozen consumers had declared bankruptcy over the course of the five years of it being in force. At present, almost any insolvent consumer who has at least one debt that he or she is unable to repay will be able to file a bankruptcy petition. The petition may be dismissed only when the debtor has contributed to his or her bankruptcy or considerably increased its extent, acting intentionally or as a result of gross negligence.

Current court and business practice reflects an ever stronger tendency to keep entrepreneurs in business by maintaining the debtor's enterprise after creditors are evenly repaid. Thus, this practice is in line with the tendency to bolster the competitiveness of home markets through corporate restructuring and keeping entrepreneurs in business. There is also a tendency to liberalise the regulations concerning consumers.

iii Insolvency procedures

As mentioned above, the BRL regulates two separate types of proceedings: liquidation bankruptcy and arrangement bankruptcy. An alternative procedure is rehabilitation, which in practice is applied very infrequently.[4] Consumer bankruptcy is regulated separately.

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3 Defined as a descendant, ancestor, sibling, relative by marriage in the same line or degree, adoptee or adopter and his or her spouse, as well as a partner.

4 http://bip.ms.gov.pl/pl/dzialalnosc/statystyki/statystyki-2011/download,1721,6.html – Table 41 (in Polish only).

Liquidation proceedings

The basic criterion for the declaration of a debtor's bankruptcy is his or her insolvency. Insolvency occurs when:

a the debtor fails to meet his or her liabilities as they fall due; or

b his or her liabilities exceed the value of his or her assets, even if the debtor meets the liabilities as they fall due.

A court may refuse to declare bankruptcy if the delay in meeting mature liabilities does not exceed three months and their sum does not exceed 10 per cent of the balance-sheet value of the debtor's enterprise. A debtor's bankruptcy is declared after evidence has been collected and the debtor's assets have been secured.

Upon the declaration of liquidation bankruptcy the debtor's assets become a bankruptcy estate and are used to repay creditors. The debtor's cash liabilities whose due date has not been reached become due, and non-cash liabilities become due as cash liabilities, even if their due date has not been reached. A declaration of liquidation bankruptcy also affects, among other matters, pending court and collection proceedings, and the possibility of setting off mutual claims. Under liquidation bankruptcy, it is no longer possible to conduct court and collection proceedings against the debtor, and all arbitration clauses expire.

When bankruptcy is declared, the debtor forfeits his or her right and ability to administer and dispose of his or her estate. The administration of the estate is taken over by the trustee, whose objective is to carry out proceedings for the repayment of the claims of all creditors using his or her powers to manage and dispose of the estate. The trustee liquidates assets, prepares a list of creditors and prepares the distribution of the proceeds from a liquidation among creditors. Once the liabilities of the estate and preferential claims are repaid or secured, the court delivers a ruling ending the bankruptcy proceedings.

A declaration of bankruptcy materially affects contracts executed by the debtor, and 'any contractual provisions stipulating the right to modify or terminate, in the event of declaration of bankruptcy, a legal relationship to which the debtor is a party shall be invalid'.[5]

Arrangement proceedings

A petition to open arrangement proceedings is filed by a debtor who is unable to meet his or her obligations and wants to defer debt repayment to remedy the financial situation of his or her enterprise without liquidating it. The debtor may file such a petition if he or she demonstrates that under the arrangement scheme creditors will be repaid to a higher degree than under liquidation proceedings. The debtor's petition should contain the proposed arrangement and should offer reasons for the proposal.

The objective of arrangement proceedings is to induce the majority of creditors to reduce considerably their debt claims, with repayment of the remaining portion deferred

5 Article 83 of the BRL.

or arranged to take place in instalments. This solution results in debt restructuring and offers the indebted enterprise a chance to overcome its financial crisis.

It is always possible to change the type of bankruptcy proceedings being undertaken; any proceedings started as arrangement proceedings may be converted to liquidation proceedings, and vice versa.

Rehabilitation proceedings

One legal solution enabling entrepreneurs to remove the threat of bankruptcy is the commencement of separate rehabilitation proceedings. Usually, these are out-of-court proceedings and are intended to restructure the entrepreneur's firm and restore its normal operations. Under this solution, the entrepreneur presents a rehabilitation plan and enters into a scheme with creditors to restructure his or her debt. Rehabilitation and debt reduction may be applied by entrepreneurs who manage to effect repayment of their liabilities (except in a situation when they default but the sum of overdue liabilities does not exceed 10 per cent of the balance sheet value of the enterprise) but expect that their enterprise will become insolvent.

