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Practical M&A Guide

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Stages of the process

Introduction

When approaching the legal side of an M&A transaction, management will typically already have completed the stage of taking a strategic decision to buy or sell the specific unit or set of assets.

As a model, transactions may be broken down into the following stages:

- **Preliminaries**
- **Due diligence**
- **Negotiation and drafting of transaction documentation**
- **Closing** (conclusion of the operative agreement or agreements)
- **Post-closing actions.**

Preliminaries

Once a decision has been taken to conclude a specific transaction, the parties will often sign a letter of intent. This is a form of expression of the intention of entering into a contract in the future. The actual contract will be concluded only following negotiations.

A letter of intent (also referred to as a “letter of understanding,” “protocol,” “heads of agreement” or “memorandum of understanding”) is not a concept specifically defined in Polish law, but is widely used in current market practice.

The parties sign a letter of intent in order to establish procedures for going forward with the transaction, scheduling, the goals they seek to achieve, and the conditions for negotiations toward signing of the operative agreement and any related agreements. The letter of intent will often include provisions concerning conduct of legal, tax and financial due diligence of the target prior to conclusion of the operative agreement, as well as provisions addressing situations in which negotiations are broken off. It may also address confidentiality issues, or these may

be governed by a separate non-disclosure agreement.

The letter of intent should expressly provide that it does not impose any obligations on the parties to conclude the final agreement (but may contain other obligations, such as an obligation to maintain confidentiality, or exclusivity of negotiations), and eventual conclusion of the agreement between the parties will require negotiation of all material aspects of the deal. The letter of intent may also include binding provisions with respect to choice of law, the manner of dispute resolution, and the controlling language version of documents. The legal effect of signing a letter of intent in this form is limited to liability for the party’s out-of-pocket costs in the case of bad-faith negotiations (*culpa in contrahendo*).

At the preliminary stage, the parties will also typically decide whether it is necessary to enter into a framework agreement. In transactions with a complicated structure, a framework agreement will identify and organise the actions that must be undertaken as part of the transaction in order to achieve the purposes of the parties and compliance with legal requirements. It thus serves as a roadmap for the transaction.

Due diligence

The stage of legal analysis of the target, commonly referred to in Polish by its English name “due diligence”, derives from the Anglo-Saxon common law tradition and the ancient principle of *caveat emptor*. As the buyer proceeds at its own risk, the buyer should examine the target “with due diligence” before deciding to acquire it.

In Poland, due diligence is typically conducted by the buyer in order to assess the degree of risk associated with the planned acquisition and to determine the value of the assets, enterprise, organised part of an enterprise, or shares being acquired.

But increasingly often, the seller itself prepares a due diligence report (known as a “vendor’s due diligence report”), which is then typically verified during due diligence by the buyer.

The subject of due diligence will vary depending on whether the transaction involves the sale of shares (a **share deal**).

In the case of a share deal, analysis of the target’s corporate documents is critical, but the company’s enterprise is also examined. Because the transaction involves the shares (rather than the enterprise as such or its assets), it is necessary to:

- First, confirm the existence of the shares and determine the rights attached to the shares
- Second, verify that the seller owns the shares and whether there are any encumbrances on the shares or restrictions on selling them.

In either of the main types of transaction, the scope of due diligence typically includes, in addition to corporate matters, an analysis of documents concerning:

- Real estate (land, buildings and other structures)
- Movables and encumbrances established for the company or on the company’s assets
- Rights to intangible assets
- Financial matters
- Employment matters
- Environmental issues
- Judicial and non-judicial proceedings and the status of receivables and other claims
- Shares and other securities owned by the company
- Fundamental operations of the company (e.g. contracts with suppliers and customers, administrative contracts and the like)
- Competition issues
- Regulatory matters (licences, permits, other administrative issues, and the like).

Negotiation and drafting of transaction documentation

After gaining information about the target, the parties begin negotiations toward a mutually satisfactory price (or mechanism for calculating the price) and **transaction structure** (i.e. the terms under

which ownership of the target will pass to the buyer).

A frequently encountered model is to sign an undertaking or conditional agreement which defines the conditions that must be fulfilled before signing of the final agreement transferring ownership of the target to the buyer or direct passage of the target to the buyer. In practice the parties often decide to sign a preliminary agreement. If it meets the requirements for the validity of the final agreement (for example, in the case of a share sale agreement, if it is made in writing with notarised signatures), and one party refuses to conclude the final agreement, the other party can enforce conclusion of the final agreement through the courts.

Conditions may include, for example, **obtaining permission for a concentration** or for **acquisition of real estate by a foreigner**, or failure to exercise a right of pre-emption by an authorised authority in the case of agricultural and forest land. Other conditions may arise under the business terms agreed between the parties, e.g. prior restructuring of employment or financing of the business.

Closing

Depending on the nature of the agreement signed before (e.g. preliminary, conditional or promissory agreement, final agreement subject to a condition, or the like), the transaction is carried out by the parties signing the operative agreement, in the form required by law, together with enclosures (e.g. list of documents disclosed to the acquirer during due diligence, price adjustment mechanisms, entities subject to non-competition) and any related documents under which the title to the target is finally transferred to the buyer (referred to as “closing” or “completion”). Often this will be accompanied by conclusion of an agreements governing the future cooperation of the parties, e.g. a shareholders’ agreement (typically in the case of a **joint venture** or agreements specifying the terms for dividing the operations. It may also be necessary to prepare documents connected with the changeover in management or laying down the rules for continuing cooperation with the existing management or key employees.

If it is a deal involving shares in a joint-stock company, it will also be necessary to transfer possession

of the share certificates (in the case of registered shares) or deliver share certificates to the buyer (in the case of bearer shares).

Post-closing actions

After the closing the buyer is required to pay **taxes** due and to file the relevant declarations with the tax authorities. The share ledger must be updated, as well as public registers affected by the transaction such as the National Court Register, the land and mortgage register, etc.

After the closing, the buyer may conduct follow-up due diligence, particularly if at the time of the original due diligence, prior to the transaction, certain confidential items were not disclosed.

Sometimes the mechanism for calculation and payment of the price provides for an adjustment, depending on certain events or results achieved by the target after the closing. Then the operative agreement transferring title to the target will define how the parties are required to cooperate and report on the financial results. This also determines how the transaction will impact the operations of the target and how the parties will make their final settlement.



Selection of transaction structure

Introduction

It is crucial for the success of any transaction to determine the optimal structure in advance, often reflecting not only the interests of the parties, but also the interests of the company whose shares are being sold. This depends not only on the discretion of the investor, but also on the current legal and tax solutions and other external circumstances (such as the fulfilment of certain conditions, obtaining the required permits, or carrying out certain preliminary or restructuring measures to prepare the company or enterprise for ownership changes).

The transaction structures most often encountered in practice are:

- **Share deal**
- **Asset deal**
- **Management buyout (MBO)**
- **Leveraged buyout (LBO)**
- **Merger**
- **Division**
- **Conversion**

Share deal

A share deal is defined as a transaction involving acquisition of shares in a capital company—which in Poland means a limited-liability company (sp.z o.o.) or a joint-stock company (SA). As a result of the transaction, the buyer becomes the owner of the shares, but (apart from the right to participate in any distribution of the company's assets or liquidation of the company) does not obtain direct rights to the assets or enterprise of the target, which remains the property of the target.

This type of transaction is of particular interest to financial investors, who invest funds in various sec-

tors of the economy and hold a diversified investment portfolio. Investors also choose a share deal when the target conducts regulated activity and an asset deal would entail the need to obtain new concessions, licences or permits. However, the greatest significance for investors is their lack of liability for the debts of the target, because while the investor obtains control over the operations of the target, it is not individually liable on this basis. The investor is generally at risk only up to the amount it pays for the shares.

When deciding to conduct a share deal, it is important to be aware that the warranty arising out of public reliance on the land and mortgage register does not apply with respect to real estate held by the target. Thus, in such transactions due diligence with respect to **real estate** should be more detailed than in the case of an asset deal.

Transferability of shares

The rule of transferability of shares is an important feature of capital companies. The articles of association of a limited-liability company or the statute of a joint-stock company (in the case of registered shares) may, however, limit transactions in the company's shares, e.g. by requiring the shareholder to obtain consent to the transfer from one of the company's authorities.

Form

Transfer of the shares in a limited-liability company must be made in writing with notarised signatures. In a joint-stock company, the form of transfer of shares depends on whether they are registered shares or bearer shares. Transfer of registered shares must be made in writing, by making a declaration on the share certificate or in a separate document, and requires transfer of possession of the share certifi-

cate. Transfer of bearer shares does not require any specific form; the shares are transferred by transferring possession of the share certificates. Shares of joint-stock companies that are listed on the stock exchange (public companies) are dematerialised (i.e. do not take the form of a paper document) and are transferred by making the relevant entries in the parties' securities accounts.

Administrative notification and consent

The permissibility of a share deal may depend on fulfilment of certain notification requirements or obtaining certain administrative approvals or decisions, if one or both parties, or the company, has certain relevant features or conducts a specific type of business.

For example, a party or parties may be required to:

- Provide **notice of a concentration** of undertakings to the Polish competition authority (the president of the Office of Competition and Consumer Protection), if the entities participating in the transaction have achieved a certain level of turnover on the Polish or worldwide market
- Obtain a **permit from the Minister of the Interior and Administration** for a foreign company to acquire or take up shares in a company with its registered office in Poland which is the owner or perpetual usufructuary of real estate in Poland
- Obtain the **position of the Agricultural Property Agency** due to the right vested in the agency of pre-emption in the case of sale of shares of a company holding agricultural real estate.

