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THE LEGAL FRAMEWORK FOR PRIVATE SECTOR DEVELOPMENT IN A TRANSITIONAL ECONOMY: THE CASE OF POLAND*

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The economies of Central and Eastern Europe are in the midst of an historic transition from central planning and state ownership to market driven private sector development. This transition requires comprehensive changes in the “rules of the game”—i.e. the legal framework for economic activity. Markets presuppose a set of property rights¹ and a system of laws or customs that enable the exchange of those rights. The legal framework in a market economy has at a minimum three basic functions:

- (1) to define the universe of property rights in the system,
- (2) to set the rules for the entry and exit of actors into and out of productive activities, and
- (3) to set the rules of market exchange.

* This study is based in part on interviews with government officials, lawyers, and law professors in Poland. The findings, interpretations, and conclusions expressed in this paper are entirely those of the authors and should not be attributed in any manner to the World Bank, to its affiliated organizations, or to members of its Board of Executive Directors or the countries they represent. The authors would like to thank Youssef Djehane for his helpful insights and Andrzej Burzynski for his extensive comments and assistance.

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¹ As used in this context the term “property rights” includes rights to real, personal, and intellectual property.

Each of these three functions typically involves numerous areas of law. Property rights are defined in practice in most market economies by a wide array of laws regulating the ownership and use of real, personal, and intangible property, as well as shares in going concerns. Company, foreign investment, and bankruptcy laws are among the subset of laws that govern the entry and exit of actors into and out of productive activities. General rules of market exchange govern contract and competition law, while more detailed laws and regulations may govern more specific rules of market exchange in particular sectors.

This paper analyzes the evolving legal framework for private sector development in Poland using this general classification.² Poland has a rich legal tradition dating from pre-socialist times. This tradition, suppressed but not eliminated during its forty years of socialism, is being revised as the country moves toward a private market economy. The current legal framework in Poland closely follows other continental jurisdictions, particularly the French system, and has a clear and reasonable internal logic. While many of the laws are old,³ most are flexible enough to permit a wide range of modern market oriented activity. The 1964 Civil Code, modelled closely after the French Napoleonic Code, lays out underlying property and contract rights. Although adopted under the socialist regime, the Civil Code was drafted by law professors and, after being recently purged of socialist rhetoric, the Code is suitable for a market economy. Recent legislation, including the 1990 Antimonopoly Law and the recently adopted Securities and Foreign Investment Laws, appears to be quite well designed for private sector development. Moreover, Parliament (the "Sejm") recently adopted a new personal income tax, and a new value-added tax law is being considered and probably will be adopted in 1992. The most problematic area is property law, which is still, in the words of one Polish legal practitioner, a "jungle."

² This paper is part of a larger research project sponsored by the World Bank to study evolving legal frameworks in Eastern Europe. Other papers include Cheryl W. Gray et al., *Romania's Evolving Legal Framework for Private Sector Development*, 7 AM. U.J. INT'L L. & POL'Y (World Bank Working Paper No. 906, 1992); Cheryl W. Gray & Peter Ianachkov, *Bulgaria's Evolving Legal Framework for Private Sector Development* (forthcoming 1992); Gray & Stiblar, *The Evolving Legal Framework for Private Sector Activity in Slovenia* (World Bank Working Paper No. 893, 1992); and Gray et al., *Hungarian Legal Reform for the Private Sector* (forthcoming 1992).

³ For example, the company law (the Commercial Code), *infra* note 34, and the Bankruptcy Act, *infra* note 133, date from the 1930s.

Although the legal structure is generally satisfactory in most areas, practice remains uncertain in all areas. The generality of the laws leaves wide discretion for administrators and courts, and a body of cases and practice to further define the rules of the game has not yet developed. Although the courts are generally honest and are used by the population, they have little experience in economic matters. Judges are not well paid, and the best lawyers have a strong incentive to go into private practice. The wide discretion and general lack of experience and competence of judges create legal uncertainty that could hamper private sector development. The answer is not a change in the law, however, but a building of precedent and competence through training and dissemination of information.

I. RIGHTS TO REAL PROPERTY

Property rights reform has lagged behind legal reforms for general business activity in the last few years in Poland. The country is now facing legal dilemmas similar to those encountered in its Central and East European neighbors, where reforming socialist economies are facing numerous problems. Compensation laws for prior expropriations are creating tremendous uncertainty. Land registration and court adjudication systems are underdeveloped. Transfer laws for state property are sparking conflict among levels of government. Additionally, privatization laws for real property are undermining both financial system stability and local government solvency. Many specific procedures for real estate development and transfer are either missing from the current legal framework or are cumbersome and in practice unenforceable. Developing economically and environmentally sensible real property regulations and removing current legal bottlenecks are critical for sustained private sector investment.

While socialist law always considered land a means of production, various socialist systems have categorized it differently. For example, the Soviet Union took the position that land must be exclusively under state socialist ownership.⁴ In Bulgaria and Romania, agricultural land was not owned by the state but was "contributed" to cooperatives, with private owners retaining only nominal property rights.⁵

⁴ Vladimir V. Laptev, *Socialist Enterprises*, in VXXVII INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW ch. 16 at 3 (Borislav T. Blagojevic & Kenneth W. Dam eds., 1978).

⁵ See Viktor Knapp, *Socialist Countries*, in VI INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW 35, ch. 2 at 59 (Frederick Lawson ed., 1975).

In Poland, however, private ownership of land remained the rule, not the exception. Poland did place certain land under state ownership, including all of Warsaw, much other urban land, land occupied by state-enterprises, and about 20% of agricultural land, primarily in the northwest area recovered from Germany after World War II.⁶ Sale of public land rarely occurred in Poland because of the constitutional protections of state property. Instead, the principle of perpetual usufruct facilitated the private or cooperative acquisition of state property for construction. Perpetual usufruct conferred rights to the land user similar to ownership, typically for 99 years upon payment of a yearly fee. Either private individuals or tenants' housing cooperatives could hold rights of perpetual usufruct.⁷

A. Fundamental Concepts of Ownership—Recent Constitutional and Civil Code Reforms

Two fundamental principles distinguish a socialist system of real property rights from a market system of real property rights: (1) the hierarchy of types of property ownership depending on the nature of the owner, and (2) the indivisibility of state ownership.⁸ Recent

⁶ Laptev, *supra* note 4, at 3. Poland's state owned land accounted for 16.9% of its gross agricultural output. *Id.*

⁷ Four main forms of housing ownership existed under socialist law in Poland: (1) State rental apartments were typically allocated to families, who then had near-ownership rights of tenancy and inheritance but circumscribed rights to sublease and no right to sell (although they could "trade" for units occupied by other families). (2) Employee housing was allocated according to the employment relationship. (3) Cooperative housing units in multi-family units took one of two forms determined at the time of allocation: (a) tenancy, which was non-alienable, non-transferable to successors (other than those registered as living on the property), and not subject to execution or (b) ownership, which was alienable, transferable and subject to execution. (4) Private housing (individual houses or apartments) was limited to a single unit for family use, i.e. personal property. Additional private units were "private property" and were heavily regulated. For example by the 1974 Housing and Tenancy Act and the 1985 Land Use and Expropriation of Real Property Act, the state allocated tenants, set rents, and determined the landlord/tenant relationship. See e.g. Ustawa o gospodarce gruntami i wywłaszczeniu nieruchomości [hereinafter Land Use and Expropriation Act], Dziennik Ustaw [hereinafter Official Gazette], Issue No. 22 (1990).

⁸ Konstytucja [hereinafter Old Constitution], ch. II arts. 7-13, Official Gazette, Issue No. 7 (1976), translated in CONSTITUTIONS OF THE COMMUNIST WORLD (William B. Simons ed., 1980); Kodeks cywilny [hereinafter Civil Code], arts. 126-133, Official Gazette, Issue No. 16 (1964), translated in INSTITUTE OF STATE AND LAW, POLISH ACADEMY OF SCIENCES, CIVIL CODE OF THE POLISH PEOPLE'S REPUBLIC, (Prawnicze, Warsaw 1981).

amendments to the Polish Constitution and Civil Code have removed both of these principles.

1. *Hierarchy of Ownership*

The 1952 Polish Constitution defined the main categories of ownership, while the 1964 Civil Code governed the details.⁹ Under Polish socialist law, "social ownership," including ownership by the state, cooperatives, and social organizations, was the highest category of ownership and was protected by the Constitution,¹⁰ the Civil Code¹¹ and the Criminal Code.¹² Typically, such property included means of production (including, for example, land, mineral resources, and public utilities).¹³ In contrast, property used for personal consumption was individually owned and considered "personal property."¹⁴ Personal property could include, for example, one's dwelling house.¹⁵

On December 29, 1989, the Polish Constitution was amended to eliminate the socialist property classifications and instead treat all types of property equally in civil, administrative, and criminal matters.¹⁶ In particular, Article VII was amended to read that the Polish state shall "guarantee the complete protection of personal property."¹⁷ In 1990, the Civil Code was amended to abolish the distinction between personal and private property.¹⁸ In addition to protecting private property, the constitutional amendment to Article VII also states that "expropriation is permitted only for a public purpose and for just

⁹ See *supra* note 8.

¹⁰ *Id.*

¹¹ *Id.*

¹² Kodeks karny [Criminal Code], as amended by Official Gazette, Issue No. 72 (1990).

¹³ Old Constitution, *supra* note 8, at art. 12.

¹⁴ Civil Code, *supra* note 8, at art. 132.

¹⁵ *Id.* at art. 133. Another form of property in socialist law was individual—or private—property, defined as the individual ownership of means of production, a residue of presocialist economic relationships founded on exploitation and expected to wither away over time. *Id.* Individual property received less constitutional protection than social or personal property and was subject to heavy taxation and numerous limitations on use and transfer.

¹⁶ Old Constitution, *supra* note 8, as amended by Official Gazette, Issue No. 16 (1990) [hereinafter New Constitution], translated in CONSTITUTIONS OF THE COUNTRIES OF THE WORLD (Albert Blaustein & Gisbert Flanz eds. 1991).

¹⁷ *Id.* at art. 7.

¹⁸ Civil Code, *supra* note 8, as amended by Official Gazette, Issue No. 55 (1990). While this equality of property has been incorporated into the Constitution and the Civil Code, distinctions between public and private property have not yet been eliminated in other areas of law.

compensation.”¹⁹ This amendment narrowed state powers contained in the Land Use and Expropriation of Real Property Act of 1985,²⁰ and 1990 amendments to the Act further limited state power.

2. *Indivisibility of State Ownership*

The socialist state, as representative of the entire people, “indivisibly” owned all state socialist property under the previous system.²¹ Under this theory, neither local governments nor state owned enterprises owned the property they used, managed, or transferred; instead they had the right of operational administration, which gave them control over day-to-day use. Because property was indivisible, ownership was indeterminate. Those who “operationally administered” property could in some cases lease it but never sell it.

Assigning state property to specific government owners is one of the most complex challenges in the transition to a market economy. In Poland it has so far been a three-step legal process. First, a 1989 amendment to the Civil Code²² designated the Treasury or another state legal persona as the legal owner of state property, the first step to making such property alienable. Most state enterprises may now become owners of the land and buildings they previously administered. Second, Poland reestablished local governments in 1990, forty years after abolishing them. The Act on Local Autonomy²³ established a framework, which is not yet implemented, to assign local governments revenue rights, including taxation and spending responsibilities, land use planning, infrastructure provision, and housing management. The implementing regulations transfer without payment certain state property to the local governments, particularly property previously under their “operational administration.” This includes most urban land, the housing stock, public utilities, and certain state owned enterprises. Once divided among state actors, state property can then be legally alienated to private investors. Third, changes to the Land Use and Expropriation Act in 1990 granted the state and local governments

¹⁹ New Constitution, *supra* note 16, at art. 7.

²⁰ Land Use and Expropriation Act, *supra* note 7.