The rehabilitation procedure is as follows:

a the entrepreneur threatened by insolvency initiates rehabilitation proceedings by filing a statement with the relevant court stating and substantiating the details of the debtor's case and the circumstances for the petition;

b the entrepreneur must also submit a rehabilitation plan and all relevant documents regarding his or her financial situation; and

c after the first two stages are completed, the creditors vote on the proposed arrangement. If it is accepted, the arrangement is filed with the bankruptcy court for approval. The approved rehabilitation arrangement is binding to the same degree as a scheme entered into during arrangement bankruptcy proceedings.

In practice, the provisions governing rehabilitation proceedings are a dead letter and the procedure itself has no wider application.

Consumer bankruptcy

The BRL also regulates bankruptcy of natural persons. A debtor who is a natural person may file for bankruptcy even if he or she has only one debt resulting in his or her insolvency. The rule is that the court dismisses a bankruptcy petition if the debtor contributed to his or her insolvency or considerably increased its extent intentionally or as a result of gross negligence, or if other bankruptcy proceedings were conducted in the last 10 years preceding the filing for bankruptcy.

When granting the petition, the court requests the creditors to submit their claims and appoints a trustee and a judge commissioner. Next, the court makes a repayment schedule, or cancels the debtor's liabilities if the debtor's personal situation clearly shows that he or she would not be capable of making any repayments.

The debtor is obligated to repay any acknowledged and listed claims within 36 months. In this period, the debtor may not execute any legal transaction concerning his or her property that might deteriorate his or her ability to carry out the repayment schedule.

The provisions regulating consumer bankruptcy introduced by the recent amendment of the BRL have been made considerably more liberal in order to increase the application of this instrument.

iv Starting proceedings

A petition for bankruptcy may be filed by the debtor or any of his or her creditors.

A creditor is defined as anyone entitled to seek payment from the bankruptcy estate, irrespective of what legal relationship his or her debt claim arises from, but only if their claim already existed at the time bankruptcy was declared.

The debtor is obliged to file a petition for bankruptcy within 14 days after the statutory prerequisites are met. Polish bankruptcy law provides for serious consequences for managers of the debtor's enterprise who delay filing for bankruptcy. They may suffer civil consequences (damages), tax liability and (in the case of companies) criminal liability.[6]

A petition to declare the bankruptcy of legal persons and unincorporated organisational units (e.g., commercial partnerships) may be filed by anyone who is empowered to represent these entities individually or jointly with others.

A petition to declare the bankruptcy of a deceased entrepreneur may be filed by his or her creditor, heir, spouse or each of his or her children or parents, even if they do not stand to inherit any of the debtor's estate.

The procedure for filing for bankruptcy, whether it is carried out by the debtor or by creditors, includes quite formal documentation requirements. If the bankruptcy petition is filed by a creditor, his or her debt claim must be substantiated in the petition, and, if he or she files for arrangement bankruptcy, a preliminary arrangement proposal must be provided.

Bankruptcy proceedings, whether they are of the arrangement or the liquidation type, are relatively lengthy. Participants in the proceedings always include the debtor and the party who filed for bankruptcy. Courts issue bankruptcy rulings within two months from the date of filing the petition, and the debtor, has the right to file a complaint with the court when his or her bankruptcy is declared.

v Control of insolvency proceedings

Usually, insolvency proceedings are controlled by a judge commissioner and a trustee. The control exercised by the judge commissioner involves verification and approval functions.

The control functions of the board of directors of the debtor vary depending on the type of bankruptcy proceedings being conducted.