It should also be mentioned here that some specific laws (such as the Gambling Act) impose restrictions on acquisition of shares in companies conducting certain regulated activity.

Seller's warranty against defects in the shares

The seller may bear liability to the buyer arising under the law or the provisions of the transaction documents. In the latter case, this will for the most part mean liability under a contractual warranty or quasi-warranty, although in line with the principle of free-

dom of contract the parties have great latitude in establishing contractual liability principles to suit their needs and the conditions of the given transaction.

The sale of shares is also covered by the statutory warranty on sales under the Civil Code. The statutory warranty provisions are an important instrument to protect the buyer in a share deal, supplementing the buyer's general claims for breach of contract.

A legal defect in shares may occur more specifically when the shares sold are encumbered by a right of pre-emption, or if the shares were created through a capital increase that was not entered in the National Court Register before the date of the sale. It should be pointed out in this respect that in a share deal, unless otherwise agreed, the seller's statutory warranty liability is directly connected solely with defects in the shares, which are the immediate subject of the transaction, and does not immediately extend to any defects in the enterprise or specific assets held by the target company. However, because the shares and their value are closely connected with the assets of the company, it cannot be entirely excluded that any defects in the company's assets could have an effect on the legal status and value of the shares.

For this reason, the parties to a share sale agreement commonly include provisions in the seller's representations and warranties concerning the condition of the company's assets, designed to protect the buyer's interests. The parties usually also provide for sanctions if the representations prove false or misleading.

Corporate notification requirements

Following a share deal and acquisition of the shares, the company must be notified of:

- change of shareholder
 - in a limited-liability company, any of the parties may notify the company of the transfer of shares, by presenting appropriate evidence, which is a condition for the company to regard the buyer as the holder of the shares (under Commercial Companies Code Art. 187.);
 - in a joint-stock company, only a person who is entered in the share register or has possession of a bearer share (subject to provisions

on securities trading) is deemed a shareholder; the relevant entry in the share register is made (under Commercial Companies Code Art. 341 and 343) at the request of the buyer, who is required to submit a document to the company justifying the entry;

and

- Establishment of control by the investor over the target company, as under Commercial Companies Code Art. 6 the new parent is required to notify the subsidiary within two weeks after obtaining control (otherwise, the parent will not be authorised to exercise voting rights to shares representing more than 33% of the share capital of the subsidiary).

Asset deal

An asset deal means a transaction in which the enterprise of a company is acquired, or an organised part of the enterprise. The sale of specific assets may also be referred to as an asset deal, but M&A transactions generally involve an entire enterprise or line of business, rather than a few individual assets.

Asset deals enable the buyer to expand or complement its existing business to include the business previously conducted by the seller. In an asset deal it is possible to divide out certain elements of the enterprise and acquire only defined parts.

In an asset deal, corporate matters are not examined because title to the company's shares is not the subject of the transaction and the buyer will not join the seller's corporate structure. The party to the transaction is not the shareholders but the company itself, which is the seller of the enterprise, an organised part of the enterprise, or specific assets. In this case, however, the assets being acquired require a more thorough analysis.

This is not the case with **real estate**, however, because in an asset deal the acquirer is protected by the warranty of public reliance on the land and mortgage register, which essentially means that if the seller of the property is entered in the land and mortgage register as the rightful owner, the seller may effectively transfer title to the property to a good-faith purchaser even if the seller is not in fact the rightful owner.

Subject of transaction

The subject of the transaction in an asset deal is an enterprise or an organised part of an enterprise, or, less often, specific assets of the enterprise.

Under Civil Code Art. 55¹, an enterprise is defined as an organised set of tangible and intangible assets intended for conducting economic activity. An enterprise includes more specifically the enterprise name (distinguishing designation of the enterprise or distinct parts of the enterprise), ownership of real estate and movables, including equipment, materials, goods and products, and other in rem rights to real estate or movables, rights under lease and tenancy agreements for real estate or movables, and rights to use real estate or movables under other legal grounds, claims, rights to securities and cash, concessions, licences and permits, patents and other industrial property rights, economic copyright and related rights, trade secrets, and books and records connected with the conduct of economic activity.

It should be borne in mind that unlike in the case of a corporate merger, conversion or division, where rights and obligations held by the company are transferred through "universal succession," transfer of an enterprise results in "singular succession." In the case of singular succession, the ability to assign each right or assume each obligation is examined individually, in light of specific regulations or contractual provisions which may prevent or restrict transferability to a third party.

Under Civil Code Art. 55¹, a transaction involving an enterprise covers everything included in the enterprise unless otherwise provided in the transaction or by specific regulations. Thus, under an agreement selling an enterprise, concessions, licences and permits pass to the buyer, unless otherwise provided by mandatorily applicable regulations, decisions of competent authorities, or the terms of the agreement. It should be borne in mind in this respect that in the case of sale of an enterprise, succession applies only to assets and not obligations. If a transaction involving an enterprise includes contracts, effective transfer of the obligations arising under the contracts requires the consent of the other party (the creditor) under each contract. If the seller of the enterprise wishes to transfer to the buyer only certain elements of the enterprise, it is necessary to include

appropriate provisions in the agreement for sale of the enterprise.

Transfer of an enterprise or organised part of an enterprise also results by operation of law in transfer of the employees of the enterprise (or the employees whose work is connected with the part of the enterprise that is being sold).

Buyer's liability for obligations

A very important issue for the acquirer is the liability imposed on it by operation of law for the obligations arising out of the operations of the enterprise. Upon acquisition of the enterprise, as a rule, the acquirer becomes jointly and severally liable with the seller also for past obligations, up to the value of the acquired enterprise. This liability also applies, for example, to employment obligations.

For this reason, an agreement on sale of an enterprise will typically contain provisions allocating the risks and liabilities between the parties, under which the acquirer may seek recourse against the seller for amounts necessary to satisfy past obligations incurred by the seller, and providing that if the acquirer itself pays such obligations it can pursue recourse claims against the seller.

Form

Sale of an enterprise must generally be made in writing, with notarised signatures, but if the enterprise includes real estate, the agreement must be made in the form of a notarial deed.

Seller's liability under warranty for defects

The statutory warranty on sales applies as relevant to the sale of an enterprise or organised part of an enterprise. The statutory warranty provisions are an important instrument to protect the buyer in an asset deal, supplementing the buyer's general claims for breach of contract.

Corporate approvals

The sale by a limited-liability company or joint-stock company of its enterprise (or an organised part of the enterprise) requires consent of the shareholders' meeting. If the appropriate shareholders' resolutions are not obtained, the sale of the enterprise is invalid.

In the case of a joint-stock limited partnership (SKA)

sale of the enterprise or an organised part of the enterprise requires the consent of all the general partners, or is invalid. Consent of the general meeting of shareholders is also required for the transaction to be valid, because regulations concerning the general meeting of shareholders of a joint-stock company also apply directly to a joint-stock limited partnership.

In the case of other types of partnerships governed by the Commercial Companies Code, sale of the enterprise without the required **corporate approvals** is valid, but may (and most often does) result in liability of the partners who signed the sale agreement.

Management buyout (MBO)

A management buyout is a transaction in which the current managers of the company (not necessarily members of the management board as such) take control over the company by buying out a controlling stake in the company's shares—either independently, out of their own funds, or in cooperation with investment funds, such as a private-equity fund. Because an MBO involves the current managers, it should be distinguished from a “management buy-in” (MBI), in which the buyout is conducted from “outside”, by persons other than the current management who plan to assume management of the company in the future, or a “buy-in management buyout” (BIMBO), which combines the features of an MBO and an MBI.

Financing

The first essential characteristic of MBO transactions is the manner in which they are financed and the source of the financing.

Although an MBO is basically understood as a buyout of the shares of a company by managers committing their own funds, in practice the managers are rarely in a position to put together enough capital to buy out the company. Reviewing MBOs over the past few years, the average equity put up by the managers themselves is perhaps 10–20%, and most of the funds come from bank loans.

Because the main security for repayment of the bank loans in an MBO is the shares that are bought out, and the obligation to repay the debt is shifted to the

acquired company, realistically the main factor enabling the managers to obtain financing for the acquisition is the creditworthiness of the target company itself. Before making a credit decision, banks review MBO proposals very cautiously, checking all aspects of the sectors in which the target of the buyout currently does business, the company itself, and the membership and quality of the management team. The last factor is crucial, as the managers are expected to present a carefully thought-out business plan for the target, together with a timeframe for the investment and a repayment schedule. The managers also need to be aware of the financial limitations the company will operate under during the debt repayment period, such as the inability to take on major investments, incur new loans for current activity, or issue shares.

Thus the practice shows that banks look more favourably on managers who are supported in the transaction by capital partners, such as private-equity funds. The presence of capital partners increases the credibility of the projects presented by the managers, because of the prior review by the funds deciding to invest in them and the commitment to carry out restructuring following the transaction. Support from a fund also reduces the amount of debt financing and thus the risk of insolvency.

Transaction structure — use of SPV

Another feature of an MBO is the use of a **special-purpose vehicle (SPV)** company as the entity carrying out the acquisition of the target company. The funds for purchasing the shares are contributed by the managers to the SPV, which then acquires the shares from the current shareholders of the target.

After the SPV acquires the shares of the target, a “debt push-down” is carried out, in which the debt is shifted to the target, so that the company itself can repay the debt incurred to purchase the shares. The debt push-down is carried out by merging the target company and the SPV.

The managers have a thorough understanding of the business and the financial condition of their own company, and in practice they will decide to conduct an MBO when they believe that the company is undervalued by the market, compared to its true potential and growth prospects.