²¹ Civil Code, *supra* note 8, at art. 128.

²² One of the first steps towards distributing state property among the various departments of the state government.

²³ Ustawa o samorządzie terytorialnym [hereinafter the Act on Local Autonomy], Official Gazette, Issue No. 16 (1990), *amended in* Official Gazette, Issue No. 43 (1990).

the right to sell land outright, rather than being limited to granting only rights of usufruct.²⁴

B. Remaining Issues in Real Property Law Reform

Although fundamental principles of ownership in the Constitution and Civil Code are now consistent with the needs of a market economy, more specific reforms in land and housing law are needed. The area is extremely complex, governed apparently by over 50 different laws and regulations, ranging from agricultural land transfer to urban land taxation. Most land formerly under public ownership currently lacks clear title.

1. Reprivatization

Poland is now struggling with issues of compensation for expropriated former landowners, including how far back in time to go, whether to offer monetary or in-kind compensation, and what form compensation procedures should take. Plans within the government for resolution of outstanding expropriation claims range from no compensation at all to in-kind return of land, with voucher compensation as the most likely. The severity of the problem varies in importance in different parts of the country. The State nationalized all of the land in Warsaw after World War II, while land in other cities remained in private hands. On the agricultural side, the state owns about 20% of the land.²⁵ Until the reprivatization issue is settled, very little land with clear and indisputable title will be available, making land sales difficult and stalling investment.

Reprivatization is an area where technical assistance may be particularly appropriate. Poland has an opportunity to learn from other socialist economies in transition. For example, East Germany's compensation law is tying up substantial amounts of property in litigation,²⁶ and Hungary's housing privatization law is destabilizing the financial system while undermining local government solvency.²⁷ In particular, Poland must carefully weigh the effect of in-kind com-

²⁴ Amendment of Land Management, Real Estate Expropriation Law, Official Gazette, Issue No. 79 (1990), translated in JOINT PUBLICATION RESEARCH SERIES, EASTERN EUROPE REPORT No. 91-021S, Feb. 15, 1991, at 81.

²⁵ See *supra* note 6 and preceding text.

²⁶ J. Weedow, *Are you Insured Against Real Property Claims in East Germany?*, E. EUR. L. WK., Oct. 1, 1990, at 6.

²⁷ J. Telgarsky & R. Struyk, *Toward a Market Oriented Housing Sector in Eastern Europe*, 90 URB. INST. REP. 10, at 93-97 (1991).

pensation on the security of title. Firms and individuals will be reluctant to invest in property improvements if there is a chance that former owners can successfully reclaim the property at some later date. Other important concerns include the length of claims periods and the effects of alternative reprivatization schemes on fragile registration and court adjudication systems.

2. *Communalization*

The process of transferring state property to local governments, sometimes called "communalization," began simultaneously in all 2500 communes but has now stalled. Until the process is completed, with the land inventoried, disputes resolved, and land properly registered, local governments cannot make legal transactions to sell communal property.²⁸ Currently local governments are concluding some short-term leases, typically for high rents and only one year terms. Generally, local governments cannot make land with clear title available for sale or long-term lease, an essential element for sustained private sector investment. Communalization is another key area in which technical assistance may be appropriate, particularly to help streamline the process of registration and the adjudication of plots.

3. *Land Registration*

A well functioning registration system is the legal bedrock of any real property system. It is essential to securing and financing most investments, since ownership in a civil law system is determined by reference to the real estate register. However, Poland's registry system is in a state of disarray. Prior to the socialist takeover, three separate registration systems—Russian, German, and Austrian—existed in different parts of the country. Many of these registers are now missing or incomplete. Under socialism, the registration system was largely neglected for land under state ownership. As in other socialist countries, there were significant incentives for both individuals and the state not to comply with registration requirements. Individuals faced potential expropriation if found to own more property than permitted under socialist regulations, and the state did not need to register property to prove its ownership rights. Therefore many transfers were

²⁸ In particular, conflicts have arisen between local governments and state owned enterprises. Because of undefined land title, capital shortages, and inappropriate tax incentives, state enterprises have typically built large, low buildings, and claimed and held substantial amounts of vacant land that would otherwise revert to local government ownership through communalization.

not recorded. In Warsaw, for example, the pre-socialist owner is often still listed as the owner of record despite subsequent transfers.

4. *Notary System*

The notarial system poses a key constraint to emerging markets in land and housing.²⁹ All land transactions must by law be notarized to have legal effect, yet many problems plague the notary system. Until recently all notaries have been state employees, there has been a shortage of notaries, and notary transactions have been slow.³⁰ A recent positive step has been the privatization of state notaries. Also the property registers have been moved from the neglected state notary bureau into the court system, which is, however, not yet well enough equipped to administer them. A review and streamlining of the notary process, another area where technical assistance could be useful, is needed.

5. *Controls on Use of Real Property*

Even where ownership is presently clear, many controls on the use of real property remain narrow or unclear. The Parliament has transferred many of the responsibilities for controlling real property use to local governments, but has not given local governments the authority to exercise that responsibility properly. Deregulation should be a high priority. After removing inappropriate regulations, Poland will have to develop economically and environmentally sensible regulation in its place. Appropriate regulation of land use is an area where there has been substantial research and experience in recent years in market economies and an area where technical assistance could be rapidly fruitful. The three main areas for concern are: (1) zoning regulations, (2) building codes, and (3) ownership and rent controls.

a. *Zoning Regulations*

Warsaw has emerged from socialism with a highly inefficient pattern of urban land use. The static, end-state socialist land use planning system, coupled with reliance on industrial large panel construction methods tended to result in concentrations of high-rise apartment buildings outside the city center. This led to relatively high infra-

²⁹ The notarial system is also a bottleneck to the formation of companies, as discussed later in the paper, *infra* part III D2.

³⁰ It routinely takes six months to register a transfer.

structure and transportation costs with few spatial economies. Currently, the land use system is in limbo. A modern land use planning system is needed, one that offers wide discretion to the market, permits rapid, inexpensive, and accessible dispute resolution, and internalizes environmental and locational costs.³¹

b. Building Codes

Poland needs new building standards for the types of office and residential buildings that market systems are likely to produce. Discussions with legal practitioners suggest that, in the current unsettled environment, side payments are often required to secure location and building permits.³²

c. Ownership and Rent Controls

There are numerous restrictions on land use and transfer that need to be reviewed and streamlined. These include, for example, the use and transfer restrictions for agricultural land, including prohibitions on conversion of such land to urban and industrial uses. Another restriction that should be reviewed is the requirement that majority foreign-owned corporations obtain approval from the Ministry of Internal Affairs to purchase land or enter into long-term leases. Although it is understandable that Poland wants to monitor land purchases by foreigners, in the short run, given the currently volatile state of land markets, foreign investors should have ready access to business premises. The current approval process can be lengthy and can force some foreign investors to rely on the limited available forms of short-term leases.

Use of state owned rental housing is strictly controlled. The many restrictions on subleasing and conversion of rental units encourage massive and inefficient evasion, an experience common to socialist economies. Furthermore, rent levels are still controlled by the central government and do not allow local governments even to recover operating costs for housing stock, much less to service debt on

³¹ Parliament is currently considering two relevant laws. The first, the Act on Special Conditions for Realization of Housing Construction in Years 1991-1995 (otherwise known as the "Anti-Crisis Act"), attempts to provide an interim solution by granting municipal councils the authority to amend the official Master Plan of a city and to issue bonds for land purchase or infrastructure development. The second, the "Spatial Planning Act," provides a longer-term framework for land use planning.

³² Parliament is presently considering a new Building Code.

infrastructure.³³ Finally, the lack of a functioning foreclosure and eviction system is a key legal obstacle in Poland requiring priority attention: It prevents emergence of a private rental sector, constrains commercial real estate development, and stunts development of a housing finance system, a system which can be an engine for economic development. While a foreclosure and eviction system is in place legally, it has apparently never been used, despite over forty years of mortgage lending. Even as written, the procedure appears cumbersome and ill-suited to the needs of modern mortgage lending. For example, the foreclosure procedure requires the court auction to reflect an *ex ante* "market" price. New foreclosure procedures that allow property to be secured but that also fit local cultural norms might include forms of pledge, third-party guarantees, or liens on bank accounts and other movable property.

6. The Legal Forms for Multi-Family Dwellings

The legal forms for multi-family dwellings need to be reviewed and revised to promote the emergence of a viable real estate industry and eventual housing privatization. Reform of the law on cooperatives has been stalled, and cooperatives still have an unclear status, somewhere between public and private, under the Civil Code's revised property classifications. Numerous restrictions remain on the sale and transfer of cooperative property. At present there is no condominium law, an important legal tool for management of multi-family housing. Poland also has not yet developed clear rules for building management in partially privatized buildings.

In sum, real property rights reform in Poland threatens to become a key obstacle in the transition to a market economy. Many legal procedures remain untested, others are clearly inadequate, and further gaps are emerging through practice. Unless investors are reasonably assured of ownership, use, and transfer rights in property, they simply will not invest.

II. RIGHTS TO INTELLECTUAL PROPERTY

A broad framework for protecting intellectual property exists in Polish law. Patents, trademarks, and copyrights are protected under

³³ A "Rental Housing and Tenant Protection Act" has been submitted to Parliament. Among other things, it proposes a controversial two-year scheme to decontrol rents in public housing.

domestic law.³⁴ Poland is also a signatory to several major international treaties on intellectual property.³⁵

Although a broad framework exists, certain types of intellectual property are not well protected by existing law. In particular, the Law on Inventions does not allow patents on certain categories of inventions, including pharmaceuticals and chemicals, and the Copyright Law does not adequately protect computer software or sound recordings. These omissions have been the subject of intense international debate, particularly during negotiations of the recently concluded United States-Poland Treaty Concerning Business and Economic Relations.³⁶ In the copyright area, this treaty obligates Poland to adhere to the Paris text of the Berne Convention by January 1, 1991 and to extend copyright protection to computer programs by the end of 1991. In the patent area, it obligates Poland to extend the length of its patent protection to 20 years, to limit compulsory licenses³⁷ of

³⁴ These statutes include the Civil Code, *supra* note 8; Kodeks handlowy [hereinafter Commercial Code], Official Gazette, Issue No. 57 (1934), *translated in* POLISH SOCIETY OF ECONOMIC, LEGAL AND COURT TRANSLATORS, THE POLISH COMMERCIAL CODE, (published by Tępis Publishing House, Warsaw 1991) [hereinafter POLISH COMMERCIAL CODE], *amended by* Rozporządzenia Prezydenta Rzeczypospolitej o zmianie—Kodeks handlowy, Official Gazette, Issue No. 94 (1991); Ustawa o zwalczaniu nieuczciwej konkurencji [Unfair Competition Law], Official Gazette, Issue No. 56 (1930); Ustawa o prawie autorskim [hereinafter Copyright Law], Official Gazette, Issue No. 34 (1952), *amended by* Official Gazette, Issue No. 35 (1989); Ustawa o wynalazczości [hereinafter the Law on Inventive Activity], Official Gazette, Issue No. 33 (1984), *amended by* Official Gazette, Issue No. 35 (1989); Ustawa o znakach towarowych [Trademark Law], Official Gazette, Issue No. 5 (1985), *amended by* Official Gazette, Issue No. 35 (1989).