When liquidation bankruptcy is declared, the debtor forfeits the right to manage, use and dispose of the property comprising the bankruptcy estate. The debtor is obliged to identify and deliver to the trustee all of his or her assets and submit all documents

6 Article 299 of the Civil Companies Code (liability for damages), Article 116 of the General Tax Regulations (tax liability), and Article 586 of the Civil Companies Code (criminal liability).

related to his or her business, property and accounts. He or she is also obliged to furnish the judge commissioner and the trustee with all necessary explanations related to the property. The BRL amendment that entered into force on 1 January 2015 introduced a mechanism permitting considerably stricter control over cash flows made on the trustee's instruction. Pursuant to Article 227 of the amended BRL (in force since 27 July 2015), the trustee is obligated to remit, to an interest-bearing bank account or a deposit account of the Finance Minister, any amounts comprising the bankruptcy estate and any proceeds from the transfer of items and rights over which property rights are secured. The above restriction does not only apply to funds subject to immediate release in accordance with the rules set out in the bankruptcy law.

When arrangement bankruptcy is declared, the debtor continues to administer his or her property under the supervision of the court supervisor and the judge commissioner, unless the bankruptcy court deprives the debtor of this right and appoints an administrator to administer the debtor's property. Upon declaration of arrangement bankruptcy, the debtor is obliged to furnish the judge commissioner and the trustee with all necessary explanations related to the property and enable the court supervisor to make himself or herself acquainted with the debtor's enterprise. The court may also impose further duties on the debtor. If the court deprives the debtor of the right to administer his or her property, the debtor is obliged to cooperate closely with the appointed administrator.

The following bodies may be appointed in the course of bankruptcy proceedings to represent creditors' interests:

a the preliminary creditors' meeting – convoked by the court to pass a resolution on the type of bankruptcy proceedings to be initiated, elect the creditors' council and (where relevant) enter into an arrangement;

b the creditors' meeting – convoked by the judge commissioner in certain situations (e.g., in the case of a change in the composition of the creditors' council) upon request by at least two creditors who jointly hold not less than one third of the total sum of acknowledged debt claims, or whenever the judge commissioner considers it necessary; and

c the creditor's council – if not already appointed by the preliminary creditors' meeting – may be appointed by the judge commissioner if he or she considers it necessary. In certain cases, the judge commissioner is obliged to appoint the creditor's council. The main role of the council is to support the trustee, the court supervisor or administrator, oversee their actions, assess the estate funds, approve actions that may be taken only with the approval of the creditors' council (e.g., withdrawal from the sale of the enterprise as a whole), as well as express their opinion on other issues if required by the judge commissioner, a trustee, the court supervisor or an administrator. In performing its duties, the creditors' council acts in the interests of all creditors.

vi Special regimes

Bankruptcy proceedings may be conducted only against those entities that have the capacity to be declared bankrupt. The following entities have no such capacity: (1) the Treasury; (2) units of local government; (3) independent public healthcare centres; (4)

institutions and legal entities established by statutes and in performance of obligations imposed by statute; (5) individual farmers; and (6) universities. No bankruptcy may be declared with respect to the National Bank of Poland and certain types of research and development units carrying on scientific research and developmental work.

The BRL also contains regulations related to separate bankruptcy proceedings for developers, banks and cooperative savings and credit funds, insurance and reinsurance companies, bond issuers and individuals not conducting business activities. Detailed regulations governing insolvency are also included in statutes in such areas as companies law, labour law, civil law, banking law, etc.

Bankruptcy proceedings for banks and other financial institutions differ markedly in form from the typical proceedings. The key role in such a case is played by the Polish Financial Supervision Authority (PFSA), which supervises the operations of financial institutions in Poland. If a bank's balance sheet at the end of a reporting year shows that its assets are insufficient to meet its liabilities or, for reasons connected directly with its financial situation, the bank fails to pay out funds deposited by its clients, the PFSA will suspend the bank's operations and permit its takeover by another bank. Only the PFSA may file a petition to declare a bank bankrupt.

The PFSA may also file a petition to declare the bankruptcy of an insurance company.

The right to file a petition for the bankruptcy of debtors that were granted public aid with a value of €100,000 or more is also bestowed on the authority that granted the aid.

Polish bankruptcy law does not provide for separate regulations for the bankruptcy of groups of companies.