MBOs are sometimes regarded as non-transparent and may raise suspicions that they involve insider trading, because the acquirers, as managers, know more about the target even than the seller, i.e. the owner of the company.

Legal aspects

MBOs raise the issue of “financial assistance” from a joint-stock company to third parties—in this case, the managers—in acquiring or taking up shares issued by the company.

Prior to the June 2008 amendment (Journal of Laws No. 118 item 747) to the Commercial Companies Code, Art. 345 of the code generally prohibited a joint-stock company from providing this kind of financial assistance, directly or indirectly, specifically when it involved providing loans, advances or security. This rule was intended to protect the shareholders and creditors of a joint-stock company. In effect, the assets of a joint-stock company taken over by the managers could not serve as security for repayment of credit granted to the SPV, and thus the bank could not expect to obtain security for repayment against the assets of the target until the SPV was merged with the target.

Under current law, a joint-stock company may finance acquisition or taking up of shares issued by the company, but the financing must be made on market terms and the shares must be acquired or taken up in exchange for fair market value. The company may finance acquisition or taking up of shares issued by the company if a capital reserve has first been created for such purpose. Financing by the company of acquisition or taking up of shares issued by the company requires adoption of a resolution of the general meeting of shareholders by a two-thirds majority, but if at least half of the share capital is represented at the meeting, an ordinary majority is sufficient.

Art. 345 §8 of the Commercial Companies Code excludes these requirements (except for the requirement to create a capital reserve) with respect to benefits provided within the ordinary course of business of financial institutions, as well as benefits provided to employees of the company or an affiliated company. The exclusions referred to in Art. 345 §8 do not apply to managers, however, unless a member

of the management board is also an employee of the company.

If the target of an MBO is a limited-liability company, there are only modest limitations on financial assistance by the company. Restrictions arise chiefly under Commercial Companies Code Art. 189 § 2, which prohibits the company from making payments to shareholders out of the assets of the company that would reduce the assets needed to fully cover the share capital. Thus an MBO would be impermissible if financing were provided to shareholders (and only shareholders) out of funds necessary to cover the share capital. (This particularly concerns a situation where coverage of the share capital was reduced as a result of losses incurred by the company.).

Leveraged buyout (LBO)

A leveraged buyout is a transaction in which an outside investor acquires a controlling stake of the shares of the target, using chiefly borrowed funds, with an equity investment of perhaps 15–25%. A key feature of this type of transaction is that the shares in the target serve as security for the borrowed capital. An LBO is very similar to a management buyout. Unlike an MBO, however, the acquirers behind an LBO are outside investors, who, unlike the managers of the target, do not have specific inside knowledge about the condition of the company.

A management buy-in (MBI) is a combination of the LBO and the MBO, in other words, a secondary management buyout. An MBI is instigated by managers who are not connected with the target, but have special knowledge about the condition of the target or, at least, the sector in which the target operates.

Subject of LBO

An LBO involves shares of capital companies of any size, operating in any sector of the economy. Investors are interested in LBOs particularly in the case of companies with hidden potential, where the shares may be resold at a profit after restructuring the target. In an LBO, the features of the target that are most important for the investors and the partners providing financing include:

- Stable financial condition (proven steady cash flow) and a low level of debt
- Holding assets (such as real estate and production equipment and machinery) that may be used as additional security for credit
- Capacity for reduction of operating costs after restructuring
- Individual characteristics of the new management team who are capable of exploiting the potential of the target
- Undervaluation by the market.

Financing

LBO transactions are mainly financed by an investment partner (such as a bank or private-equity fund), whose contribution represents about 75–85% of the transaction value, with the strategic investor putting up 15–25%. Financing by the investment partner requires a positive assessment of the proposal.

Because the shares of the target are the main security for repayment of the loan, and the obligation to repay the loan is shifted to the company itself, assessment of an LBO proposal is based on an analysis of:

- The market sector of the target
- The target itself, including its current and projected cash flows
- The quality of the new management team
- The plan for restructuring the target

Legal aspects

As with MBOs, LBOs are connected with the issue of financial assistance granted to the investors by the target company for acquisition of its own shares.

If the target is a joint-stock company, the issue of financial assistance is governed by Commercial Companies Code Art. 345. This provision generally allows the company to finance the acquisition of its own shares, if certain conditions are met:

- The financing of acquisition of the shares is made on market terms, after review of the solvency of the debtor.
- The shares are acquired at a fair value.

- The financing of acquisition of the shares is made from the company's capital reserves.
- The financing is conducted on the basis of prior consent of the shareholders, in the form of a resolution.

If the target of an LBO is a limited-liability company, there are only modest limitations on financial assistance by the company, mainly under Commercial Companies Code Art. 189 §2, which prohibits the company from making payments to shareholders out of the assets of the company that would reduce the assets needed to fully cover the share capital.

Merger

The decision to conduct a corporate merger is typically made because of the economic or market condition of the companies, in order to optimise administrative costs (bearing in mind the **tax aspects**) or for reasons related to restructuring within the capital group.

Permissibility of merger

The Commercial Companies Code regulates what types of entities may merge:

- Capital companies (i.e. joint-stock companies and limited-liability companies) may merge with one another or with commercial partnerships, but the partnership may not be the acquirer or the company newly formed pursuant to the merger.
- A capital company or a joint-stock limited partnership may merge with a foreign company established under the laws of another member state of the European Union or the European Economic Area with its registered office, central administration or principal place of business in the EU or EEA (cross-border merger), but a joint-stock limited partnership may not be the acquirer or the company newly formed pursuant to the merger.
- Commercial partnerships may merge with one another only by establishing a capital company.
- More than two companies may participate in a merger.
- A company in liquidation that has begun distribution of its assets, or a company in bankruptcy, may not be involved in a merger

Forms of merger

There are two distinct forms of merger:

- Merger by acquisition—the company or companies being acquired transfer all their assets to another company, the acquirer, in exchange for shares in the acquirer, which are taken up by the shareholders of the target.
- Merger by establishment of a new company—a new capital company is established to which the assets of all the merging companies are transferred in exchange for shares in the newly formed company, which are taken up by the shareholders of the merging companies.

Rights and obligations after the merger

As of the merger date, the rights and obligations of the company being acquired or the companies merging by forming a new company pass to the acquirer or the newly formed company by operation of law. More specifically, concessions, exemptions and entitlements that are part of the assumed assets pass to the acquiring or newly established company (unless otherwise provided by law or by the decision establishing such rights).

The merger date is the date the relevant entry is made in the National Court Register. The entry is a technical matter, and for organisational or tax reasons companies often request registration on a specific date. The court is not bound by such request, but generally will comply.

The acquirer or the new company formed through the merger assumes all tax-law rights and obligations of each of the merging entities.

Main stages of merger

- Preparation stage
 - Preparing documentation needed for the merger (merger plan and enclosures)
- Decision stage
 - Adoption of merger plan by the shareholders and management boards of the merging companies

- Preparation by the management boards of the merging companies of reports justifying the merger and its legal and economic grounds, in particular the share exchange ratio
- Application to appoint an auditor to examine the merger plan
- Filing of merger plan with the National Court Register and publication of the merger plan
- Notice to shareholders of the merging companies (twice)
- Adoption of merger resolution
- Registration stage
 - Filing of motion to register the merger
 - Registration of the merger.

In practice, apart from an ordinary merger, an acquirer which is the sole shareholder of the company being acquired or holds at least 90% of the shares of the target may conduct a simplified merger, not requiring:

- Preparation of a written report justifying the merger
- Review of the merger plan by an auditor
- A resolution of the shareholders' meeting approving the merger

A simplified merger may be conducted in a shorter time, i.e. within about 3 months. (By contrast, the standard merger procedure typically takes about 6 months.).

Division

The decision to conduct a corporate division is typically made because of the economic condition of the company, in order to optimise cost management (bearing in mind the **tax aspects**) or for reasons connected with the global strategy of the group.

Permissibility of division

The Commercial Companies Code regulates what types of entities may be divided:

- Only capital companies (i.e. a joint-stock company or a limited-liability company) may be divided.
- A joint-stock company may not be divided if its share capital has not been fully covered.
- A company in liquidation may not be divided if it has begun to distribute its assets or is in bankruptcy.
- Commercial partnerships may not be divided.

Forms of division

There are several distinct forms of division:

- Division by acquisition—all of the assets of the divided company are transferred to other companies in exchange for shares in the acquiring companies, which are distributed to the shareholders of the divided company.
- Division by establishment of new companies—the shareholders establish new companies, taking up all their shares, and in exchange transfer to the new companies all of the assets of the divided company.
- Division by acquisition and establishment of new company—the assets of the divided company are assigned to an existing company and to a newly formed company or companies.
- Division by split-off (division by separation)—part of the assets of the divided company are transferred to an existing or newly formed company or companies

Division of a company requires a shareholders' resolution of each of the companies involved in the division, passed by a $\frac{3}{4}$ majority of votes representing at least half of the share capital (unless the articles of association or statute provides for a more stringent requirement).

The division date is the date of deletion of the company from the National Court Register. The deletion is a technical matter, and for organisational or tax reasons companies often request that the division be registered on a specific date. The court is not bound by such request, but generally will comply.

Division by establishment of a new company occurs as of the date of its entry in the register. In the case of transfer of part of the assets of the divided company to an existing company, the division occurs as of the date of entry in the register of the increased share capital of the acquirer (the division date).