³⁵ These include, among others: the Paris Convention for the Protection of Industrial Property (Stockholm text), April 26, 1970, 21 U.S.T. 1583, 828 U.N.T.S. 305 (Poland signed this treaty March 24, 1975); the Universal Copyright Convention, Sept. 6, 1952, 25 U.S.T. 1341, 216 U.N.T.S. 133 (Poland signed Dec. 9, 1976); and the Berne Convention for the Protection of Literary and Artistic Works (Rome text), Aug. 1, 1931, 123 L.N.T.S. 233 (Poland signed Nov. 21, 1935). In August, 1990, Poland ratified the 1971 Paris text of the Berne Convention, S. Treaty Doc. No. 27, 99th Cong., 2d Sess. (1988), which extends copyright protection from 25 to 50 years. Poland's adherence, however, is limited only the administrative provisions. Eric S. Schwartz, *Recent Developments in the Copyright Regimes of The Soviet Union and Eastern Europe*, 38 J. COPYRIGHT Soc'y U.S.A. 123, 143 (1991). Poland is not a signatory to the Madrid Agreement for the International Registration of Trademarks of 1891, the Patent Cooperation Treaty of 1970, or the Hague Agreement for the International Deposit of Industrial Designs of 1925.

³⁶ S. Treaty Doc. No. 18, 101st Congress, 2d Session (1990), *reprinted in* 29 I.L.M. 1194 (1990). The treaty was signed on March 21, 1990. The U.S. Senate ratified the treaty in late 1990 and the Polish Parliament ratified it in mid-1991.

³⁷ A compulsory license provision allows the government to compel the holder

patented technology, and to extend the coverage of its patent law to cover pharmaceuticals, foodstuffs, and chemical products by December 31, 1992. There has been great resistance to these treaty provisions on the part of the Polish software and pharmaceutical lobbies, which have feared incurring liabilities due to their use of foreign intellectual property over the past forty years. There has also been widespread debate within the Polish community, and more generally within reforming socialist countries and developing countries, on whether the benefits of such rigorous patent protection outweigh the costs.³⁸ On the positive side, intellectual property protection helps spur domestic invention and creation and helps to attract foreign investment from firms with high technology products. On the negative side, granting monopoly rights tends to raise the domestic price of protected technology. The most contentious areas are patents for pharmaceuticals, where lives are often at stake, and copyrights for computer software and books, which are easily copied and are crucial for economic development.

Administrative and institutional problems within this area of law are similar to those encountered in other areas. The Polish patent office is not prepared for new and more sophisticated problems. Qualified regulators are scarce, and investigation procedures are weak. As in other areas of law, enforcement proceedings tend to be seen as state intervention, which remains politically unpopular.

III. COMPANY LAW

The current applicable company law in Poland is the Commercial Code of 1934.³⁹ Although the law fell into disuse during Communist rule, it was never entirely abrogated.⁴⁰ However, a variety of gov-

of a patent to sell non-exclusive use rights to a third party. Many countries provide for compulsory licenses in their patent laws, and such licenses are also allowed under the Paris Convention. In Poland compulsory licenses have been used sparingly. About two or three were granted annually during the 1970s and 1980s, and of the total over this period only two or three involved foreign patents.

³⁸ See generally WOLFGANG E. SIEBECK, STRENGTHENING PROTECTION OF INTELLECTUAL PROPERTY IN DEVELOPING COUNTRIES: A SURVEY OF THE LITERATURE (World Bank Discussion Paper No. 112, 1990).

³⁹ Commercial Code, *supra* note 34.

⁴⁰ Apparently some types of state owned companies, including Foreign Trade Organizations and some banks, continued to be organized as companies under the commercial code. Eventually the Civil Code of 1964 abrogated the Commercial Code except for sections 9, 11, and 12, which deal with company forms. Civil Code, *supra* note 8.

ernmental restrictions⁴¹ made this law virtually unusable. During this period, the Commercial Code was not taught in the universities, nor was it a subject for litigation. As a result lawyers and judges are unfamiliar with its application.

The Commercial Code did not reemerge until the 1980s, when it was revitalized to accommodate Poland's economic liberalization. This comeback started with the Law on State Enterprises of 1982,⁴² which opened up the possibility of creating joint ventures with foreign or domestic partners. The comeback continued with the first Foreign Investment Law of 1986,⁴³ the Foreign Investment Law of 1988,⁴⁴ and the Foreign Investment Law of 1991,⁴⁵ which called for foreign investment to be organized in the company forms provided in the Commercial Code.

While specific provisions in the Commercial Code could be slightly modernized, these forms are adequate for the formation of private companies. Until the 1940s, the Code provided a functioning framework for companies. The market within which the Code operated, however, differed from contemporary market conditions. For example, no strict rules were seen as necessary for limited liability companies at that time because they tended to be smaller, family-type businesses that were self-regulated through personal relationships between partners with personal stakes in the business.

As the western market economies developed and more economic actors entered into the marketplace through widespread ownership of shares, their company laws developed accordingly in an effort to protect new classes. Indeed, the development of most company law reflects the constant shifting of protection to and from such various interests as the company, its employees or managers, its creditors, the investing public, or the national economic interests. Poland, however, has not yet experienced this economic evolution, and its company law has therefore not developed as the company laws of

⁴¹ These restrictions include a lack of necessary permits and prohibitive taxation.

⁴² *Ustawa o przedsiębiorstwach państwowych* [Law on State Enterprises], *amended by Official Gazette*, Issue No. 35 (1987).

⁴³ *Ustawa o spółkach z udziałem kapitału zagranicznego* [1986 Foreign Investment Law], *Official Gazette*, Issue No. 17 (1986).

⁴⁴ *Ustawa o działalności gospodarczej z udziałem podmiotów zagranicznych* [1988 Foreign Investment Law], art. 9, *Official Gazette*, Issue No. 41 (1988), *amended by Official Gazette*, Issue No. 74 (1989), *translated in 2 CENTRAL AND EASTERN EUROPEAN LEGAL MATERIALS* (1990).

⁴⁵ *Ustawa o spółkach z udziałem zagranicznym* [Foreign Investment Law], *Official Gazette*, Issue No. 60 item 253 (1991).

Western market economies have. The coming years should witness the natural evolution of Polish company law as it seeks to protect newly emerging social and financial interests.

The two corporate forms allowed by the Commercial Code are the limited liability company ("LLC") and the joint stock company ("JSC").⁴⁶ The limited liability company is similar to the French S.A.R.L. (*société à responsabilité limitée*), the German GmbH (*Gesellschaft mit beschränkter Haftung*), and the private corporation in Anglo-American law. The joint stock company resembles the French S.A. (*société anonyme*), the German AG (*Aktiengesellschaft*), and the Anglo-American public corporation. As noted in more detail below, there is relatively little difference between the two (less than between the two analogous forms in other market economies). The LLC is the preferred form for most investors, because it is more flexible and less cumbersome bureaucratically. In addition to these two corporate forms, businesses can operate through one of three partnership forms, the Registered Partnership, the Limited Partnership (both governed by the Commercial Code),⁴⁷ or the Civil Partnership (governed by the Civil Code).⁴⁸

A. Characteristics of a Joint Stock Company

1. Capital and Disclosure Requirements

As mentioned above, the Polish joint stock company resembles most closely the French S.A. At least three founders are necessary, unless the State is a founder, in which case no co-founders are necessary.⁴⁹ Minimum capital of 1 billion zlotys (about U.S. \$87,000) is required.⁵⁰ This may include the value of in-kind contributions, which are evaluated by private auditors and confirmed by court appointed experts.⁵¹ Valuation of assets in all the eastern European countries has been a great problem in privatization, and the same

⁴⁶ Commercial Code, *supra* note 34, at arts. 158-497.

⁴⁷ *Id.* at arts. 75-142.

⁴⁸ Civil Code, *supra* note 8, at arts. 860-75.

⁴⁹ Commercial Code, *supra* note 34, at art. 308.

⁵⁰ *Id.* at art. 311. Although all shares must be issued, not all capital must be paid up-front. Only 25 percent of the value of registered shares must be paid in. This is considered an advantage over the limited liability form, for which all capital must be paid up-front.

⁵¹ Commercial Code, *supra* note 34, at arts. 311-313.

problems could prevail in valuation for the purposes of determining a company's initial capital.⁵²

The Commercial Code's provisions on the joint stock company incorporate the principles of transparency common to western corporation statutes. These principles are designed to insure that potential and actual shareholders and creditors have sufficient information to make efficient investment decisions and exert control on corporate governance. Disclosure requirements make financial data on companies available at both the court of registration and the Ministry of Industry and Trade.⁵³ Announcements of public subscriptions, including investor information, are mandatory.

2. *Rights and Duties of Shareholders*

Both registered and bearer shares are allowed, and these are exchangeable for one another unless otherwise stipulated in the articles of association.⁵⁴ Shares are transferable, but the articles of association may stipulate that registered shares may be transferred only with permission of the company (i.e. the Board of Directors) or place other restrictions on the transfer of shares.⁵⁵ However, if the articles of association do not provide a mechanism for identifying another purchaser, the seller may sell his shares freely.⁵⁶

Shareholders are entitled to dividends and to a return of the company's assets in the event of liquidation. However, interest bearing shares are not allowed.⁵⁷ This distinguishes Poland's law from that

⁵² If the court appointed regulators determine a value that is at least 20% lower than that declared by the founder, then subscribers are free to renounce their part in the company. *Id.* at art. 325.

⁵³ See generally *id.* at arts. 307-38.

⁵⁴ Bearer shares may only be issued upon full payment. One who pays only a part of the purchase price obtains certificates entitling the holder to the shares upon paying the balance. Registered shares may be purchased for partial payment. They may also be issued in exchange for the duty of repeated non-monetary contributions, but only with consent of the company. *Id.* at arts. 346-47.

⁵⁵ *Id.* at art. 348.

⁵⁶ *Id.* This provision allowing the company to restrict the transfer of registered shares removes the characteristic distinction between the joint stock company and the limited liability company known to the French system. Under French law, only LLC may condition the transfer of the company's shares on the consent of either the shareholders or the Board of Directors (i.e. the shares are "saleable"). In contrast, the shares in a JSC are freely negotiable, meaning no permission is necessary to sell these shares.

⁵⁷ Commercial Code, *supra* note 34, at art. 354.

of Hungary, which allows for the issuance of interest bearing shares.⁵⁸ Interest bearing shares require the company to pay interest on the shares, regardless of how much company profit is earned. With ownership comes risk, and interest bearing shares are an attempt to create ownership without its attendant risk. Yet interest bearing shares might prove useful in countries trying to encourage private ownership of companies by an inexperienced and risk averse population.

A share entitles its holder to at least one vote at the appropriate meetings. There are no non-voting shares, although "a company's articles may restrict the voting power of shareholders holding a larger number of shares."⁵⁹ Certain shares may be assigned preferences with regard to voting rights, dividends, or claims on assets in the event of dissolution, with terms to be defined by the company's articles of association.⁶⁰ Also, certain registered shares, which may be transferred only with the company's consent, may be linked to the obligation of repeated non-pecuniary performance for the benefit of the company.⁶¹ These provisions that differentiate the rights and obligations of various shareholders enable control to be concentrated more than ownership, which may be helpful in addressing the Polish desire for widespread ownership of privatized companies while maintaining strong corporate governance.

B. Characteristics of a Limited Liability Company

Although not fundamentally different in concept, the Polish limited liability company is a more flexible form than the joint stock company and is therefore preferred by most domestic and foreign investors. Only one founder is necessary.⁶² The minimum capital requirement is only 10 million zlotys (about U.S. \$3,500).⁶³ Shareholders are free to negotiate how profits will be distributed, how voting rights will be assigned and exercised, how large the majority vote and quorum must be to validate the shareholders' general meetings, and how rights to choose representatives on the supervisory and management boards

⁵⁸ In both Hungary and Czechoslovakia, interest-bearing shares may not exceed 10 percent of the company's share capital. See Act VI of 1988 on Economic Associations, sec. 245, translated in INFO. SERV., HUNGARIAN CHAMBER OF COMMERCE, ECONOMIC INFO., SPEC. ED. (1989); Maher S. Mahmassani, *The Legal Framework for Investment in Czechoslovakia*, 6 ICSID REV. 65, 72 (1991).

⁵⁹ Commercial Code, *supra* note 34, at art. 404.

⁶⁰ One share may be assigned no more than five votes. *Id.* at art. 358.

⁶¹ *Id.* at art. 361.