In 2009 the BRL was supplemented by provisions related to consumer bankruptcy which, on account of their provisions, were hardly ever applied in practice.[7] Material changes in this respect were introduced by the amendment that came into force on 1 January 2015.[8]

vii Cross-border issues

With respect to bankruptcy proceedings in the European Union area, Poland applies European Council Regulation (EC) 1346/2000 of 29 May 2000 on insolvency proceedings (O.J. EC L.00.160.1, Regulation 1346). Under this Regulation, the opening of bankruptcy proceedings in one EU Member State results in the automatic recognition of the opening of the proceedings in Poland. The recognition of the opening of the main proceedings does not preclude the initiation of ancillary bankruptcy proceedings in Poland (without reference to the reason for the debtor's insolvency). Rulings by EU courts regarding the conduct and completion of bankruptcy proceedings, court approval of the arrangement scheme and all decisions related to the securing of claims are all recognised in Poland under the principles of Regulation 1346. Polish courts may refuse

7 In the period from 31 March 2009 to 31 December 2011, out of 1,875 petitions to declare consumer bankruptcy, only 36 bankruptcies were declared.

8 In the first half of 2015, 601 consumer bankruptcies were declared.

to recognise a foreign ruling related to bankruptcy proceedings only if its recognition or execution contradicts the fundamental principles of Polish law.

Forum-shopping is limited by EU rules on court jurisdiction. Pursuant to Article 3 of Regulation 1346, the courts with the jurisdiction to open insolvency proceedings are those within the EU territory where the debtor's main interests are situated. In the case of legal persons, the place of the registered office stated in the organisations' articles of association is presumed to be the site of their main interests. The courts of another Member State have jurisdiction to open insolvency proceedings against the debtor only if he or she possesses an establishment within the territory of that Member State, and the proceedings may be conducted only in respect of the assets of the debtor situated in the territory of that Member State.

Rulings on insolvency originating outside the European Union are recognised in accordance with the rules set forth in the BRL. Proceedings to recognise foreign insolvency proceedings are initiated upon the request of a foreign administrator, who must submit, among other documents, a copy of the ruling initiating bankruptcy proceedings and appointing the administrator to his or her function in the case, or any other credible form of written proof stating these facts (e.g., a statement from a foreign court). These documents must be translated into Polish. A foreign decision is recognised unless it falls within the exclusive jurisdiction of Polish courts and unless such recognition is contrary to the fundamental principles of the Polish legal system.

Legal regulations require courts and participants of bankruptcy proceedings to cooperate. Within the EU, the provisions of Regulation 1346 apply; thus, the administrator of the main proceedings and the administrators of the ancillary proceedings (trustees, appointed administrators or court supervisors) are obliged to cooperate with and to provide information to one another. In turn, under the BRL Polish courts are entitled to contact foreign courts and foreign administrators directly, and are obligated to cooperate with foreign units in insolvency cases. Trustees, court supervisors and administrators perform their duties by way of the court.

II INSOLVENCY METRICS

The Polish economy emerged largely unscathed from the 2008 recession and financial crisis, but in recent years a gradual reduction in the rate of gross domestic product (GDP) growth has been observed. Since 2013, an upward trend in domestic activity has been observed which became stronger in 2014 largely due to improving internal demand. According to the initial estimates of the Polish statistical office, in 2014 Poland's GDP increased by 3.3 per cent in real terms. Both industrial output and activity in construction and assembly sectors improved, as did exports and investments. These factors have resulted in a recovery in the financial situation of businesses and, consequently, may lead to a reduction in the number of bankruptcy proceedings being opened. The current political situation in Ukraine and its effects on exporters to Russia and Ukraine (among other factors, as a result of imposed embargoes) may pose risks for the Polish economy.

According to a report by the Coface Group (that is involved in securing claims), 823 bankruptcies were declared in Poland in 2014, which is the best result in the past four years (7 per cent less than in 2013). It is noteworthy that statistics concerning businesses

from sectors traditionally prone to bankruptcy show a greater decline in the number of declared bankruptcies. Among businesses, compared to 2013 there was a decrease of 14 per cent in bankruptcies in the manufacturing sector, and a decrease of 21 per cent in the number of bankruptcies in the construction sector. In 2014, the businesses that went bankrupt were mainly from the retail, manufacturing and construction sectors. This problem mainly affected small and medium-sized businesses, such as those with a turnover of up to 5 million złotys (31 per cent of bankruptcies) and between 5 million złotys and 50 million złotys (56 per cent of bankruptcies).