Rights and obligations after the division

As of the division date, or separation date, the acquirers or the companies newly created in connection with the division assume the rights and obligations of the divided company as specified in the division plan. More specifically, concessions, exemptions and entitlements that are connected with the assets allocated to the given acquirer or newly established company pass to that company (unless otherwise provided by law or by the decision establishing such rights).

The acquirer or the new companies formed in connection with the division assume all tax-law rights and obligations of the divided company connected with the assets allocated to them under the division plan.

Main stages of division

- Preparation stage:
 - Preparing division documentation (division plan and enclosures)
- Decision stage:
 - Preparation by the management boards of the company being divided and each of the acquiring companies of reports justifying the division and its legal and economic grounds, in particular the share exchange ratio
 - Filing of division plan with the National Court Register
 - Application to appoint an auditor to examine the division plan
 - Notice to shareholders of the company being divided (twice)
 - Adoption of division resolution
- Registration stage:
 - Filing of motion to divide the company
 - Registration of the division.

Conversion

The decision to change the corporate form is made in connection with the economic condition of the entity, in order to optimise the management (bearing in mind the **tax aspects**). The converted company continues to hold the same rights and obligations and continues the business, but under a new legal form.

The decision to convert the legal form may also be dictated by a desire to limit liability, because in commercial partnerships the partners may be personally liable for the debts of the partnership, but in capital companies the shareholders' liability is generally limited, and they are at risk only for the consideration they have provided for the shares. Moreover, conversion into a capital company may be tied to growth in the scale of the business or an intention to float the company on the stock market (which is possible only in the case of a joint-stock company or joint-stock limited partnership).

Companies are sometimes converted into partnerships in order to reduce tax liabilities. A company is an income tax payer, and thus income tax is paid at the level of the company as well as the shareholders. But in the case of a partnership, income tax is paid only at the level of the partners. An exception is the joint-stock limited partnership, which, like companies, is an income tax payer..

Permissibility of conversion

The Commercial Companies Code regulates what types of entities may undergo conversion:

- A registered partnership (s.j.), professional partnership (sp.p.), limited partnership (sp.k.), joint-stock limited partnership (SKA), limited-liability company (sp.z o.o.) or joint-stock company (SA) (pre-conversion) may be converted into another form of commercial company or partnership (post-conversion).
- An ordinary partnership (s.c.) may be converted into any commercial company or partnership; however, in the event an ordinary partnership is converted into a registered partnership, a different legal regime applies.
- The business of a sole trader (i.e. business conducted pre-conversion by an individual on his or

her own account) may be converted into a single-shareholder capital company.

A company in liquidation that has begun to distribute its assets may not undergo conversion, nor may a company in bankruptcy.

Forms of conversion

There are two main forms of conversion:

- Conversion of a partnership into a capital company
- Conversion of a capital company into a partnership

Rights and obligations after conversion

As of the conversion date, the post-conversion entity assumes all of the rights and obligations of the pre-conversion entity, specifically including concessions, exemptions and entitlements (unless otherwise provided by law or by the decision establishing such rights).

The conversion date is the date when the post-conversion entity is entered in the National Court Register. The entry is a technical matter, and for organisational or tax reasons parties often request that the conversion be registered on a specific date. The court is not bound by such request, but generally will comply.

In the case of conversion into a company, the company assumes all tax-law rights and obligations of the pre-conversion entities.

A partnership arising as a result of conversion of a company enters into the totality of the tax-law rights and obligations of the converted company. After the conversion, the taxpayers are the partners of the

partnership, subject to taxation under the rules appropriate to them (personal income tax or corporate income tax, as the case may be).

Main stages of conversion

- Preparation stage:
 - Preparing conversion documentation (conversion plan and enclosures).
- Decision stage:
 - Filing of conversion plan with the National Court Register
 - Application to appoint an auditor to examine the conversion plan
 - Notice of the conversion to the shareholders/partners of the entity being converted (twice)
 - Adoption of conversion resolution
 - Declaration of the shareholders on participation in the converted company, submitted within one month after adoption of the conversion resolution
- Registration stage:
 - Filing of motion for conversion
 - Registration of the conversion

In the case of conversion of a company into a partnership, it is important to examine the tax aspects of the conversion carefully. If the company has undistributed profit or profit assigned to capital other than share capital, upon conversion it will be taxable income of the partners.



Specific conditions concerning the parties

Introduction

Depending on the type of parties actively involved in the transaction, in many situations it is necessary to reflect additional legal considerations related to their involvement in the transaction. Four such types of parties whose specific nature must be taken into consideration at the planning, negotiating and documentation stages of the transaction are discussed below:

- **partnerships**
- **joint ventures**
- **investment funds**
- **special-purpose vehicles**

Partnerships

The distinction between commercial partnerships (referred to in Polish law literally as “personal companies”—other than ordinary partnerships operating under the Civil Code)—and other commercial companies is based on the joint action of the owners of these entities, i.e. the partners. Unlike capital companies, which may have a single shareholder, it is not possible to form a partnership which has only one partner.

A partnership is also characterised by the personal liability of the partners (or least some of them) for the debts of the partnership, and the partners’ direct handling of the affairs of the partnership, which varies in scope depending on the specific type of partnership and may be governed to a certain extent by the partnership agreement. These partnerships do not have legal personality, but it is clear that they are legal entities in the sense that they have the capacity to acquire certain rights in their own name, including real estate and other property rights, and to incur obligations, as well as the capacity to sue and be

sued. These partnerships operate under the partnership name. The partners (in this respect much like the shareholders of a capital company) undertake to pursue a common purpose by making their contributions to the partnership and, as provided by the partnership agreement, by cooperating in other ways.

One common feature of all partnerships is the necessity to include the name of at least one of the partners in the name of the partnership.

Transfer of rights and obligations

A partner may not join a partnership by buying shares or leave the partnership by selling shares, because shares do not exist in a partnership (with the exception of shares of stock in a joint-stock limited partnership). A change in the membership of a partnership essentially consists of transferring the totality of the rights and obligations of a partner. All rights and obligations of a partner in a partnership may be transferred to another person only where the partnership agreement so provides. Unless the partnership agreement provides otherwise, all rights and obligations of a partner in a partnership may be transferred to another person only after the written consent of all of the remaining partners has been obtained. In case of a professional partnership, the Commercial Companies Code provides for a requirement that a new partner hold certain professional qualifications.

In the case of assumption of an existing partner’s rights and obligations by a new partner, the new partner is jointly and severally liable with the former partner for the partner’s obligations related to the business of the partnership as well as the obligations of the partnership itself arising prior to the new partner’s joining the partnership.

Purpose and features of specific types of commercial partnerships

1. Registered partnership (s.j.)

A registered partnership is the basic form of a commercial partnership, and the regulations governing the functioning of a registered partnership apply to other types of commercial partnerships as well, if not otherwise provided by specific regulations applicable to the other types.

The partners, who may be either natural or legal persons, or entities with no legal personality but with legal capacity granted by law, enter into a written partnership agreement, which must specify the name and registered office of the partnership, the contribution of each partner and its value, the scope of the partnership's business, and the duration (if limited).

The partners may make contributions to the partnership in cash or kind, including ownership or usufruct of property. A partner may also contribute his or her labour. No minimum value of contributions is established by law, but the amounts are determined by the partnership agreement. As a rule, even partners who have made the minimum contribution have rights and obligations equal to the other partners and share in the partnership's profits and losses equally. A partner in a registered partnership may not be deprived of the right to profit.

Each of the partners has the right and duty to conduct the affairs of the registered partnership and to represent the partnership without compensation. These actions may not be assigned to third parties to the exclusion of the partners. The partners of a registered partnership are secondarily liable for the debts of the partnership. This means that if execution against the assets of the partnership is ineffective, the creditor may execute against the assets of the partner.

If the partnership has been formed for an undefined period, the partnership agreement of a registered partnership may be terminated upon six months' notice, effective at the end of the financial year. Termination of the partnership agreement leads to the dissolution of the registered partnership; however, the partnership continues among the remaining partners if the partnership agreement so provides or

the remaining partners so decide. In such event, a partner leaving the partnership is reimbursed in an amount equivalent to the partner's capital participation in the partnership.

2. Professional partnership (sp.p.)

A professional partnership may be established only by individuals, for the purpose of practising one of the free professions specified in the Commercial Companies Code or other statute.

Unlike in a registered partnership, the partners of a professional partnership are not liable for the obligations of the partnership connected with practice of the profession by other partners or the employees who are their subordinates. They may provide in the partnership agreement which of the partners shall be liable for the debts of the partnership on the same basis as a partner in a registered partnership.

If not otherwise provided in the partnership agreement, each partner may represent the partnership individually. The partners may also provide in the partnership agreement that the management board of the partnership will conduct the affairs of the partnership and represent the partnership.

As in the case of a registered partnership, leaving a professional partnership requires notice six months prior to the end of the financial year. A partner who has lost the required professional qualifications is required to leave the partnership at the latest at the end of the financial year in which he or she lost the right to pursue the profession.

In addition to obtaining the consent of all the partners, a new partner must demonstrate that he or she holds the appropriate professional qualifications in order to join the partnership.

In other respects, the regulations concerning registered partnerships apply.

3. Limited partnership (sp.k.)

A limited partnership operates an enterprise in its own name. A limited partnership must include at least one general partner, who bears unlimited liability to the creditors of the partnership, and at least one limited partner, whose liability to the creditors of the partnership is limited to a fixed, agreed amount, sometimes referred to in English as the "commandite sum" or the "commendam sum." The

limited partner's contribution may be made in a value lower than the commandite sum, unless otherwise provided in the partnership agreement.