⁶² *Id.* at art. 158(1).

⁶³ *Id.* at art. 159(2).

will be allocated. A partner's share is transferable by statute, although the law permits the company's articles of association to make transferability contingent upon the consent of the company's board or shareholders. If consent is refused, the requesting party may appeal to the court of registration.⁶⁴ This flexibility allows partners to a joint venture to arrange a balance of power reflecting their perceived real contribution to the company rather than merely the distribution of shares.⁶⁵

That permission may be required to transfer one's shares in a limited liability company, a provision common to analogous company forms in other market economies, reflects the nature of that company. Limited liability companies in most market economies tend to be smaller, closed companies, for example, family concerns. Permission to transfer shares is a way of controlling ownership, which the participants desire because shareholders are expected to take an active part in the affairs of the company, while passive shareholders are not expected to invest. Because those involved in a limited liability company are small in number and expected to communicate, given their close interest in the company, the legal requirements of the limited liability company are fewer (e.g. there are less strict reporting requirements and lower capital requirements). Since the investing public at large is not at risk, the state has less of an interest in regulating the company's activities.

The Polish Commercial Code places no maximum limit on the number of people who may constitute a limited liability company. This diminishes the difference between the limited liability company and the joint stock company in Poland. Whereas in most industrialized countries limited liability companies must automatically transform to

⁶⁴ *Id.* at art. 181(3).

⁶⁵ An example of the importance of this flexibility can be seen in recent negotiations between the Polish Post Telegraph and Telephone ("PPTT") and two foreign investors to create a joint venture to build and operate a cellular telephone system in Poland. Polish telecommunications regulations required that PPTT maintain majority ownership of the venture, yet the foreign partners—providers of both the capital and the technology for the venture—wanted to have *de facto* control over the decisions of the company. The parties negotiated an arrangement that (a) gave PPTT 51 percent ownership of the shares in the company but (b) gave the foreign investors the right to choose a majority of the members of the supervisory and management boards and (c) increased the threshold for the quorum and majority vote needed to validate the shareholder's general meeting from 51 to 60 percent. This arrangement is not yet final, and has not yet been approved by the court of registration.

joint stock companies after reaching a certain membership (for example, forty-nine in France), the Polish law appears not to set such a restriction. This most likely reflects the period in which the Code was drafted, when the need to regulate growing companies was not yet felt.

In sum, the limited liability form imposes less rigorous requirements on shareholders than the joint stock form. Its minimum capital requirement is lower, although all must be paid up-front, and the procedures for evaluating contributions and making decisions on corporate governance are less strict than that for a joint stock company. Since the limited liability form of the company is favored by both domestic and foreign investors, it is likely to remain predominant for some time.

C. *Characteristics of the Three Forms of Partnerships*

The three partnership forms currently in use are the Registered Partnership, the Limited Partnership, and the Civil Partnership. The first two are more flexible than the last and are better suited to larger initiatives where partners' contributions, rights, and responsibilities are not necessarily equal.

The Registered Partnership, governed by Section IX of the Commercial Code,⁶⁶ is a general partnership form imposing unlimited ("joint and several") liability on all partners.⁶⁷ Partners are free to assign management responsibilities and to define their respective shares in profits and losses through a deed of partnership, but this deed cannot assign management responsibilities to third parties to the exclusion of partners, and it cannot limit any partner's access to information about the partnership.⁶⁸

The Limited Partnership is a very recent addition to the Commercial Code, passed by the Parliament on August 31, 1991.⁶⁹ Unless the articles of association provide otherwise, this partnership form imposes unlimited liability only on the general partners, who are responsible for management and for forming the Board of Directors.⁷⁰ The other partners are passive and their liability is limited to their capital contribution, unless otherwise provided in the articles.⁷¹ For-

⁶⁶ Commercial Code, *supra* note 34, at arts. 75-142.

⁶⁷ *Id.* at art. 85(1).

⁶⁸ *Id.* at art. 91.

⁶⁹ Official Gazette, Issue No. 94 (1991).

⁷⁰ Commercial Code, *supra* note 34, at art. 155.

⁷¹ *Id.* at art. 156.

eign investors will continue to be restricted in their direct investment to limited liability companies and joint stock companies by virtue of the Foreign Investment Act, but the Polish companies in which they invest should be free to create limited partnerships.⁷² Perhaps the greatest advantage of the limited partnership is the combination of limited liability with pass-through tax treatment.⁷³ While this feature is common in western countries, Poland's adoption of this tax treatment is unique in eastern Europe.

The Civil Partnership is governed by title XXXI of the Civil Code of 1964⁷⁴ and is a less flexible form intended to cover simple initiatives among a few equally involved individuals. It is defined as a contract, as evidenced by a "deed of partnership," between two or more persons who bind themselves to attain a common economic objective.⁷⁵ Each partner may contribute property, rights, or services to the partnership. The partners' contributions are presumed to be of equal value, and the partners are entitled to share equally in both the company's profits and its losses.⁷⁶

The main benefit of this form over no company form at all is that it protects the common property of the group from outside encroachment by third parties. Jointly held property is not divisible among the partners for the life of the partnership, and a partner may not sell his share.⁷⁷ Furthermore, jointly held property may not be used to satisfy a creditor's claims against an individual partner,⁷⁸ although a creditor may seek the dissolution of the partnership in order to gain access to a partner's share.⁷⁹ A partner may withdraw from the partnership and recover his original contribution in kind, or its cash value, plus an appropriate portion of the partnership's accrued profits.⁸⁰ As with the Registered Partnership, partners are jointly and severally liable for the obligations of the partnership.⁸¹

⁷² Cole Corette & Abrutyn, Briefing Paper 1991-8, at 3-4 (Nov. 7, 1991) (on file with author at 110 Vermont Avenue, N.W., Washington, D.C. 20005).

⁷³ Pass-through tax treatment means that the partnership is not taxed as an entity. Only the partners are taxed as individuals on their respective shares of partnership income.

⁷⁴ Civil Code, *supra* note 8, at arts. 860-75.

⁷⁵ *Id.* at art. 860.

⁷⁶ *Id.* at art. 867.

⁷⁷ *Id.* at art. 863(1-2).

⁷⁸ *Id.* at art. 863(3).

⁷⁹ *Id.* at art. 870.

⁸⁰ *Id.* at art. 871.

⁸¹ *Id.* at art. 864.

Partners are expected to be active, each being entitled and bound to manage the partnership's affairs.⁸²

D. Procedures for Establishing a Company

While the basic framework for company law appears reasonable and admirably flexible, the process of establishing a private company in Poland continues to require significant time and expense, although simplified greatly in recent years. Future reforms in the area of company law should in particular address the role of notaries and procedures in the Court of Registration. The following steps are currently required to open a private corporation in Poland.

1. The Articles of Association

When establishing a company in either the joint stock or limited liability form, the founder must first draft the articles of association. The articles of association state the company's name and founders, define its object, and set out the specifics of its stock capital (i.e. number, classes, and nominal values of shares).⁸³ Previously, companies with foreign participation had to seek approval from the Foreign Investment Agency, whose application included a number of documents informing the Agency of the legal and financial status of the foreign partner. Now, however, with the passing of the new Foreign Investment Act of June 14, 1991,⁸⁴ approval is no longer necessary.⁸⁵

2. Notary Approval and Stamp Fees

Once the articles of association are drafted, they must be approved by a notary. Unlike those of common law systems, civil law notaries take a much more active role in approving official documents. A limited number of notaries have enjoyed a de facto monopoly in the market. They are difficult to find and there is little room for choice among them. Until recently all notaries were state employees. The profession is now being privatized and opened to entry. Because Polish notaries have little experience in contemporary corporate forms, they may not understand complex or innovative arrangements, and Polish lawyers report that articles of association must sometimes be

⁸² *Id.* at art. 865(1).

⁸³ Commercial Code, *supra* note 34, at arts. 309 and 162, respectively.

⁸⁴ Foreign Investment Law, *supra* note 45. See discussion *infra* notes 91-105 and accompanying text.

⁸⁵ See *infra* notes 92-114 and accompanying text.

simplified in order for the notary to understand them. Notaries often offer advice on the articles' content or have difficulty understanding innovative arrangements. Getting notary approval is reported to be at times a time consuming and frustrating process.

Notary approval is also quite expensive. Notarial fees must be paid for every notarial act involved in the founding of a company. Notarial acts include approving a company's articles of association and subsequent amendments to them, including increases in capital. Notarial fees equal 3% of equity capital up to 250 million zlotys, plus .01% of the equity capital over 250 million.⁸⁶

Stamp duties are another cost in starting a company. These are equivalent to the French *droits d'enregistrement* (registration fees). Stamp duties equal 2% of the company's equity up to 50 million zlotys, plus 1% of the amount from 50-100 million, plus .5% of the amount from 100-200 million, plus .1% of the sum exceeding 200 million zlotys.⁸⁷

It is widely agreed that these fees are unnecessarily high and encourage firms to incorporate with minimum capital. Furthermore, they discourage modifications of a company's articles of association. Locating a notary is itself often difficult and the approval process takes days or weeks.

3. Registration

After the articles of association have been notarized, the company must file at the Court of Registration.⁸⁸ Registration gives the company legal personality. This application for registration must include the articles of association as well as the identities of the members of the governing bodies.⁸⁹ If the initial capital was raised by public subscription, the application must also include the minutes of the organizational meeting, as well as the list of subscribers and their contributions and shares held.⁹⁰

Currently the greatest difficulty with the Court of Registration is its backlog. Although judges are seen as competent, the court is slow due to lack of modern equipment and well-trained staff. Having

⁸⁶ These fees are set out in Regulation of the Ministry of Justice, Official Gazette, Issue No. 60 (1989), *amended by* Official Gazette, Issue No. 46 (1990).

⁸⁷ Regulation of the Minister of Finance, Official Gazette, Issue No. 9 (1989), *amended by* Official Gazette, Issue No. 12 (1990).

⁸⁸ *See generally* Commercial Code, *supra* note 34, at arts. 13-16.

⁸⁹ *Id.* at art. 331(1).

⁹⁰ *Id.* at art. 331(2-3).

“connections” within the court is said to expedite approval and registration.

4. *The Shareholders' Agreement*

The shareholders' agreement, if there is to be one, must also be drafted during this period.⁹¹ Included with this can be the *regulamin*, or rules governing the supervisory board. As noted earlier, the current Commercial Code leaves parties great freedom to negotiate the terms of these contracts. As a practical matter, however, shareholders' agreements are said to be better left short and precise (20 pages or less), as Polish partners are believed by some lawyers interviewed to harbor a general suspicion for long and complex documents, particularly where foreign investors are involved. Because the shareholders' agreement is a private contract among individuals, it is governed by the Civil Code rather than the Commercial Code, although it may not abrogate mandatory provisions of the Commercial Code. Although shareholder agreements are meant to fill in gaps left open by the codes, short shareholders' agreements may leave some issues unresolved, increasing the potential for future disputes and litigation.

5. *Summary*

The general legal framework set out in the Commercial Code does not in itself restrict the development of the private sector. Refinement of the registration procedure and a reduction of accompanying fees would certainly facilitate the registration of companies, but these concerns should be subordinate to other areas discussed in this paper, which are in greater need of attention.

IV. FOREIGN INVESTMENT LAW

A new Law on Foreign Investment was promulgated on June 14, 1991.⁹² This law establishes the procedures and conditions for forming and operating a joint venture with foreign parties within Poland. It abolishes some of the administrative barriers to foreign investment contained in the former law.⁹³ This is not the only law affecting

⁹¹ Shareholders agreements are a normal feature of business organization in common law jurisdictions, but have not been typical in civil law jurisdictions. They are becoming more common in Poland with increasing foreign investment. They create greater clarity and certainty for shareholders than is possible under articles of association alone.

⁹² Foreign Investment Law, *supra* note 45.