These numbers do not reflect the total number of insolvent businesses, since no account is taken of the petitions that were dismissed by courts due to the fact that the assets of the insolvent debtors were insufficient to cover the costs of bankruptcy proceedings. Research conducted by Coface shows that in 2014 there were 4,469 petitions for bankruptcy filed with Polish courts (compared to 4,806 petitions in 2013). Due to the lack of sufficient assets to carry out bankruptcy proceedings, 1,081 petitions were dismissed.

In the past 12 months, bankruptcy was declared by companies including Domex Sp z o.o. (construction wholesaler), Infrastruktura Kapuściska SA (infrastructure management and utilities supply), FagorMastercook SA (household appliance manufacturer), Alpine Bau GMBH Sp z o.o. Oddział w Polsce (construction) and HENPOL Sp z o.o. (construction).

III PLENARY INSOLVENCY PROCEEDINGS

In January 2014, the arrangement bankruptcy of GANT Development SA was declared. The court changed this declaration in July 2014 to one of liquidation bankruptcy. Proceedings were ultimately discontinued because the company's assets were insufficient to cover the costs of the bankruptcy proceedings, which were estimated to be at least 2.5 million złotys.

This company is the third largest development and construction company in Poland (based on the number of apartments sold throughout Poland) and is listed at the Warsaw Stock Exchange. Its financial problems began when it failed to repay 250 million złotys in bonds owed to around 2,500 investors. At present, the number of investors exceeds 1,000.

When the ruling discontinuing the bankruptcy proceedings becomes final, creditors who purchased apartments under construction by GANT will be forced to pursue their claims according to general principles of law. Unimplemented amendments to the provisions of Polish bankruptcy law introduced in April 2012 would have given them an opportunity to successfully pursue their claims in bankruptcy proceedings. Under the amended regulations, any funds paid with a view to purchasing apartments would have been deposited in an escrow account. Upon declaration of bankruptcy, the funds related to a particular project would have become a separate estate, as would the title to the land on which the project is being constructed and the funds that would have paid in the course of the bankruptcy proceedings for construction to be completed. These creditors would have become exclusively entitled to repayment from these separate estates, independently of any bank mortgages. Additionally, the creditors would have

been able to organise a meeting and pass a resolution on repayment from the funds collected in the escrow account or those allotted for the continuation and completion of the project by the trustee.

IV ANCILLARY INSOLVENCY PROCEEDINGS

i Alpine Bau GmbH of Wals, Austria

In January 2014, ancillary insolvency proceedings were opened in connection with the liquidation of the assets of Alpine Bau GmbH, an Austrian construction company from the Alpine Holding Group based in Wals, Austria.

The company built three stadiums in Gdansk, Poznan and Warsaw for the 2012 UEFA European Championships hosted by Poland and Ukraine, as well as several segments of Polish dual carriageways and motorways. The latter series of operations by the company in Poland led to claims by its Polish subcontractors estimated at several dozen million złotys. The pursuit of these claims in the main insolvency proceedings before the Austrian insolvency court had the result that GDDKiA (the Polish central road management authority) was left with a limited capacity to satisfy the claims, on the basis of a special statute enacted by the Polish parliament in 2012 following a large number of bankruptcies in the construction industry.

Under this statute, a Polish subcontractor who has performed a contract with the main contractor of a segment of dual carriageway or motorway, but has not received due payment because the latter was declared bankrupt, may submit its claims to GDDKiA. In this way, such claims may be repaid more promptly outside of the pending bankruptcy proceedings. To receive such repayment, a list of claims must be submitted specifying claims against the contractor that have been acknowledged and are undisputed. However, in this case, obtaining such a list from the Austrian insolvency court proved too time-consuming.

The initiation of ancillary bankruptcy proceedings in Poland allowed a list of claims to be obtained in a shorter time and facilitated the repayment of the subcontractors' claims by GDDKiA, which minimised the risk of their bankruptcy. This was of particular importance because the contracts with Alpine Bau GmbH were often the only source of income for these entrepreneurs.

ii Fabryka Mebli Tapicerowanych Christianapol Sp z o.o.

The ancillary bankruptcy proceedings involving the liquidation of the estate of Christianapol were declared in May 2013 and may therefore seem less topical in light of the current issues connected with cross-border bankruptcies. However, the ancillary bankruptcy of this company is noteworthy for at least two reasons.