Operating in the form of a limited partnership, in which the partners have a varying range of liability, contributions and authority, allows the general partners to bring new members into the partnership, who as limited partners generally make an investment in the partnership but have limited authority to act for the partnership and also limited liability for the debts of the partnership.

A limited partnership is represented by the general partners. A limited partner basically has no right or duty to conduct the affairs of the partnership, unless otherwise provided in the partnership agreement. The limited partner may represent the partnership under a power of attorney. Unless otherwise provided in the partnership agreement, a limited partner participates in the profits of the partnership in proportion to the actual contribution.

The name of a limited partnership must contain the name of one or more of the general partnership and the suffix "spółka komandytowa" (abbreviation "sp.k."), identifying the legal form. The partners may be either natural or legal persons or entities with no legal personality but with legal capacity granted by law. If a general partner is a legal person, its name may be included in the partnership name, together with a designation of its legal form. The partnership name may not contain the names of the limited partners. Persons whose names are included in the name of the partnership are liable for the partnership's debts to creditors like general partners, regardless of their actual role under the partnership agreement.

The partnership agreement is concluded in the form of a notarial deed, stating the name and registered office of the partnership, the subject of its business, the duration (if limited), and the contributions made by each of the partners, as well as the commandite sum.

In other respects, a limited partnership is subject to the regulations governing a registered partnership.

4. Joint-stock limited partnership (SKA)

A joint-stock limited partnership is a partnership that has share capital, which enables it to raise capital by selling shares, while the general partners retain

control over the partnership. The share capital must be at least PLN 50,000.

A joint-stock limited partnership conducts an enterprise under its own name. In this form of partnership, at least one partner (a general partner) has unlimited liability for the debts of the partnership, and there is at least one partner who is a shareholder. The shareholders are not liable for the debts of the partnership.

The name of a joint-stock limited partnership must contain the name of one or more general partners and the suffix "spółka komandytowo-akcyjna" (abbreviation "SKA"), identifying the legal form. It may not contain the name of a shareholder. Persons whose names are included in the name of the partnership are liable to the creditors like a general partner, regardless of their status in the partnership.

The rules governing a registered partnership apply to the relations of the general partners between one another and to the partnership, the shareholders and third parties.

In other matters, particularly involving share capital, shareholders' contributions, shares, the supervisory board (if appointed) and the general meeting, the regulations concerning a joint-stock company apply. The statute may provide for establishment of a supervisory board, and it is mandatory if there are more than 25 shareholders.

The general partners have the right and duty to conduct the affairs of a joint-stock limited partnership and represent it externally. The statute may provide that such right is vested in one or more general partners. A shareholder may represent the partnership only on the basis of a power of attorney. Unless otherwise provided in the statute, the general partners and the shareholders participate in the profits of the partnership in proportion to their actual contributions.

Authority reserved to the general meeting is excluded from the authority of the general partners managing the affairs of the partnership, such as:

- Review and approval of the general partners' report on the business of the partnership and the annual financial report

- Granting a release to the general partners for their management of the affairs of the partnership in the prior year
- Granting a release to the members of the supervisory board.

Some resolutions of the general meeting (e.g. concerning distribution of profit attributable to the shareholders, or sale of real estate belonging to the partnership) require the consent of all of the general partners.

The statute is signed in the form of a notarial deed by the founders, who must include, at a minimum, all of the general partners.

The statute must state:

- Name and registered office of the partnership
- Subject of the business
- Duration (if limited)
- Contributions made by each general partner
- Amount of the share capital
- Number, type and par value of the shares
- Names and addresses of the general partners
- Organisation of the general meeting, and the supervisory board if provided for in the statute.

Only a general partner has a right to terminate the partnership agreement, and then only if permitted by the statute.

5. Limited partnership or joint-stock limited partnership with a capital company as a partner

The structure of a limited partnership or joint-stock limited partnership in which the general partner is a limited-liability company or joint-stock company is most often formed through conversion of a capital company into a commercial partnership, with the capital company as the general partner and an individual as the limited partner, where the individual is also a shareholder of the capital company, or by a capital company joining a commercial partnership as a general partner. The purpose of this structure is to achieve limited liability for the partners while maintaining the tax transparency of a partnership.

In a partnership structured in this way, the management board of the company that is the general partner acts for the partnership. To be certain of the representation of such a partnership, it is necessary to review the National Court Register for both the partnership and the company that is the general partner.

Joint ventures

The term “joint venture” covers a broad range of different forms of cooperation between individuals or other entities, aimed at achieving the purposes defined by the participants—typically profit-making or organisational. All the participants in a joint venture need not have the same purposes in mind. A joint venture may be aimed at achieving an end result, or pursuing a process of continuing cooperation. In the first variant, the joint venture typically has a fixed end date, after which the parties will end their cooperation or change it into a different form of cooperation. In the second variant, the joint venture may have no fixed term, but may be terminated by either of the parties under certain agreed conditions. Polish law does not contain specific regulations governing joint ventures as such. Thus any agreement for pursuing projects as a joint venture may be concluded as an unclassified type of agreement, governed by the Civil Code. Additionally, if upon conclusion of a joint-venture agreement a company is established in which the parties to the joint venture become shareholders, the joint-venture agreement is governed by the Commercial Companies Code with respect to the corporate relations between the shareholders.

Consideration provided by the parties to a joint venture to carry out the project

The basis for carrying out a joint-venture project or transaction is for each of the participants to provide specific consideration for the project. More specifically, this may involve provision of certain assets for use in the project, labour, capital, knowhow and the like. It is assumed that through joint action, the consideration provided for the joint venture by its participants will release synergies and enable achievement of their common goal.

A joint-venture transaction may take the form of a greenfield project, i.e. implementing the project

from the ground up by providing the consideration indicated above, defining the legal, organisational and asset structure, and further cooperation in the joint investment. A joint venture may also involve further pursuit of a project using an existing legal and organisational structure. When new partners join an existing venture, together they may develop the project more quickly, based on the existing asset structure.

Transaction structure — creation of SPV and options

Most joint ventures include two main elements that are the basis for carrying out the project: the knowhow, innovative solution or market position of one participant, and the capital or fixed assets of the other participant. A concession or licence to conduct a specific type of business may be an additional element. In order to carry out a joint venture, in practice, the parties may commit other components at their disposal or obtained from external sources. These elements are typically combined through establishment of an enterprise based on them, which may take the form of a company or a partnership. Thus **an SPV company** is a frequent instrument for carrying out a joint venture.

But before establishing an SPV, the parties will usually enter into one or more agreements generally governing their cooperation and implementation of the project. A principal agreement serving as the basis for further agreements is also a characteristic feature of a joint-venture project or transaction. It will cover such terms as the grounds for the parties' cooperation, the assets to be devoted to realisation of the project, the necessary organisational instruments (including the SPV), the duration of the project, the rules for financing, decision-making authority, and the plans for winding up the cooperation.

This last element may involve another aspect typical for joint ventures, namely bilateral or unilateral options for transferring the shares in the joint-venture structure and clauses for exiting the project. Such options are essentially agreements for purchase or sale of specific rights, creating rights or obligations connected with taking over or changing the control over the project, or increasing or reducing the level of participation in the project by specific parties, or a party's withdrawal from the project altogether.

Withdrawal may also be tied to introduction of a new participant to take the place of the party exiting the joint venture, in which case the project will continue with a new team. The options are most often established with respect to the shares in the SPV conducting the venture. Nonetheless, other approaches to framing the rights and obligations of the participants, also in the nature of an option, may also be used.

Transaction stages

The overall picture of a joint-venture transaction is generally as follows:

- Organising a group of investors and agreeing on a preliminary plan for carrying out the transaction, including identification of the assets needed to carry out the project
- Drafting a business plan
- Conducting legal, economic, technical and other analyses of the assets earmarked for carrying out the project, a legal analysis of the administrative requirements to be met before starting the project and during implementation, and an analysis of the sources of financing
- Conclusion of the joint-venture agreement (this may be done at an earlier stage and include conditions for carrying out subsequent actions)
- Establishment of the special-purpose company or transaction vehicle (SPV) to carry out the project
- Main project implementation phase
- Completion of the project or converting it into another form of operation or cooperation by the parties

Legal aspects

Although joint-venture agreements have been used in Poland since the start of the economic transformation in the late 1980s, they are not governed by specific regulations in the Civil Code or other legal acts. Nonetheless, their permissibility is undoubted, based on the principle of freedom of contract. Commercial entities established for the purpose of implementing joint-venture projects are governed by the applicable regulations of the Commercial Companies Code and other acts.

A fundamental and fairly common issue is the correlation between the main joint-venture agreement and the articles of association or statute of the SPV. The joint-venture agreement tends to be a multi-faceted agreement. The corporate charter of the SPV, on the other hand, generally deals with a narrower set of issues, with the main purpose of establishing the SPV that will carry out the venture and the rules for functioning of the SPV, reflecting the general rules for the project set forth in the joint-venture agreement.

The charter of the SPV contains provisions governing the rights and obligations of the founders and shareholders or partners of the SPV, who are typically the parties to the joint-venture agreement, but the scope of regulation of their cooperation in the corporate charter is typically narrower than in the case of the joint-venture agreement because of the limitations imposed by corporate law.

An additional issue often arising with respect to the rules governing a joint-venture project, and increasing the degree of complication in its structure, may be the desire to choose foreign law to govern the joint-venture agreement, while the charter of a Polish SPV must be governed by Polish law; likewise with the transfer of ownership of its shares, even if provided for in a joint-venture agreement governed by foreign law.