⁹³ See 1988 Foreign Investment Law, *supra* note 44.

foreign investment, and some important related provisions are included in other laws—including Foreign Exchange Regulations,⁹⁴ the Land Use and Expropriation Act,⁹⁵ sector-specific laws such as the Banking,⁹⁶ Insurance,⁹⁷ and Telecommunications Laws,⁹⁸ and the Law on Acquisition of Real Property by Foreigners.⁹⁹

A. *Form and Ownership*

The foreign investment law applies to investment by non-resident legal or natural persons, including Polish nationals.¹⁰⁰ Foreign persons (non-residents) may participate only in companies established in Poland, although they may own up to 100 percent of the shares of such a company.¹⁰¹ Branches of foreign companies are not permitted under this law, although a separate law regulating foreign branches is expected to be passed in the future. Independent personal services are not explicitly forbidden, but they are not covered by the law and do not enjoy the related protections and benefits.

B. *The Approval Process*

One of the most important changes introduced in the new law is the abolition of a separate Foreign Investment Agency and the resulting downsizing and streamlining of the approval process. A smaller office will instead exist in the Ministry of Ownership Changes engaged mainly in promotional activities.¹⁰² The authority of government to

⁹⁴ Prawo Dewizowe [Foreign Exchange Law], Official Gazette, Issue No. 6 Item 33 (1989), *amended by* Official Gazette, Issue No. 74 Item 441 (1989).

⁹⁵ Land Use and Expropriation Act, *supra* note 7.

⁹⁶ Prawo Bankowe [Banking Law], Official Gazette, Issue No. 4 (1989), *amended by* Official Gazette, Issue No. 74 (1989).

⁹⁷ Ustawa o dzia alności ubezpieczeniowej [Insurance Law], Official Gazette, Issue No. 59 (1990).

⁹⁸ Ustawa o ężności [Telecommunications Law], Official Gazette, Issue No. 86 Item 504 (1990), *amended by* Official Gazette, Issue No. 69 Item 293 (1991).

⁹⁹ Ustawa o nabywaniu nieruchomości przez cudzoziemców [Law on Purchasing Real Property by Foreigners], Official Gazette, Issue No. 24 Item 202 (1933), *amended by* Official Gazette, Issue No. 41 (1988), *amended by* Official Gazette, Issue No. 79 Item 466.

¹⁰⁰ This may cause some problems, as according to the Constitution all Polish nationals are to be equally treated. New Constitution, *supra* note 16, at art. 67(2). On the other hand, some Polish nationals may claim they reside abroad in order to qualify for some of the incentives provided.

¹⁰¹ The Foreign Investment Law does not explicitly provide for this, however, because no limitation on foreign ownership is set forth. Since no domestic participation is required, it seems such companies may be 100% foreign owned.

¹⁰² The Foreign Investment Law also abolishes several administrative requirements, such as the evaluation of feasibility studies. *See* Foreign Investment Law, *supra* note 45.

screen and approve foreign investment is restricted to a small pre-defined list of "strategic" areas.¹⁰³

Joint ventures with public enterprises will continue to require government approval.¹⁰⁴ Required permission may contain conditions for the establishment of the enterprise, such as the ratio of foreign to Polish participation or the ratio of voting rights, depending on the subject of activity of the company. As formulated, the law requires the prior consent of the Ministry of Ownership Changes for a company to diversify its activities.¹⁰⁵ Furthermore, joint ventures with newly privatizing enterprises situated on public land will need to deal with the government to acquire land rights, and purchases of land by majority foreign owned firms require the approval of the Minister of Internal Affairs.¹⁰⁶ Even if land is not purchased, leasing business premises from the state is itself a cumbersome process. In effect this means that many joint ventures (i.e. all those with state owned enterprises or on state owned land) will continue to require government screening and approval. It is unclear to what extent managers of small public enterprises will be allowed to independently negotiate and carry out joint ventures with foreign partners. If extensive foreign investment is desired, the screening process will need to be cursory for smaller projects and serious only for the more significant ones to avoid the re-creation of a large approval body.

In sum, formally unrestricted foreign investment is in reality only possible for 100 percent foreign owned companies or ventures with private Polish partners that do not lease or own real property. While the Polish private sector is a growing part of the economy in trade and services, its role in industrial manufacturing is still very small. Furthermore, access to real property is a problem for both domestic and foreign private firms, and in-depth negotiations with government over real property rights will still be required of all investors for some time to come.¹⁰⁷

¹⁰³ Foreign Investment Law, *supra* note 45, at art. 4. These include: sea and airports, real estate, defense industries, wholesale trading in imported consumer goods, and legal services. *Id.*

¹⁰⁴ Though it uses the term, the law does not specifically define "state enterprise"; most assume that this is an enterprise with more than 50% state participation. Even the Law on State Enterprises does not define the term.

¹⁰⁵ Foreign Investment Law, *supra* note 45, at art. 19.

¹⁰⁶ See Law on Purchasing Real Property by Foreigners, *supra* note 99, at art. 1.

¹⁰⁷ See *supra* discussion at part IB5, *Controls on Use of Real Property*.

C. Profit Repatriation

The previous law limited profit repatriation to fifteen percent of profits except where the firm generated sufficient net foreign exchange earnings to cover the desired repatriation. The new law allows unrestricted repatriation of all profits,¹⁰⁸ a very important change to most foreign investors. Another uncertain area under the old law was the transfer abroad of capital gains. The new law's wording suggests that no restrictions are imposed on the transfer of shares inside Poland and the subsequent repatriation of the proceeds as long as the company is not liquidated during the period of tax incentives or within two years afterwards.¹⁰⁹

D. Tax Incentives

The 1988 Foreign Investment law provided for three-year tax holidays, which could be extended up to three more years by the Minister of Finance upon request.¹¹⁰ The new law also provides tax incentives for foreign investors, but with greater limitations. A tax credit may be granted by the Minister of Finance to a company that (a) has a foreign capital contribution of at least 2,000,000 ECU (expressed in zlotys) and (b) operates in regions with high unemployment, is engaged in high technology activities, or exports at least 20 percent of its production.¹¹¹ However, the definition of the tax credit to be provided is not clearly formulated, and there are varying opinions on what it means in practice.

The translation of Article 23(6) is approximately as follows: "The amount of exemption from income tax [i.e. the tax credit] may not exceed the value of stock or shares acquired by foreign persons."¹¹² This provision may have one of two interpretations: either the *total* amount of the company's tax credit may not exceed the initial capital contributed by the foreign partner, or the *proportion* of the total tax that may be credited in any one year may not exceed the proportion of total capital contributed by the foreign partner. Under the first interpretation, which is most likely correct, no time limit on the credit is needed, and the credit may presumably be used immediately or over several years. Under the second, there is a need for some time

¹⁰⁸ Foreign Investment Law, *supra* note 45, at art. 25.

¹⁰⁹ *Id.* at arts. 24-26.

¹¹⁰ 1988 Foreign Investment Law, *supra* note 44, at art 28.

¹¹¹ Foreign Investment Law, *supra* note 45, at art. 23.

¹¹² *Id.*

limit unless the Poles intend the credit to be available indefinitely.¹¹³ No time limit is specified in the present law, although some experts apply this interpretation and assume a three year limit, as existed under the previous law. In either case, the tax incentives will be difficult to administer and oversee, given the limited capacity of Polish tax administration.

Such a system of specialized tax reliefs will continue to cause distortions and provide incentives for tax evasion and avoidance. It can also lead to political problems because it favors foreign over domestic investment. The experience of other countries, including Bulgaria and Hungary as well as many developing countries around the world, should be considered in weighing whether the uncertain benefits gained by tax incentive schemes outweigh the obvious resulting loss of revenue and efficiency.

E. Dispute Resolution Between Investors and the State

Although disputes arising under the Foreign Investment Law can be brought in Polish courts under Polish law, this avenue is unlikely to give confidence to most foreign investors. Poland does not accede to the ICSID Convention.¹¹⁴ However, mechanisms for the settlement of disputes between foreign investors and the government are established in a number of bilateral treaties, including treaties with virtually all major capital exporting countries.

In sum, the new foreign investment law is an important step forward in removing some of the legal and administrative barriers for foreign direct investment. This step needs to be supported by similar progress in privatization, real property, and tax law, and through institutional strengthening throughout the legal system.

V. CONTRACT LAW

Polish contract law is embedded in the Polish Civil Code of 1964.¹¹⁵ This Code was significantly amended in July, 1990. Presently, a reform commission composed of judges, lawyers, and professors is considering further changes.

¹¹³ This would amount to a perpetual tax holiday for 100-percent foreign-owned firms.

¹¹⁴ Convention on the Settlement of Investment Disputes between States and Nationals of Other States, March 18, 1965, 17 U.S.T. 1270, 575 U.N.T.S. 159 [hereinafter ICSID Convention].

¹¹⁵ Civil Code, *supra* note 8.

A. Origins of the 1964 Civil Code

Divided and annexed by Prussia, Austria, and Russia in the eighteenth century, an independent Poland re-emerged following the First World War. Civil law at the time of re-emergence reflected a complex mix of foreign laws. The Poles responded with a codification movement designed to unify Polish law. Of relevance to contract law were the 1933 Code of Obligations and two 1936 Acts on negotiable instruments, one governing bills of exchange and the other regulating checks.¹¹⁶ This codification movement resulted in a contract regime patterned after German and French models. The law was western, complete with doctrines of offer and acceptance, rules of fraud, duress, and undue influence, and a statute of frauds.

Under the post-World War II political structure, existing contract law remained in force except where it was inconsistent with socialist principles. Initially, most of Poland's contract law and law of negotiable instruments remained intact. Socialist conceptions of property and the practice of central planning, however, soon required changes in the civil law. From 1945 to 1964 the promulgation of individual acts and decrees created adaptations to the 1933 Code of Obligations. The 1964 Civil Code attempted to collect and unify these adaptations.

The 1964 Civil Code reflected a mature system of contract law under socialism. This Code maintained many of the provisions found in the 1933 Code but tacked on a variety of socialist adaptations. The amendments of July 1990 reversed this evolution to recreate a civil law attuned to the market rules of the early 1930s.

B. Central Features of Socialist Contract Law in Poland

Three central features distinguish the Polish contract law of the past twenty-five years from that in western market economies: (1) the presence of central planning and the corresponding distinction between contracts between state enterprises and contracts between private individuals; (2) the socialist conception of property, including the limitations on private ownership and the preferences afforded to state property; and (3) the socialist ideology embodied in the constitutional principle of social co-existence.

1. Central Planning

A principal feature of the 1964 Polish Civil Code was the distinction between contracts among private persons (and contracts between state

¹¹⁶ Prawo czekowe [Law on Checks], Official Gazette, Issue No. 37 (1936); Prawo wekslowe [Law on Bills of Exchange], Official Gazette, Issue No. 37 (1936).

enterprises and private persons) versus contracts between state enterprises. With regard to the former law of the 1930s¹¹⁷ remained intact. Within the realm of activity afforded private persons in the socialist system, parties engaged in contractual conduct in ways similar to those found in western market economies. By contrast, contracting between state enterprises reflected the needs of central planning. The "General Conditions of Sale or Delivery" governed state enterprise contracts in detail, and through that plan the state had extensive control over whether commercial entities entered into contracts, with whom they contracted, and what conditions would be contained in their contracts. The Civil Code¹¹⁸ established the possibility of "pre-contractual liability" for state enterprises, a legal duty for enterprises to enter into contracts in accordance with state plans. Failure to accept a contract offer in harmony with a state target could result in liability.¹¹⁹ Similarly, failure to create an offer in a timely fashion could also lead to damages.¹²⁰ In addition, once a contract was executed between state enterprises, each party became a fiduciary for the interests of the other.¹²¹ Article 2 provided administrative organs with the authority to suspend the operation of the Code, and hence authorized administrative adjustment of contractual terms. Article 386 imposed a duty on all parties to cooperate with such adjustments. Contractual disputes between state enterprises were to be resolved pursuant to a system of state arbitration, not in the courts.¹²²

Recent reforms have largely removed the legal distinction between contracts between individuals and contracts between state enterprises. First, Article 2, which grants administrative authority to suspend the operation of the Code, has been repealed. All contracts, whether between state enterprises or between private parties, are now governed by the Civil Code. In addition, in 1989 the system of state arbitration was dismantled, and all contractual disputes are now heard by the judiciary.¹²³ Finally, the system of pre-contractual liability, while still

¹¹⁷ E.g. the 1933 Code of Obligations and the Laws on Checks and Bills of Exchange, *see supra* note 116.