First, the rulings issued by the Polish Supreme Court in a number of cases related to this bankruptcy have impacted on the interpretation of the public policy clause contained in Article 26 of Regulation 1,346.[9]

Second, the fact that the main insolvency proceedings involving this company were opened in France while it had its registered office in Poland has contributed to an amendment of the legal regulations related to the repayment of employees' cash claims in the case of their employer's insolvency. In this respect, the concept of employer insolvency (whose occurrence was a condition for the repayment of certain benefits to employees) was changed, such that an employer whose ancillary insolvency was declared would also be considered insolvent *simpliciter*. This change made possible the repayment of employees' claims resulting from the work performed by them in Poland in the period following the main declaration of insolvency in France and before the declaration of ancillary insolvency in Poland.

As mentioned above, the main safeguard insolvency proceedings against Christianapol were opened in France in October 2008 in accordance with the French Commercial Code, although the company's registered office (the site of its main interests), and the majority of its creditors were in Poland. The French court established its jurisdiction over the case, holding that the core of the defendant's business activities were located in France, given that the defendant was a member of the Cauval Industries Group, and that the grounds for opening bankruptcy proceedings were not directly connected with the financial situation of Christianapol, but with the entire group of companies. In addition, in July 2009, a plan to protect creditors providing for their repayment in instalments over a period of 10 years was agreed and approved.

In the course of court proceedings initiated by Polish creditors against Christianopol before Polish courts, usually for the payment of overdue amounts, an issue arose as to whether it was admissible, in light of Article 26 of Regulation 1,346, for a Polish court to appraise the ruling of a foreign court regarding the initiation of bankruptcy proceedings as concerns the establishment of jurisdiction by the foreign court and the grounds that it identified for opening bankruptcy proceedings. The Supreme Court held that such a ruling may be automatically recognised only when such recognition does not lead to a result that is clearly contrary to Polish public policy. Therefore, the Supreme Court established that what is relevant for acceptance of a ruling by a foreign court is not the basis of the ruling but whether a contradiction exists between the result of the ruling and Polish public policy. In this case, the result of the Supreme Court's decision was the initiation of proceedings similar to Polish rehabilitation proceedings.

V TRENDS

The first half of 2015 saw a continuation of the downward trend in the number of declared bankruptcies, although the change is not as marked as it was in 2014. The

9 Judgments of the Supreme Court of 16 February 2011 (file reference II CSK 326/10, II CSK 406/10, II CSK 425/10, II CSK 541/10), of 12 January 2012 (file reference II CSK 202/11) and of 2 February 2012 (file reference II CSK 305/11).

number of petitions for consumer bankruptcies has increased considerably, which is the result of the changes introduced at the beginning of 2015. Robust indices of economic growth indicate that the downward trend should continue. As a result of the embargo imposed by Russia in 2014, temporary problems are experienced by food and transport companies. If the situation persists, the number of bankruptcies among businesses from these sectors is likely to increase.

Among the practical measures taken to limit corporate bankruptcy, two trends are noteworthy. The first is the attempt to hold company managers liable for their failure to file for the bankruptcy of an insolvent company on time. In particular, these measures are being applied against the board directors of limited liability companies under the additional grounds for liability regulated in Polish companies law. The other trend is the tendency by courts to file for prohibitions on the conduct of business activity for managers who fail to file for bankruptcy on time or who obstruct bankruptcy proceedings by concealing assets.

The Act of 15 May 2015 that will enter into force at the beginning of 2016 essentially reforms the existing regulations of the bankruptcy law and introduces separate regulations concerning restructuring proceedings.

The main objective of the Act is to introduce effective instruments permitting restructuring of the debtor's enterprise and preventing its liquidation. Preservation of the debtor's enterprise is often better for creditors than its liquidation, and makes it possible to save jobs and generally execute orders without interruption, so it has positive social and economic significance.

The social perception of a particular legal regulation and the procedure through which restructuring is to take place are of major significance when carrying out an effective corporate restructuring. Practice shows that often the very fact that a debtor's bankruptcy has been declared precludes any chance of effective restructuring, irrespective of whether it is arrangement bankruptcy or liquidation bankruptcy. The association of bankruptcy with the end of business, economic failure and creditors' inability to recover their claims is so strong that in many cases, after bankruptcy has been declared, creditors do not want to engage in any talks with the debtor. For these reasons the Act separates restructuring proceedings from stigmatising bankruptcy proceedings. For a clear division, restructuring proceedings are regulated in a separate act, the Restructuring Law (RL).