Acquisition of a significant stake in public companies

Unlike transactions involving private companies, acquisition of shares of public companies is subject to a number of special requirements, particularly concerning the procedure for the transaction, depending on the size of the acquired stake and reporting obligations referred to in the Public Offerings Act (the Act on Public Offerings, Introduction of Financial Instruments into an Organised System of Trading, and Public Companies).

It should also be pointed out that any due diligence prior to the transaction must be conducted in a limited scope, due to the obligation of a public company to protect inside information that could affect the price. Due diligence can cover information that the company releases to the public pursuant to its

reporting obligations, i.e. financial data and information material to investors and the market that does not constitute inside information.

Another characteristic of transactions in shares of listed companies is that in the case of a significant stake of shares, a brokerage must be involved in the process.

Acquisition of a significant stake of shares

Investors can freely carry out transactions involving shares of public companies (i.e. listed on the Warsaw Stock Exchange) only when the transaction will not result in increasing the investor's share in the total number of votes by more than 33% or 66%.

Crossing the threshold of 33% of the total votes in the company may occur only as a result of voluntary announcement of a tender offer for sale or exchange of the shares in a number ensuring achievement of 66% of the total votes, and crossing the threshold of 66% of the total votes in the company may occur only as a result of voluntary announcement of a tender offer for all of the remaining shares of the company.

An investor who has crossed the 33% threshold through indirect acquisition of shares (i.e. as a result of a public offering, by in-kind contribution of the shares to a company, merger or division of a company, as a result of a change in the company's statute, expiration of share privileges, or occurrence of a legal event other than a transaction or taking up of newly issued shares) is required within 3 months to announce a tender offer for sale or exchange of shares (compulsory tender) in a number resulting in achievement of the threshold of 66%, or to sell the shares so that the holdings fall below the threshold of 33%.

Similarly, crossing the threshold of 66% for the foregoing reasons results in an obligation to announce a tender offer for all the remaining shares of the company within 3 months, unless during that time the total number of votes falls to no more than 66%.

The tender offers referred above are conducted by brokerages after the acquirer provides full financial security for the transaction in the form of cash or a bank or insurance company guarantee.

In assessing whether an investor intending to acquire shares is bound by the obligation to conduct a tender offer, the shares held by its affiliates should also be counted, as well as the number of votes held by entities acting in concert with it or holding a proxy to vote for it at the general meeting.

The obligation to announce a tender offer does not arise if:

- The shares acquired are listed on the NewConnect market
- The transaction occurs between entities in the same capital group
- The shares are acquired under the procedure set forth in the Bankruptcy Law or in an execution proceeding, or
- The shares are acquired pursuant to an agreement on establishment of financial security or the shares are pledged to satisfy the pledgee under the procedure of assuming ownership of the collateral

Price specified in tender offer

An investor who announces a tender offer cannot freely set the price but is bound by the following legal restrictions.

The price offered for the shares may not be lower than:

- The average market price for the 6 months preceding announcement of the tender
- The average market price for a shorter period if the company's shares have been traded on the main market for less than 6 months
- The highest price paid for the shares during the 12 months preceding the tender by the entity required to announce the tender, or entities controlled by it, controlling it or acting in concert with it
- The highest value of the non-cash consideration which the entity required to announce the tender gave in exchange for the shares during the 12 months preceding announcement of the tender, or

- The average market price for the 3 months of trading in the shares on the regulated market preceding announcement of the tender, in the case of a tender seeking to exceed the threshold of 66% of the total votes in a public company

The acquirer may agree with the seller on a lower price in the tender, but only in relation to a minimum of 5% of all shares in the company that will be acquired in the tender.

Squeeze-out

A tender offer for sale or exchange of shares also affects the situation of shareholders who do not intend to accept the offer. A shareholder who achieves or exceeds the threshold of 90% of the votes has a right to demand that the remaining shareholders sell all of their shares. Fulfilment of this demand does not depend on the consent of the minority shareholders. This situation is referred to as an "involuntary buyout" or "squeeze-out." Under the same arrangement, the minority shareholder may demand that its shares be bought out by the shareholder who has achieved or exceeded 90% of the votes.

Reporting obligations

An investor who:

- Achieves or exceeds the threshold of 5%, 10%, 15%, 20%, 25%, 33%, 33⅓%, 50%, 75% or 90% of the total votes in a public company, or
- Holds at least 5%, 10%, 15%, 20%, 25%, 33%, 33⅓%, 50%, 75% or 90% of the total votes in the company and as a result of a reduction in the shares falls to 5%, 10%, 15%, 20%, 25%, 33%, 33⅓%, 50%, 75%, 90% or less of the total votes

is required within 4 business days from learning of the change in percentage or within 6 trading days from the date of the transaction on the regulated market or alternative trading system to disclose this information to the public, KNF and the company.

A notification obligation also arises in the event of acquisition or sale of a number of shares changing the existing share:

- In the event of a share above 10%, a change of at least 2% of the total votes in the case of a company listed on the main market, or 5% if the shares are admitted to trading on a regulated market other than the official market, or
- In the event of a share above 33%, a change of at least 1% of the total number of votes at the general meeting.

The notification obligation also applies to an entity that has achieved or exceeded a given threshold of votes in connection with the occurrence of a legal event other than a transaction, e.g. gift or inheritance, or a change in the number of votes due to a change in the structure of the shareholding as a result of redemption of a portion of the shares, and in the case of indirect acquisition of the company's shares.

Consequences of violation of reporting obligation

If these reporting obligations are not performed, the shareholder cannot exercise the voting rights to the shares, and votes cast in violation of this prohibition shall not be counted in calculating the result of the vote on a resolution of the general meeting.

The ban on voting the shares also applies to all shares held by entities controlled by the entity that acquired the shares in violation of these obligations.

Acquisition of shares in financial institutions

The intention to acquire shares in a financial institution (i.e. a bank, insurance company, investment fund company or brokerage) requires notification of KNF, as provided in the Banking Law of 29 August 1997, the Insurance and Reinsurance Act of 11 September 2015, the Act on Investment Funds and Alternative Investment Fund Management of 27 May 2004, and the Trading in Financial Instruments Act of 29 July 2005.

Notification of KNF

A duty to notify KNF arises when the intended acquisition of shares, direct or indirect, will result in obtaining or exceeding 10%, 20%, one-third or 50%, respectively, of the total votes at the share-

holders' meeting of a financial institution, or the equivalent percentage of the share capital. The notification requirement also applies to:

- Situations in which the investor intends to obtain control over a financial institution, directly or indirectly, in some way other than acquiring or taking up shares or rights to shares giving it a majority of the total votes
- A pledgee or usufructuary entitled to vote the shares
- Situations in which an entity obtains voting rights at a given threshold as a result of events other than acquiring or taking up shares or rights to shares, particularly as a result of amendment of the statute or as a result of extinguishment of voting privileges or restrictions
- Situations where two or more entities act in concert to exercise voting rights.

KNF will declare its objection to acquisition or taking up of shares or rights to shares or obtaining control over a financial institution, in the form of a decision, if there are formal defects in the notification, if the deadline to submit additional information or documents is not met, or if justified by the need for prudent and stable management of the given institution, the potential influence by the notifying party over the institution, or the assessment of the financial condition of the notifying party.

If the party intending to acquire the shares files the notification with KNF with all the required documentation and does not receive any response from KNF within 60 business days, KNF is deemed to consent to the acquisition.

A duty to notify KNF also arises if an entity intends to dispose of shares of a financial institution authorising it to exercise over 10% of the total votes at the general meeting, as a result of which it would hold a stake of shares authorised to exercise less than 10%, 20%, one-third, or 50% of the total votes at the general meeting. This obligation also applies to an intention to sell bonds convertible into shares, depository receipts or other securities providing a right or obligation to acquire shares in a financial institution.

Prohibition of exercise of voting rights to acquired shares

If these obligations are not met, the voting rights under the acquired shares cannot be exercised. But in specifically justified instances, KNF may waive this prohibition if required in the interests of the customers of a Polish bank, insurers, insureds, beneficiaries of insurance policies, participants in investment funds or collective securities portfolios, customers of investment funds, brokerages or their customers.

KNF may also issue a decision prohibiting an entity from exercising voting rights to shares or rights vested in the dominant entity, based on a justified need for prudent and stable management of a financial institution, or evaluation of the financial condition of an entity that has directly or indirectly gained voting rights or become the dominant entity or could influence the given financial institution.

KNF may also issue a decision ordering an entity to divest shares within a designated period.

Notification of financial institution of number of shares held

An entity that has directly or indirectly acquired or taken up shares or rights to shares in a Polish bank which represent or together with shares already held represent a block of shares reaching or exceeding the threshold of 5%, 10%, 20%, 25%, one-third, 50%, 66% or 75% of the total shares at the general meeting, or has obtained control over a Polish bank, is required in each instance to notify the bank promptly, and the bank in turn will forward this information to KNF.

A notification obligation also arises in the case of acquisition, taking up or disposing of shares in a brokerage, insurance company, or investment fund company.

Transaction vehicles (SPV)

In the case of acquisition of shares in a Polish company by investors (including foreign investors), it will often prove necessary for the investor to use another Polish company as the acquirer. To this end, the structure used most often is a limited-liability company serving in the transaction as a special-purpose vehicle (SPV).

Shelf companies

The investor can establish a new company and take up the shares in the company. But given the time required for the procedure of entering a newly established company in the commercial register, as an alternative to establishing a new SPV for the purposes of the transaction investors often decide to acquire an existing “shelf company” and then participate in the transaction via the shelf company.