¹¹⁸ *See generally* Civil Code, *supra* note 8, at arts. 397-404.

¹¹⁹ *Id.* at art. 397.

¹²⁰ *Id.* at art. 384.

¹²¹ *Id.* at art. 355.

¹²² *Id.* at art. 398.

¹²³ This was achieved by amending the Kodeks Postępowania Cywilnego [Code of Civil Procedure], Official Gazette, Issue No. 43 (1964), *amended by* Official Gazette, Issue No. 55 (1990).

nominally on the books, is quickly becoming obsolete given the abolition of central planning.

The first goal of the 1990 amendments was to provide a system of contract law which could be uniformly applied to any type of transaction. This has been largely achieved.

2. *The Socialist Conception of Property*

As noted earlier in the discussion of real property law, the Civil Code¹²⁴ provided for various types of property—social, individual or private, and personal. Administrative regulations strictly limited the subject matter of private market activities and thus profoundly affected the content and reach of contract law. Market based contract principles were allowed to apply only in the sphere of petty trade for goods under personal or private ownership, and even there price or other government controls often limited the parties' freedom to contract.¹²⁵ In major commercial transactions, the contract principles associated with central planning were in effect. This strictly limited the Polish experience with the complexities of privately structured contractual relations. Furthermore, the state had certain legal privileges in contracting. For example, state claims were not subject to any statute of limitations, which gave the state distinct advantages in the settlement of claims.

As noted earlier, the July 1990 reforms changed this property scheme, repealing Articles 126 through 135. Today there are two basic types of property—property held by the state, including that held by public enterprises, and private property. The formal preference for state property has been eliminated, and there is no longer a limitation on the private ownership of property. The second goal of the 1990 amendments was to provide a uniform contract system for all types of property. This, too, has largely been achieved.

3. *The Principle of Social Co-existence*

Changing socio-economic practice in the 1950s demonstrated the need for a more flexible enforcement of Civil Law rules in the interest of equity. In addition, socialist ideology seemed to call for a new set of equitable or moral principles to guide business conduct. The

¹²⁴ See generally Civil Code, *supra* note 8, at arts. 126-35.

¹²⁵ See generally Gyula Eorsi, *Contract in the Socialist Economy*, in VII INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW ch. 5 at 3 (Arthur von Mehren ed., 1981).

Poles responded to these practical and ideological needs by introducing the principle of "social co-existence" into the Civil Code. Article 5 provided: "A right cannot be used in a way which would be in contradiction with the socio-economic purpose of that right or with the principles of social co-existence in the Polish People's Republic."¹²⁶ This section was used as a check on excessive use of individual rights and created the opportunity to introduce moral standards into contractual conduct. Article 4 operated in a similar fashion. It stated: "Civil law regulations should be interpreted and applied in accordance with the principles of the political system and the objectives of the Polish People's Republic."¹²⁷ Here the Code specifically provided for a political check on the substance of private civil agreements.

These articles have been widely used in judicial practice. For example, Article 4 has been used to protect long-term tenants from the harshness of eviction and to shield debtors against the demands to pay interest accumulated over long periods of time. Article 4 was repealed in 1990. Article 5, a variant of which appears in many civil codes around the world, remains in the Code.

C. *The Current Situation*

The Poles are in the process of crafting a set of contract laws appropriate to a market economy. They started with the existing Civil Code of 1964. Most sections were retained, several sections were deleted, other sections are to be added, while still other sections must be reinterpreted in the light of current necessity. Thus far, the amendment process has emphasized deletions. Additions to the Code and re-interpretations of retained sections are yet to come.

Most of the Civil Code does not need to be changed. Many of the core rules of contracting, such as rules of offer and acceptance or rules relating to performance, were fashioned in the 1933 Law of Obligations and remained in force throughout the decades of central planning. These sections, for the most part, reflect current western practice. Their exact meaning will be filled in over time through practice and judicial interpretation.

The major deletions taken to date, regarding central planning, property concepts, and socialist ideology, are highlighted above. Other deletions will follow. Since the majority of Polish property is still in state hands, some administrative rules regulating exchange of state

¹²⁶ Civil Code, *supra* note 8, at art. 5.

¹²⁷ *Id.* at art. 4.

property are still necessary. These should be phased out in time. The sections creating "pre-contractual" liability for state enterprises provide an example of a set of laws that are quickly becoming obsolete.

Additions to the Code are currently being considered by a group of scholars empaneled by the Ministry of Justice. This group has three areas of concern. First, the present Code does not provide standard terms for certain types of transactions found in industrialized countries. Rules regulating commercial leases, franchises, and factor leasing are conspicuously absent. The commission is considering such additions.¹²⁸ Second, the state of commercial law may be in need of reorganization. The Civil Code regulates sales¹²⁹ and pledges of personal property.¹³⁰ Another body of law regulates mortgages.¹³¹ Still another regulates negotiable instruments.¹³² There is some concern that these various sources of commercial law need to be unified or updated. Third, and perhaps most importantly, the Poles wish to harmonize their Civil Code with the laws and customs of the European Community and with the rules of various international conventions. The reform commission envisions a two year study in which these technical matters can be studied and changes made.

The most interesting changes in contract law may come in the form of re-interpretation of existing doctrine. For example, contracting under central planning officially embraced the principle of "freedom of contract," yet in practice there was in fact very little freedom. Contracts were set by the plan and were subject to the political needs of the state and the principle of social co-existence. Practice under a market system will bring new meaning to this principle. Similarly, reinterpretations are likely in most areas of private interaction.

The task of redrafting formal contract laws is highly complicated and technical. Yet, the problems associated with such a task pale in comparison to the difficulties of teaching an entire society to think in market terms. It will take time to change attitudes and build

¹²⁸ The existing Code is flexible enough, however, to permit these types of arrangements on a case-by-case basis. In fact, standard rules for these and other special types of contracts have been added to the French Civil Code over the years, but many appear to have fallen into relative disuse as lawyers find it preferable to craft individually tailored arrangements under the more general provisions of the Code.

¹²⁹ Civil Code, *supra* note 8, at arts. 535-95.

¹³⁰ *Id.* at arts. 306-35.

¹³¹ Prawo o księgach wieczystych i hipotece [Act on Mortgages], Official Gazette, Issue No. 19 (1982).

¹³² See Law on Checks and Law on Bills of Exchange, *supra* note 116.

knowledge, experience, and a body of legal interpretation, and thus create adequate certainty in the decentralized contracting process for a market to function effectively.

VI. BANKRUPTCY

Bankruptcy as practiced in market economies was unknown in centrally planned economies. Western-style bankruptcy procedures were not needed in a centrally planned system because of the absence of truly adversarial interests. Companies' creditors, whether banks or suppliers, were owned by the state, which also owned the debtor company and would thus arrange to settle financial disputes amicably as they arose, often through additional cash infusions for the debtors or creditors. Furthermore, no comparative law courses on bankruptcy were offered in the universities for 40 years, and thus the concept was virtually unknown to a generation of lawyers trained after the World War II.

A. *The Law of 1934*¹³³

The concept of bankruptcy was gradually reintroduced during the 1980s, but the provisions of the laws did not begin to be applied until very recently. In the Polish case, the relevant law is the Bankruptcy Act of 1934.¹³⁴ It was never formally abolished, but was dormant until three years ago and has been used recently only for closures of state owned enterprises, which is still not a true adversary situation. Western-style bankruptcy procedures will be needed as the private sector grows, with private suppliers and banks who face truly hard budget constraints and thus have a strong incentive to collect on bad debts. Conversely, an absence of efficient bankruptcy procedures and other debt collection mechanisms will inhibit the growth of the private sector.

The Polish law, as amended several times, most recently in 1990, appears reasonable in broad terms,¹³⁵ providing general procedures for both liquidation and reorganization under the control of a receiver

¹³³ Prawo upadłościowe [Bankruptcy Act], Official Gazette, Issue No. 93 (1934), amended by Official Gazette, Issue No. 14 (1990), translated in *The POLISH COMMERCIAL CODE*, *supra* note 34.

¹³⁴ *Id.*

¹³⁵ There may be problems in some of the detailed aspects of the law that are not included in this initial look. Further expert analysis of the current law would be useful.

appointed by the court.¹³⁶ Bankruptcy is overseen by a tribunal of the local court. Under the law, either the debtor or a company's creditors may initiate an investigation.¹³⁷ The initiator must prove that the company cannot pay its debts. There are no precise criteria for this standard of proof, although two weeks of nonpayment appears to be a minimum requirement.¹³⁸ The tribunal accepts the case only if the assets of the enterprise are sufficient to cover the procedural costs.¹³⁹ This establishes some barrier to legal action and helps to keep trivial cases from clogging the courts. If accepted, the tribunal appoints a judge-commissioner and an official receiver.¹⁴⁰ The receiver manages the company with the mandatory cooperation of the original managers, who lose their management rights,¹⁴¹ but may continue to be involved if deemed appropriate by the receiver and approved by the judge-commissioner.¹⁴² The receiver evaluates the company's assets and creditors' claims and proceeds to liquidate the company.¹⁴³ Liquidation can be avoided if the bankrupt company has reached an alternative agreement with creditors,¹⁴⁴ approved by the judge-com-

¹³⁶ A Law on the Procedure for Mutual Agreement was also passed in 1934 (Prawo o postępowaniu układowym, Official Gazette, Issue No. 93 (1934), amended by Official Gazette, Issue No. 55 (1990)) and is still on the books. This law, modeled after a 1927 German statute and similar to numerous other European precedents of the late 1800s and early 1900s, was meant to provide an alternative to bankruptcy and liquidation by promoting the amicable settlement of debts between an on-going company and its creditors. The procedure, which can be initiated *only* by the debtor, is very similar to that of bankruptcy, with (a) the appointment by the court of a judge, (b) the appointment by that judge of a trustee (under a different name), (c) the overseeing by that trustee of the operations of the company while the company prepares a plan to pay off its debts, and (d) the implementation of such plan if agreed to by two-thirds of the creditors (with some protection of the remaining minority from overly onerous terms). The main differences between this procedure and bankruptcy are that only the debtor can bring a mutual agreement case, and the trustee does not have the power to remove the management of the debtor company and take over the enterprise (but can terminate the case and in essence throw it into bankruptcy if the company does not comply with his wishes). It appears that this law (used often before the war) has remained dormant until now because of lack of knowledge of the public, although debtors may choose to use it in the future if it remains on the books because it is more favorable to them than bankruptcy.

¹³⁷ Bankruptcy Act, *supra* note 133, at art. 4.

¹³⁸ *Id.* at arts. 2 and 5.

¹³⁹ *Id.* at art. 13.

¹⁴⁰ *Id.* at art. 14.

¹⁴¹ *Id.* at art. 20.

¹⁴² *Id.* at art. 98.

¹⁴³ *Id.* at art. 110.

¹⁴⁴ *Id.*

missioner, regarding debt reduction, debt rescheduling, or reorganization of the company.¹⁴⁵ Thus, there appears to be a rudimentary framework for reorganization in lieu of liquidation, although it is not as well developed as in other market economies.