Four types of restructuring proceedings are envisaged:

a arrangement approval proceedings;
b accelerated arrangement proceedings;
c arrangement proceedings; and
d curative proceedings.

The common characteristic of these proceedings is the debtor's restructuring – first, the restructuring of the debtor's liabilities, and then, to a varying degree, of his or her property, of the way his or her enterprise is managed and of employment. These proceedings are intended to ensure that the form of restructuring selected is best suited to the needs of a specific enterprise in a specific financial situation.

All the restructuring proceedings will be addressed both to those entrepreneurs who are insolvent and those who face insolvency. These proceedings will be unavailable to those entrepreneurs who are able to settle their liabilities and do not face a threat

of insolvency, but nonetheless would want to unfairly gain benefits from undergoing restructuring proceedings. Allowing insolvent debtors to be covered by restructuring proceedings is justified mainly by the interests of creditors, for whom it may be more advantageous to be repaid as a result of an arrangement than by liquidation of the debtor's assets in the bankruptcy proceedings.

The same regulations concerning the range of debt claims covered by an arrangement; arrangement proposals; execution and approval of the arrangement and its consequences; as well as rules for changing or cancelling the arrangement will apply to all the restructuring proceedings.

The first two proceedings can be conducted only when the sum of disputable claims conferring the right to vote on the arrangement does not exceed 15 per cent of all the claims conferring such right. The setting of the disputability threshold at 15 per cent results from the necessity to ensure that in every situation the decision to enter into an arrangement is made by the majority of creditors. When it is necessary to obtain the acceptance of creditors holding at least two-thirds of all the claims of voting creditors in order to enter into an arrangement (Article 124.1 RL), even if all creditors with disputable claims who vote in favour of the arrangement (a maximum of 15 per cent) are omitted, the decision is made by creditors holding more than 51 per cent of all the claims conferred to voting creditors.

The Act provides for a simplified procedure of making the list of claims. The arrangement approval proceedings will be conducted by the debtor, with the involvement of an arrangement supervisor. The court's role will be limited to delivering a ruling approving the arrangement adopted by the creditors by way of the debtor collecting their votes. The arrangement proceedings will be admissible if the sum of disputable claims conferring the right to vote on the arrangement exceeds 15 per cent of all the claims conferring such right. Curative proceedings involve, in addition to entering into an arrangement, a more extensive action aimed at restructuring the debtor's enterprise through a partial or total implementation of the curative plan in the course of the procedure, with an option to use instruments to reduce employment or rescind mutual agreements.

The Act introduces institutions that increase creditors' influence on the course of the procedure and reduce the role of the court and the judge commissioner. Creditors will be able to request that the creditors' council should be appointed and their request will obligate the judge commissioner to do so. In addition, the judge commissioner will be obligated to appoint to the creditors' council a creditor chosen by other creditors involved in the claims. Likewise, the judge commissioner will be obligated to change the composition of the creditor's council. Creditors holding 30 per cent of claims will be able, jointly with the debtor, to file a request to appoint a specific person to act as the court supervisor or administrator. The judge commissioner will be able to refuse to appoint such person only in exceptional cases.

The creditor's council will be able, among other things, to bring about a change of the court supervisor or administrator or enable the debtor to administer his or her enterprise within the extent of ordinary administration. The Act also provides a number of regulations intended to prevent prolongation of proceedings, and in particular will introduce time limits for the court supervisor, administrator, judge commissioner and the court.

The Act also introduces solutions to prevent the possibility of abusing restructuring proceedings to harm creditors. The court will refuse to open restructuring proceedings if the opening might result in harming the creditors, when the debtor's actions and the way of managing his or her enterprise and conducting negotiations with creditors shows that the only objective of such procedure would be to prevent creditors from successful debt enforcement (through getting rid of assets or conducting business in a seemingly inept way) or to vote through an arrangement with creditors towards whom fictitious obligations were incurred (for the benefit of entities with no formal links). For the same reasons, the court will discontinue restructuring proceedings. The discontinuation will open the way for creditors to file a simplified petition for bankruptcy. Until the simplified petition is examined, the debtor's assets will be secured by a court supervisor or administrator. In the event of a collision of a petition to open restructuring proceedings and a bankruptcy petition, the former will take precedence (but not absolute precedence) over the bankruptcy petition. To secure creditors' interests, the Act introduces a principle that enables the court to examine the bankruptcy petition first, before petitions for restructuring proceedings, if petitions for these proceedings are filed to harm creditors.