This is a fully registered company, with legal personality and also holding:

- National Court Register number (KRS), tax number (NIP), CIT and VAT registration, and statistical number (REGON)
- Temporary registered office
- Minimum share capital (PLN 5,000 in the case of a limited-liability company)
- Bank account holding the funds from the shareholder’s payment to cover the share capital.

Shelf companies generally do not have an operating history; that is, before being offered to a potential investor the company has not been used to conduct any operations or business, and its activity has been limited to carrying out accounting and reporting requirements.

When a shelf company is used, the course of the transaction does not depend on the length of the judicial proceeding to register the company, and upon acquisition of the shares the SPV is ready to proceed with the planned venture. After acquiring a shelf company, it may be necessary to amend the articles of association to meet the buyer’s needs; these changes become effective upon entry in the National Court Register. But in most instances a shelf company can be used immediately after it is acquired.

It should also be pointed out that effective from the beginning of 2012, the Commercial Companies Code now provides for the possibility of quick establishment of a limited-liability company based on a standard online form for the articles of association. As the practice develops in this respect, it will be possible to assess whether this express approach to establishing a company is a more practical alternative to using shelf companies and streamlining of the

procedure for amending the standard articles of association after formation of the company.

Capital increase of SPV

Before using the SPV for the transaction it will typically be necessary to add to its capital to provide the funds to carry out the planned acquisition of the shares of the other entity.

The capital of the SPV will usually be increased in one of three ways:

- Contribution to cover the shares in the newly created share capital (in the case of a new company) or the shares in the increased share capital of an existing company
- Surcharges (dopłaty) by the shareholders (if permitted by the articles of association of the SPV)
- Loans to the SPV by its shareholders.

In the case of loans, however, the limitations arising under thin capitalisation rules must be observed.

Simply put, under the thin capitalisation rules, a shareholder loan will be tax-neutral for the company so long as a company's total indebtedness to shareholders (including the value of loans) does not exceed the company's share capital (1:1 ratio). For this reason, a potential loan to the company by a shareholder is preceded by an increase in the company's share capital.

It also happens in practice that a shareholder first makes a loan to the company (in an amount not exceeding the company's equity), and then after some time the parties agree to convert the loan into an increase in share capital. Such measures are mainly aimed at improving the company's balance sheet.

Shareholder guarantee

If the investor uses an SPV, strictly speaking the entity involved in the transaction is not the investor

itself—which probably has a reputation and a recognised position on the market—but an empty “shell” with no assets or operating history.

For this reason, the other party (e.g. the seller of the shares that are the subject of the transaction) will typically demand that the investor guarantee the obligations taken on by the SPV in the transaction.

Depending on the legal construction of the venture, the guarantee will typically take the form of the investor's assumption of the SPV's debt under the transaction documentation (becoming jointly and severally liable with the SPV, in which case the investor will become a party to the transaction) or by providing the other party with a separate document, issued by the investor, in which the investor guarantees the obligations of the SPV.

Control issues

If the party interested in acquiring shares in a Polish company is a financial investor (such as an investment fund or private-equity fund), unlike an industry investor it will typically not have its own managerial team with knowhow in that specific industry.

Thus, until closing, the management board of the SPV will be made up of the investor's representatives, appointed temporarily, who then will be replaced after closing by a management team, often coming from the company acquired in the transaction. Consequently, the same persons will often serve on the management boards of both entities. Often the final element of the transaction is to simplify the capital structure by merging the Polish entities, where the SPV is the acquirer of the company acquired in the transaction.

In these situations, it is crucial to schedule the closing activities properly.



Specific transaction conditions

Introduction

Depending on the subject of the transaction, it is sometimes necessary to reflect additional legal aspects related to the target or the scale of the operations of the participants or the target.

The specific conditions most frequently encountered arise under **environmental law**, **employment law**, regulations governing specific industries, **regulations governing banking and finance**, **competition law** and **real estate regulations**.

Environmental issues

Issues under environmental law in an M&A transaction should be identified separately for transactions in which there is a change of shareholder (share deals) and for transactions involving an enterprise, an organised part of an enterprise, or other assets (asset deals). The risks should then be appropriately addressed in the transaction structure and documentation.

Identification of risks related to environmental impact of operations

In many situations, an expert understanding of the complex issues of environmental law and skill at identifying risks and drawing the proper conclusions on the basis of a thorough analysis of the operations of the target and the findings of an environmental audit are a condition for carrying out the transaction properly.

The risk arising from non-compliance with environmental requirements is important not only in the context of transactions involving major industrial facilities, or companies operating in the chemicals, mining or transport sector—in other words, entities with significant environmental impact. In such cases, irregularities may occur more often and entail

serious consequences, but the risk of environmental impact of the target's operations also arises in other transactions, particularly when real estate is involved.

Attention must also be paid to essential environmental issues in many transactions involving corporate merger, division or conversion, and in transactions involving an enterprise (or organised part of an enterprise), real estate, or shares.

The importance of detailed environmental due diligence is increasing, as is visible in three aspects.

First, for several years there has been a visible trend toward expanding the list of environmental requirements imposed on businesses. This has been accompanied by imposition of more rigorous liability standards. Examples include implementation into Polish law of the Environmental Liability Directive (2004/35/EC) and the Environmental Crime Directive (2008/99/EC). The Environmental Liability Directive imposes costly obligations to prevent and remedy harm to the environment, and the Environmental Crime Directive requires EU member states to punish perpetrators of environmental crimes. The trend toward expansion and stiffening of environmental laws is expected to continue in the upcoming years.

Second, apart from criminal environmental liability and liability with respect to remediation of environmental harm, businesses may also face administrative sanctions in the form of increased fees and fines. Significantly, these administrative sanctions are imposed on the basis of strict liability, without regard to fault on the part of the persons conducting the business. In order to impose administrative sanctions, it is sufficient to prove a violation of the regulations, and as a result these are the sanctions most commonly imposed on businesses. And in

many instances there is no fixed upper limit for increased fees or fines, because the amount often depends on the duration of the violation and the type of substances released to the environment.

Third, Poland's history, the legacy of the former communist system, and a continuing low ecological awareness have resulted in widespread neglect of environmental compliance, which even many years later may present a material risk for acquirers of businesses or brownfield sites.

Evaluation of the environmental risk associated with a planned transaction is thus extremely difficult. The lack of a highly developed legal culture in the area of environmental compliance significantly hinders contract negotiations. This awareness is rapidly growing, however, among parties to transactions and environmental enforcement authorities. This means that even if the enforcement authorities are not in a position now to identify a given violation, they may be in the near future.

In short, the importance of environmental legal issues in transactions is often underestimated. At the same time, these issues are fundamentally important to many foreign investors. This can cause a disconnect in risk assessment and difficulties in negotiations. But when environmental risks are identified at an early stage, this knowledge can be used as an argument in negotiations and in properly framing the transaction structure and documentation. This also helps avoid incurring additional, often significant, costs after the closing, or a claim by the acquirer that certain aspects of the transaction were not disclosed thoroughly enough.

Share deals

In share transactions, it is important to identify risks arising out of violation of environmental regulations because it enables an assessment of the potential sanctions that could be imposed on the entity or its managers for environment violations. Violations could result in imposition of financial sanctions, and in the case of environmental harm, a duty to remediate (restore the prior state), and in extreme cases the environmental compliance authorities may also issue a decision to shut down the operations of the business.

All of this will typically translate into major expenditures, impacting the financial condition of the acquired company. Failure to identify environmental compliance issues and address them in the transaction documents may result in the real value of the company whose shares are acquired being much less than the price established (or already paid) for the shares.

This issue may be depicted using the examples of risks arising out of improper waste management and risks arising out of failure to obtain required permits.

Improper waste management

The statutory model for waste management rules is complex, not very transparent, and subject to frequent changes. A business must comply with a large number of regulations spread across many different legal acts. This creates a risk of irregularities resulting in liability for improper waste management.

The most obvious examples would include situations in which a company conducts operations without a required permit or in violation of the terms of its permit. This may result in financial liability and in certain instances may also lead the environmental authorities to issue an order to shut down operations.

Another example of the risks connected with improper waste management has to do with the classification of substances or items. Businesses that produce or store certain substances or items often are unaware that they are classified as wastes. Doubts surrounding the definition of wastes increase the uncertainty in this area.

A final example of irregularities that may have major financial ramifications is neglect of requirements imposed on entities dealing in electrical and electronic equipment. The regulations lay down requirements that such equipment must meet before being introduced onto the market, as well as rules for handling such equipment when it becomes waste. Businesses operating in this area are often not in a position to properly assess which regulations apply to them or how they should comply with them. If they do not do so properly, they may face fines that go as high as PLN 500,000, depending on the degree of fault.

Failure to obtain required permits

Exploitation of the environment by business entities is regulated. This means that a business must often obtain permits specified by environmental laws or submit notifications to administrative authorities. Entities whose operations have significant impact on the environment are required to obtain an integrated permit.

Fines and increased fees will be imposed on businesses operating without obtaining a required permit or with a permit that is no longer valid. A permit may cease to be valid not only because the period for which it was granted has expired, but also for many other reasons. For example, a permit may expire as a result of failure to conduct operations for a certain period. A permit may be withdrawn in certain circumstances because of environmental violations, or invalidated because of gross errors in issuance of the permit. The latter risk is often overlooked, but practice provides numerous examples of decisions that were issued in violation of applicable law, for example by the wrong authority, without the proper wording, or contrary to statutory requirements.

Oftentimes an operator holding valid environmental permits will still face financial liability, particularly for failure to comply with the terms of the permits—for example by releasing substances different from those specified in a permit or in excessive quantities. A business may also face financial sanctions if, for example, it operates on the basis of a permit to discharge gas or particles into the atmosphere when under the environmental regulations it should obtain an integrated permit instead, or when it holds an integrated permit but it is no longer valid (e.g. as a result of improper assignment of the permit during an earlier transaction involving the installation for which the permit was issued).