B. The Law in Practice

Despite its general reasonableness, it remains to be seen how this law will be applied, as very few bankruptcies have actually been carried out pursuant to it.¹⁴⁶ Practice is necessary to establish precedents and fill in more precise rules. Some observers fear the procedure is too complicated to handle the large number of liquidations anticipated in the coming years. As with antimonopoly law, it is important that decisions be publicized to provide guidance to potential creditors, to educate the public and the courts, and to provide an opportunity for debate over the emerging framework.

Court capacity and training is certain to be a bottleneck to the development of sound bankruptcy precedents and principles. The legal institutions are not prepared for the plethora of bankruptcy cases that may confront them. Courts and judges are not adequately trained for bankruptcy cases. No training in bankruptcy has been organized for the acting judges, and in the universities bankruptcy law is still developing and very theoretical. The law demands a special judge-commissary to be appointed for every case, which further reduces the already limited operational capabilities of the courts. While special economic courts have been established in Warsaw and some other big cities, the complicated bankruptcy procedures may overwhelm smaller generalized courts.

The availability of receivers is another serious problem. Specialized firms existed in the pre-war period, but the number of present experts is very limited. The law requires that receivers not be associated with the creditors in any way, and prohibits creditors from proposing to the court a specific receiver. In practice, however, this law is often violated.

Statistics on bankrupt companies are not yet compiled, nor are court rulings published, as was the pre-war practice. The Ministry of Justice is supposed to organize this, but the work is in its initial stage and apparently not coordinated with the courts.

¹⁴⁵ *Id.* at art. 20.

¹⁴⁶ We were told that thirty cases are now pending, and only two cases have been completed.

C. Related Concerns: Credit Rating Services and Rules on Collateral

Two broader problem areas related to bankruptcy are (1) creditors' access to information before extending credit, and (2) rules on collateral. The only publicly available information on a company's financial situation is its registration on file at the Court of Registration. This data is insufficient and unreliable, because only the company's initial capital is registered, and proof that this initial capital exists is not confirmed by the court at the time of registration. Credit rating services, a concept hardly known in Eastern Europe, are badly needed.

In the area of collateral, both real and movable property may be used as collateral, but only security interests in real property can be publicly registered, with the registration date determining creditor priority. The only workable means to secure a loan with personal property is to transfer title to the property while the debt is outstanding. A modern system for registering security interests in personal property would facilitate credit expansion and alternative means of satisfying claims in lieu of bankruptcy. This could include the "floating lien" on inventory and accounts receivable that is prevalent in common law jurisdictions but not generally recognized to date in civil law jurisdictions.

VII. ANTIMONOPOLY LAW

Clearly one of the biggest impediments to the Polish private sector is the dominant role of the public sector. Small private firms often deal only with public enterprises, who exert market power and may impose unfair or onerous conditions. For example, small private firms are often required to pay for all purchases in cash, while they must supply interest-free credit, in the form of delayed payment, to public enterprises that purchase their products. Privatizing public enterprises and insisting on competition in the market are essential for long-term growth of the private sector. Proper enforcement of competition law is important for private sector development. Low tariffs can themselves go a long way in promoting competition by importing world prices (adjusted for transport costs) as an effective ceiling on domestic prices, but they should be complemented by domestic laws against monopoly behavior.

The Polish Antimonopoly Act of 1990¹⁴⁷ provides a comprehensive framework for competition law and practice to develop. It establishes

¹⁴⁷ Ustawa o przeciwdziałaniu praktykom monopolistycznym [Antimonopoly Act],

broad principles concerning illegal behavior and it sets up a specialized Antimonopoly Office to prosecute cases, based on complaints filed by individual firms or companies, or on the office's own initiative, with the possibility of appeal to a special antimonopoly branch of the Warsaw district court, and then to the Supreme Court.

The law regulates both market structure and business conduct, and its definition of anticompetitive behavior is all-encompassing. It defines four types of "monopolistic practices": (1) onerous contract terms that yield unjustified benefits; (2) conditioning a contract on the performance by the other party of unrelated services it would not otherwise perform ("tie-ins"); (3) acquisition of shares or property of other companies, if it results in "major weakening of competition"; and (4) interlocking directorates or supervisory councils of more than one competing company if one controls more than 10 percent of the market.¹⁴⁸ Article 4(2) adds to this list (1) direct or indirect price fixing among competitors; (2) geographical or product specific market-division agreements among competitors; (3) restriction of output, sales, or procurement; (4) limiting market access of third parties ("group boycotts"); and (5) fixing the terms of contracts with third parties such as "resale price maintenance."¹⁴⁹ Article 5 defines "monopolistic" as the abuse of a dominant position, assumed to exist in Article 2(7) if market share exceeds 30 percent, and names several examples of such abuse, including market division, price discrimination, refusal to deal, resale price maintenance, and predatory pricing.¹⁵⁰ Article 7 forbids monopolies or firms with monopoly-like dominant positions from cutting output or suspending sales to increase prices, or from imposing "exorbitant prices."¹⁵¹

While the law is all-encompassing, it adopts a "rule of reason" approach in most cases, giving virtually unlimited discretion to the antimonopoly office to decide which cases to prosecute. Yet the wording implies that the named practices are *prima facie* illegal (i.e., if charged, the burden of proof lies with the company). Under Article 6, the practices defined in Articles 4 and 5 (i.e. "monopolistic practices" and "abuse of a dominant position") are prohibited "unless they are indispensable to the conduct of economic activity and do

Official Gazette, Issue No. 14 (1990), *translated in* JOINT PUBLICATION RESEARCH SERIES, E. EUR. REP. No. 90-115S, Aug. 13, 1990, at 68.

¹⁴⁸ *Id.* at art. 4(1).

¹⁴⁹ *Id.* at art. 4(2).

¹⁵⁰ *Id.* at art. 5.

¹⁵¹ *Id.* at art. 7.

not cause a significant curtailment of competition."¹⁵² The practices of actual monopolies listed in Article 7 are per se prohibited.¹⁵³

If any of these practices are ruled anticompetitive, the Antimonopoly Office has broad powers to order the abandonment of such practices, impose a monetary fine of up to fifteen percent of the offender's annual income in the previous year,¹⁵⁴ roll back prices, or even order the break-up or dissolution of violators with a dominant position.¹⁵⁵ It also has the authority to review all proposed mergers and acquisitions, with no minimum size limit. The law gives it broad powers of investigation in line with this broad mandate.¹⁵⁶

The problem with the law is inherent to the subject: even industrial countries have found it notoriously difficult to differentiate a restraint of trade that reduces efficiency from a legitimate business deal that raises efficiency in the short- or long-run. Sophisticated economic analysis in the United States and Europe shows that many vertical restraints—such as tying of sales, resale price maintenance, refusals to deal, and discriminatory pricing—may enhance efficiency under certain circumstances, typically when market structure is competitive and the firms imposing the restraints are not in a dominant position. As a result of this economic analysis, enforcement of U.S. antitrust law has softened in the 1980s, and the Department of Justice refuses to prosecute many cases it would have brought in earlier times. The OECD is also recommending that European jurisdictions relax their laws to look at each case on an individual basis (the "rule of reason" approach) rather than forbidding certain practices under all circumstances (the "per se" approach). Opponents of the rule of reason approach argue that businesses need certainty above all, and that the rule of reason approach leaves too much uncertainty as to what is permitted and what is not, and therefore inhibits business activity.

The Polish Antimonopoly Office is made up of some 100 economists/lawyers in the headquarters and eight regional offices. Because of the newness of this office, the enormous degree of change required in Polish industrial structure, and the complexity of antitrust analysis in general, the office is likely to make many questionable rulings in the early years. Yet rather than concentrate on legal changes, this

¹⁵² *Id.* at art. 6.

¹⁵³ *Id.* at art. 7.

¹⁵⁴ *Id.* at art. 14.

¹⁵⁵ *Id.* at art. 8.

¹⁵⁶ *Id.* at art. 9.

office could perhaps best be supported with training and funds to allow them to publicize their studies and rulings. Given the generality of the law, the rulings will define what the law actually is. Additionally, businesses should have access to this developing body of practice so that they can adapt their behavior accordingly, or challenge it if they believe it is inappropriate. In this way, the office could play an important role in educating the public and reducing uncertainty.

VIII. JUDICIAL INSTITUTIONS

It is one thing to have a western-style set of laws on the books, and quite another for those laws to be implemented predictably and efficiently. Habits of thought can be slow to change, and expertise develops only through practice. One suspects that Polish inexperience with complex market oriented legal matters may retard market advances. This inexperience is likely to surface in the judiciary, in the ministries, and in the business community itself.

A. *The Court System*

The structure of the Polish judiciary is similar to that in other continental European systems. The Polish Supreme Court, the highest court in the system, is composed of about one-hundred judges appointed by the Council of Ministers for five-year terms.¹⁵⁷ It is divided into several chambers: civil, administrative, social (labor and social insurance), criminal, and military. Each chamber is divided into specialized sections. The civil chamber deals with all private matters, both commercial and noncommercial, including property law, company law, bankruptcy, and family law. The Supreme Court's role is to review questions of law in final decisions of the general appellate courts and the High Administrative Court. Only certain high public officials, including the President of the Supreme Court, the Ombudsman, the Minister of Justice, and the General Prosecutor, can bring cases before the Supreme Court for review ("extraordinary revision"). Parties to the dispute cannot bring cases directly, but can petition these officials to bring the cases. Most cases are decided by panels composed of three judges.

Two types of courts are under the Supreme Court: courts of general jurisdiction and courts of special jurisdiction. The latter include the

¹⁵⁷ Hoon Chun, *The Legal System of Poland*, in 8 MOD. LEGAL SYS. CYCLOPEDIA 8.90, 8.90.16 (Kenneth Redden ed., 1991). Judges in lower courts have life tenure.

courts for military and social insurance matters, and the High Administrative Court.¹⁵⁸ All civil, commercial, social, and criminal cases are tried in general courts, which are either local or district—"voivodship"—courts, depending on the amount at issue or the nature of the charge, with right of appeal of both factual and legal issues to the relevant court of appeal.¹⁵⁹

In addition to these courts, a separate Constitutional Tribunal was established in 1985 to advise Parliament on the constitutionality of laws and to review government regulations to ensure that they comply with parliamentary acts.¹⁶⁰ Only certain high public officials can bring cases to this tribunal. Parliament has the final say over how to treat a decision of the tribunal regarding the constitutionality of a parliamentary act. The judiciary is subordinate to the Parliament (as is also the case in France), and does not have the power to declare statutes null and void (as is possible in countries with separation of powers and full fledged judicial review such as the United States). The Tribunal's decisions with regard to the legality of sub-statutory regulations are, in contrast, final and binding.

Although the court system has jurisdiction over the whole panoply of commercial matters likely to arise as Poland moves toward a private market system, it has limited competence in these areas. Until 1989, commercial disputes were resolved through state enterprise arbitration¹⁶¹ rather than in the courts. Over the past two years the role of the courts has expanded dramatically to include a whole range of commercial matters never before considered. Furthermore, most high-level judges are new. About eighty percent of the appellate level

¹⁵⁸ Leszek Garlicki, *Legal Profession in Poland*, 24 ST. LOUIS U. L.J. 486, 495 (1980).

¹⁵⁹ The district courts play the appellate role for the local courts, while several courts of appeal review decisions of the district courts.

¹⁶⁰ New Constitution, *supra* note 16, at art. 33(a). In contrast with Anglo-American models, European constitutional tribunals are typically separate from the courts of general jurisdiction and have exclusive jurisdiction in constitutional matters.

¹⁶¹ During the socialist period, state economic arbitration was the mechanism for settling disputes between state owned enterprises. This form of arbitration was centralized in the Chief Arbitration Commission, a hybrid institution embracing both judicial and administrative functions. This fact was reflected in its subordination to the Ministry of Finance, as opposed to the Ministry of Justice. In its judicial capacity, the Commission settled individual disputes. In its administrative capacity, the Commission had rights and duties to discover and remedy the cause of the dispute in an effort to insure fulfillment of the state economic plan. In this dual role, the Arbitration Commission was committed to socialist legality, or adherence to the state economic plan, which held the status of law.

judges have been replaced during the past two years in order to replace old ways with new thinking. Many of the newly appointed judges have been associated with the Solidarity movement for some time. Nonetheless, they lack experience with the various accounting, engineering, and economic problems associated with complex market transactions. Developing such expertise will take time.