Appendix 1

ABOUT THE AUTHORS

KRZYSZTOF ŻYTO

Chajec, Don-Siemion & Żyto

Krzysztof Żyto is an attorney-at-law, partner and head of the restructuring and insolvency department at Chajec, Don-Siemion & Żyto.

Krzysztof specialises in dispute resolution and restructuring and insolvency law. His practice is focused on representing corporate clients in court and arbitration proceedings. Krzysztof has extensive expertise in civil procedure.

He advises media and telecommunication companies with foreign ownership and has represented major Polish telecom operators. Krzysztof advises bankruptcy trustees of companies operating in the banking, real estate and construction, TMT and healthcare sectors, in court proceedings against debtors as well as on matters connected with insolvency proceedings. Currently he is engaged in over 100 cases handled by our litigation and restructuring and insolvency departments.

Recently he advised the bankruptcy trustee of a Polish commercial television station in a liquidation-type bankruptcy. This case is precedential both in court and in legal doctrine as it concerns the withholding of enforcement, payment for bonds and a potential set-off of bond price receivables with bond redemption receivables. He also advised a Dutch Company on a case for repayment of a loan granted to a Polish company operating in the hospitality sector. The loan agreement was executed in the Netherlands and the repayment was sought before a Polish court, which resulted in issues with the choice of governing law.

Krzysztof also represented a leading Polish bank in insolvency proceedings of a debtor operating in the construction sector; a private client on a demand for compensation for losses incurred by a Forex trader in connection with the CHF exchange rate turmoil in January 2015; and a company from the TMT sector regarding a demand to pay the price for shares in a limited company with a concurrent demand that a set-off of the buyer's mutual claim be declared inadmissible as being contrary to bankruptcy law regulations.

Krzysztof is an arbitrator at the Court of Arbitration at the Polish Chamber of Commerce in Warsaw. In addition, he worked for 10 years as a judge at the Commercial Division of the Voivodeship Court in Poznań. His judicial practice concentrated on commercial law and civil procedures related to commercial claims.

Krzysztof is recommended by *The Legal 500* EMEA 2015 in the field of dispute resolution.

MILENA BEŁCZĄCKA

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Milena Bełczącka is an advocate and senior associate in the restructuring and insolvency department at Chajec, Don-Siemion & Żyto.

Milena specialises in dispute resolution, including commercial disputes, enforcement proceedings and bankruptcy law. She also deals with capital markets law and the protection of personal rights. She represents clients in proceedings before the Voivodship Administrative Courts, the Supreme Administrative Court and the Supreme Court.

Milena represents clients mainly from the real estate and construction, banking, insurance and TMT sectors, as well as general contractors, creditors and debtors in bankruptcy proceedings and court disputes. She has represented clients in lawsuits for damages, including before Austrian and German courts. Moreover, she advises bankruptcy trustees on matters connected with debtors' business activities in bankruptcy proceedings and in court disputes.

Currently she advises a number of bankruptcy trustees, for example on a case related to declaring ineffectiveness – in relation to the bankruptcy estate of one of the largest tour operators in Poland – of mortgages established on real properties comprising the bankruptcy estate and on a case related to a demand to pay the price for shares in a limited company with a concurrent demand that a set-off of the buyer's mutual claim be declared inadmissible as being contrary to bankruptcy law regulations.

Since 2008, Milena has cooperated with the Helsinki Foundation for Human Rights, for which she drafts documents for proceedings before the European Court of Human Rights in Strasbourg.

Milena graduated from the Lublin's John Paul II Catholic University Faculty of Law Studies, Konstanz's University Faculty of Law Studies (Germany), and completed a course at the German Law School of the Marie Skłodowska Curie University, in cooperation with the University of Hannover (Germany).

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