The lack of experience and expertise in the court system creates uncertainty in the business community. Moreover, the cost of both money and time involved in the court system is a serious problem. In the case of commercial disputes, courts require the claimant to deposit with the court a sum equal to twelve percent of the disputed amount. This sum is supposed to be returned upon resolution of the case. This deposit does not earn interest, nor is the return of the sum, if the sum is indeed returned, adjusted for inflation. Since many cases continue for about two years, this deposit imposes a significant financial liability on plaintiffs.

B. Arbitration in Poland

In light of the problems attendant to the Polish court system, arbitration may be an attractive and efficient alternative form of resolving domestic commercial disputes.¹⁶² Moving toward arbitration away from litigation in effect "privatizes" dispute resolution itself, which can be highly desirable when government capacity is severely stretched, as in much of Central and Eastern Europe. Arbitration is already the preferred form of international dispute resolution, primarily because it provides participants with a neutral forum.¹⁶³ Do-

¹⁶² When discussing arbitration in Poland, it is important not to confuse ad hoc arbitration with state economic arbitration, the previous administrative mechanism by which disputes between state owned enterprises were resolved (now defunct). See *supra* note 161.

¹⁶³ Poland is a signatory to the following international conventions on arbitration:

(1) Protocol on Arbitration Clauses, Sept. 24, 1923, 27 L.N.T.S. 157, and Convention on the Execution of Foreign Arbitral Awards, Sept. 26, 1927, 92 L.N.T.S. 301.

(2) Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter the New York Convention]. This convention ensures the cooperation of all signatory countries in recognizing and enforcing arbitral awards granted in other signatory countries. Poland was an original signatory, ratifying the convention in 1961.

(3) Final Act of the Special Meeting of Plenipotentiaries for the Purpose of Negotiating and Signing a European Convention on International Com-

mestic arbitration is increasing in popularity in more advanced market economies, primarily because it circumvents problems common to national court systems. Arbitration is usually faster than litigation, not only because tribunals are set up ad hoc, thus avoiding court back-log, but also because arbitral decisions are final and not subject to appeal. Arbitrators are usually well-versed in commercial matters, whereas judges sitting in courts of general jurisdiction are not. Although Poland's court system includes an economic branch, the judges' lack of experience in private sector disputes makes arbitration more attractive, because parties can choose arbitrators who have specific experience with private sector disputes of various types.

The Polish Code of Civil Procedure¹⁶⁴ provides for formal arbitration similar to that in other western systems. The parties may choose anyone to arbitrate,¹⁶⁵ however, state judges are prohibited from arbitrating disputes.¹⁶⁶ Parties may design their own procedure. Alternatively, the arbitrators may determine the procedure or the parties may submit to arbitration convened by an organized forum with its own procedural rules,¹⁶⁷ such as the Court of Arbitration at the Polish Chamber of Commerce.¹⁶⁸ Parties may also conduct their ad hoc arbitration at the Court of Arbitration at the Polish Chamber of Foreign Trade, in which case certain administrative fee guidelines apply.¹⁶⁹ The parties, however, are still free to determine their own procedure.¹⁷⁰ In the event the parties cannot agree on the procedural rules, UNCITRAL rules are applied.¹⁷¹

mercial Arbitration, Apr. 21, 1961, 484 U.N.T.S. 349.

Poland is also a signatory to a number of bilateral investment protection treaties that provide for arbitration. However, Poland has not yet signed or ratified the ICSID Convention, *supra* note 114, which guarantees a forum to resolve disputes between one Contracting State (or one of its subdivisions or agencies) and a national of another Contracting State. Parties must have consented to ICSID's jurisdiction before the dispute occurs in order to be heard there.

¹⁶⁴ Code of Civil Procedure, *supra* note 123.

¹⁶⁵ *Id.* at art. 699(1).

¹⁶⁶ *Id.* at art. 699(2).

¹⁶⁷ *See id.* at art. 705.

¹⁶⁸ *See* discussion *infra* accompanying note 177.

¹⁶⁹ *See generally* RULES FOR "AD HOC" ARBITRATIONS ADMINISTERED BY THE COURT OF ARBITRATION AT THE POLISH CHAMBER OF FOREIGN TRADE IN WARSAW (1987) [hereinafter AD HOC RULES].

¹⁷⁰ *Id.* at sec. 4.

¹⁷¹ *Id.* *See* U.N. Commission on International Trade Law Decisions on Arbitration Rules and the Text of the Rules, Apr. 28, 1976, 15 I.L.M. 701 (1976). UNCITRAL refers to the United Nations Commission on International Trade Law.

In ad hoc arbitration, the arbitrators' fees may be agreed upon in the arbitration agreement, or will be fixed by an ordinary court upon request of the parties.¹⁷² The winner may request that the loser pay his costs. Unlike in the courts, no earnest money must be deposited with the arbitration tribunal.

Ad hoc arbitrators usually have broad powers, which include taking evidence or testimony under oath.¹⁷³ Arbitrators must give reasons for their decisions¹⁷⁴ unless otherwise agreed upon by the parties. The award is then signed by the arbitrators and the parties and filed with an ordinary court.¹⁷⁵ The award becomes enforceable, nevertheless, only when the successful party procures an enforcement order from a court of law.¹⁷⁶ Arbitral awards may not be appealed; they may, however, be set aside if the award falls out of the scope set down in the agreement, the rules of procedure have been breached, or the award is redundant with a court award.¹⁷⁷

The Court of Arbitration at the Polish Chamber of Commerce provides one interesting forum for private arbitration. This originated as the Court of Arbitration at the Polish Chamber of Foreign Trade, which was established in 1950 to resolve international trade disputes. Although it was an office of the Polish Chamber of Foreign Trade, the Court of Arbitration was, and still is, an independent body. Until 1990, disputes with CMEA countries averaged around 200 per year, while the number of cases involving non-CMEA countries, including Yugoslavia, averaged ten to fifteen per year, or less than ten percent of all disputes brought to the tribunal.¹⁷⁸ This later figure is disproportionately low, considering that trade with non-CMEA countries amounted to approximately thirty percent of all of Poland's foreign trade volume.¹⁷⁹ Western parties were particularly hesitant to submit to any socialist legal body. Most disputing parties chose instead to present their cases in a neutral forum, such as Switzerland or Austria. Despite this prejudice, however, the Polish Court of Arbitration of the Polish Chamber of Foreign Trade was reputed for being fair and objective in adjudicating trade disputes brought before it.

¹⁷² Code of Civil Procedure, *supra* note 123, at art. 704(1).

¹⁷³ *Id.* at art. 706(1).

¹⁷⁴ *Id.* at art. 708(1)(v).

¹⁷⁵ *See id.* at art. 708(1)(vi).

¹⁷⁶ *Id.* at arts. 711(2) and 711(3).

¹⁷⁷ *Id.* at arts. 711(1) and 712(1).

¹⁷⁸ A. Wisniewski, *The Practice of the Court of Arbitration at the Polish Chamber of Foreign Trade*, in 8 REVUE DE DROIT DES AFFAIRES INTERNATIONALES, 1012 (1989).

¹⁷⁹ *Id.*

In 1991, this tribunal was renamed the Court of Arbitration at the Polish Chamber of Commerce. The court remains available for the resolution of international commercial disputes, but through its transfer to the Chamber of Commerce the court's jurisdiction has been expanded to include disputes between Polish economic subjects. As of yet, this court has not been commonly utilized by domestic parties. Few private parties have sought alternatives to the court system. There seems to be a lack of awareness about the availability of arbitration among domestic parties and a lack of confidence in the enforceability of arbitral awards.

Parties may submit to the Court of Arbitration only if they have agreed to do so in their commercial contract or by subsequent agreement. The clause must specify this court as the locus of arbitration.¹⁸⁰ The Court keeps a list of qualified and available arbitrators, both Polish and foreign. These candidates include professors, practicing lawyers, economists, and others with expertise in commercial matters. Whereas domestic parties are limited to this list in choosing arbitrators,¹⁸¹ it seems that foreign parties are free to choose anyone whom they wish.¹⁸² In keeping with standard arbitration rules worldwide, each party chooses one arbitrator.¹⁸³ The opposing party may object to a party's choice if that arbitrator is deemed incapable of disinterested adjudication, e.g. if he is related to one of the parties.¹⁸⁴ Arbitrators may also be refused for the same reasons a judge may be excluded for a court proceeding, which reasons are set out in the Code of Civil Procedure.¹⁸⁵ Together, the two chosen arbitrators chose a third, who acts as the presiding arbitrator.¹⁸⁶ Parties may agree to a panel of five or seven as well.¹⁸⁷

Arbitration fees must be paid before proceedings begin.¹⁸⁸ Further, arbitration is not considered commenced until all arbitration fees are paid.¹⁸⁹ Administrative fees are based on a sliding scale measured by

¹⁸⁰ RULES OF THE COURT OF ARBITRATION AT THE POLISH CHAMBER OF FOREIGN TRADE IN WARSAW, (1987) [hereinafter REGULAR RULES], Section 1(b).

¹⁸¹ *Id.* at sec. 10(1).

¹⁸² *Court of Arbitration at the Polish Chamber of Commerce, in POLISH CHAMBER OF COMMERCE* 5 (1990).

¹⁸³ REGULAR RULES, *supra* note 180, at sec. 10(1)(b).

¹⁸⁴ *Id.* at sec. 16(1).

¹⁸⁵ *Id.*

¹⁸⁶ *Id.* at sec. 14.

¹⁸⁷ *Id.* at sec. 37.

¹⁸⁸ *Id.* at sec. 10(1).

¹⁸⁹ *Id.* at sec. 10(2).

the amount in controversy.¹⁹⁰ Fees may be partially returned depending upon the length of the arbitration.¹⁹¹

Arbitral decisions from both the Court at the Polish Chamber of Commerce and ad hoc panels are published annually without the parties' consent. Confidentiality is maintained, however, by not identifying the parties involved.

IX. CONCLUSION

This paper has surveyed some of the fundamental areas of law that are critical to the development of the private sector in Poland. The general conclusion is relatively optimistic. Pre-war Poland had a reasonable legal framework that now is being revived, amended, and supplemented by committed and intelligent law professors, legislators and administrators. The result is a set of laws that, although still needing careful study and revision in some key areas, most notably property rights, provides a cohesive legal framework to support the growth of the private sector. Practice and experience are needed to add detailed content to this framework and to establish the precedents that reduce uncertainty in everyday transactions.

In addition to a developing legal framework, Poland has a legal history and legal institutions firmly embedded in the European tradition, despite a forty year detour along the socialist path. Courts and judges are used and respected. They have not lost their reputation for honesty and integrity, although they may have trouble attracting the best talent given the burgeoning opportunities in the private sector. With time, there is every reason to believe that they can develop the competence and expertise needed to give them a central role in interpreting and shaping the law and in providing the private sector with a reliable means for the resolution of disputes. It would be wise, however, for the Poles also to promote alternative means for dispute resolution—most notably, private or quasi-public arbitration—that place fewer demands on the scarce legal talent in the public sector.

¹⁹⁰ *The Tariff of Fees of the Court of Arbitration at the Polish Chamber of Foreign Trade*, in RULES OF THE COURT OF ARBITRATION AT THE POLISH CHAMBER OF FOREIGN TRADE sec. 2 (1987). The basic fees are: three percent for cases up to U.S. \$10,000, plus 2 percent of the excess up to \$100,000, plus 1 percent of the excess of up to \$200,000, plus 0.5 percent of the remainder.

¹⁹¹ *Id.* at sec. 18.