If it is found in an inspection that the conditions set forth in a permit are being or have been exceeded, financial sanctions should be expected, and the amount of the sanctions will generally depend on the quantities of substances unlawfully released into the environment and the duration of the violation. In the worst case, the company may face withdrawal of the permit or shutting down of operations, which in practice may put the company out of business.

Asset deals

Asset deals present some of the most complex legal issues, particularly when they involve transfer of an enterprise. Some of the risks described in the section involving share deals should also be addressed in the transaction documents for an asset deal.

Asset deals require a particularly cautious approach, however, because it is necessary to reflect additional conditions that are specific to transactions of this type and which may have very serious consequences for the acquirer of the enterprise or specific assets if the risks are not identified.

An excellent example of the risks arising out of non-compliance with environmental regulations in asset deals is the issue of failure to make a proper assignment of rights and obligations under the administrative decisions under which the operations are conducted using the transferred assets. It should be borne in mind that under the administrative law governing issuance of environmental permits, the administrative authority controls the permit. Without the appropriate legal basis, the parties to the transaction may not decide by contract that the rights and obligations under the particular permit will pass to the acquirer of specific assets. Such provisions will not be effective, and the acquirer of the plant or installation will not become the holder of the permits for the facility in question.

It is somewhat simpler in the case of transactions involving transfer of an enterprise. The general rule is that the sale of an enterprise results in the acquirer's obtaining title to the assets that are part of the enterprise. There are numerous restrictions on transfer, however. With respect to rights and obligations under administrative decisions, such as decisions on environmental conditions, the regulations allow for only a limited ability for assignment to the acquirer of the enterprise. This means that administrative succession is the exception and requires an express legal basis.

Environmental harm

Regardless of whether the deal is for shares or assets, if it involves real estate one of the fundamental risks is environmental harm—such as soil contamination.

Analysis of this risk typically requires cooperation between lawyers and environmental consultants, as

well as particular caution. This is especially important with respect to harm to the earth's surface, i.e. contamination, as real estate is very often included in a transaction. But the risk is also material in the case of harm to water, protected species, or natural habitats.

Generally environmental harm is understood to mean any negative, measurable change in the condition or function of natural elements, compared to the prior condition, caused directly or indirectly by an entity exploiting the environment. This definition is narrowed down with respect to the specific natural element affected by the harm. For example, with respect to soil, it is accepted that there is harm when soil quality standards defined by regulation have been exceeded.

If harm occurs, then by operation of law the duty arises to remedy the harm. With respect to the surface of the earth, this means that if there is soil contamination, it is necessary to conduct reclamation. The costs of reclamation may be significant. In certain circumstances the environmental authorities may conduct remediation, whose costs can be great.

The entity required to conduct remedial measures is generally the entity exploiting the environment which caused the harm. With respect to certain types of harm to the surface of the earth, liability will be imposed on the owner of the real estate, regardless of whether or not the owner was the perpetrator of the harm. An acquirer of real estate may thus also acquire an obligation to conduct remediation, and often it might not be feasible to obtain reimbursement for reclamation costs from the person who caused the contamination. The owner of real estate may also be jointly and severally liable with the perpetrator for conducting remediation or covering remediation costs, if the owner knew of or consented to the contamination. Failure to conduct remediation may also entail criminal liability on the part of the persons required to conduct it (e.g. members of corporate management boards).

Due to the specific nature of environmental law, each transaction requires an individual approach in the analysis and assessment of the transaction's environmental risk as well as the proposed preventive measures to minimise the risk for the potential investor. In any event, it will be essential to address such risks in the transaction documents.

Employment law issues

Employment issues in M&A transactions should be considered separately for share deals (involving changes in partners or shareholders), and for asset deals (involving an enterprise, an organised part of an enterprise or other assets), which result in a change of the employer by operation of law.

Share deals

Share deals generally do not affect the employer's duties to the employees or the employment relationship in force between them, and do not entail the necessity to take additional actions with respect to employees.

If the employer joins a new capital group, however, that may make it necessary to carry out changes in the operations of the employer, the level of employment, or the organisation of the work in order to adapt them to the needs of the group or the rules in force within the group. Such measures may require notification and consultation with the works council (if appointed).

Under the Employee Notification and Consultation Act of 7 April 2006, the employer is required to provide the works council with information concerning the current situation of the employer: the employer's business and economic situation, the state and structure of employment, and actions planned for the future, i.e. anticipated changes in the employer's business and economic situation, changes in employment, measures intended to maintain the level of employment, and actions that may cause significant changes in the organisation of the work or the terms of employment. The employer is required to provide information to the works council on its own initiative of anticipated changes or intended actions, and at any time upon written request of the works council. If the works council and the employer have not specifically agreed on the procedures for information and consultation, it is assumed by analogy to regulations concerning transfer of the employment establishment that 30 days' advance notice to the works council concerning planned changes is sufficient.

Apart from the duties to provide information to the works council, in matters directly affecting employees, i.e. issues related to employment, terms of employment, and maintaining the level of employment,

and actions that may cause significant changes in the organisation of the work, the employer is required to consult with the works council. Share deals are rarely consulted with the works council, however, because the transaction documents hardly ever cover issues that require consultation. In practice, changes that require consultation typically happen after the share deal is over.

The consultation obligation is a duty to make best efforts—not to achieve a result. The employer is required to make every effort to reach agreement with the works council through dialogue and an exchange of views, but the parties are not required to agree on a common position on the matter. The purpose of consultations is for the employer to hear out the position of the employees' representatives and if possible reflect their position in its plans. As with the informational duties, the regulations do not provide a fixed timeframe in which consultations must be conducted, but only indicate that consultations should be conducted in a time, form and scope enabling the employer to act on the matters subject to consultation. This means that consultations should be conducted far enough in advance that the employer has an opportunity to modify its plans to reflect matters agreed on during the consultation process. In other words, changes should be consulted with the works council before implementation, not after the fact.

If as a result of a share deal any actions are to be taken that require notification and consultation with the works council, the transaction documents should include a statement by the seller concerning its compliance with these requirements.

Failure to comply with the requirement to notify and consult with the works council does not affect the transaction as such, but may subject the employer (as a rule, the management board) to punishment with probation or a fine.

Asset deals

Under Polish employment law, an asset deal generally results in passage of the establishment (or part of the establishment) to a new employer.

Under Labour Code Art. 231, passage of an establishment (or part of an establishment) results by operation of law in the new employer's assumption of

the rights and obligations of the former employer in relation to the acquired employees. Succession in employment relationships occurs automatically, regardless of the intentions of the employees or the opinions expressed by the employee representatives or any actions they may take with respect to transfer of the establishment.

Transfer of an establishment (or part of an establishment) may occur as a result of various legal events, including sale, conclusion or termination of a tenancy agreement, separation of the new establishment from the employer's organisational structure, conversion of a cooperative establishment into a separate cooperative, or—in certain circumstances—agreements transferring tasks and functions (e.g. outsourcing agreements).

1. Notice to employees/trade unions

Transfer of an establishment (or part of an establishment) entails a requirement to notify the trade unions operating at both the former and new employers, or if there are no trade unions, the employees. The notice should specify the anticipated date of the transfer and the reasons, as well as the legal, economic and social effects of the transfer for the employees, including the intended actions concerning the conditions of employment, pay, retraining and the like. If there is a change in the date of the transfer, the employer is required to notify the trade unions (or employees) of the new date. Notice of the planned transfer should be provided at least 30 days prior to the anticipated date of the transfer.

If the former or new employer does not intend to make any changes in the conditions of employment in connection with the transfer, once the requirement to notify the trade unions under Art. 261 of the Trade Unions Act of 23 May 1991 has been fulfilled, the employer has no further obligations to the establishment (or inter-establishment) trade unions in connection with transfer of the establishment.

However, if the employer does intend to make such changes, it is required to consult them with the establishment (or inter-establishment) trade unions. In this situation, consultations are obligatory if the planned changes are connected with the transfer of the establishment. Planned changes in the conditions of employment unrelated to the transfer of the

establishment do not constitute grounds for commencing consultations under the procedure provided in Trade Unions Act Art. 261.

The purpose of the consultations with the establishment (or inter-establishment) trade unions is to reach a collective agreement providing the rules for carrying out changes in the conditions of employment. This procedure is provided only for employers where establishment (or inter-establishment) trade unions are in operation. Staff at other employers are deprived of the opportunity of exerting an influence over the planned changes in the conditions of their employment, as the law does not provide for consulting them and reaching an agreement on such changes.

The agreement should be concluded within 30 days after the employer informs the establishment (or inter-establishment) trade unions of the planned actions. This period is only a guideline, and if it takes longer to reach agreement that will not affect the validity of the agreement.

The employer's failure to follow the procedure for consulting the transfer of the establishment with the establishment (or inter-establishment) trade unions does not invalidate the transfer to the new employer or its assumption of the employees. However, the individuals who were required to inform and consult with the trade unions due to the positions they hold are subject to sanctions in the form of a fine or probation.

Apart from notification of the employees or trade unions concerning the planned transfer of the establishment (or part of the establishment), as in the case of a share deal, employers may be required to inform and consult with the works council, if the transfer may affect matters that are subject to informing and consulting with the works council.

If as a result of an asset deal there will be a transfer of the employment establishment (or part of the establishment), it is reasonable to regulate in the transaction documents the scope of shared liability of the employers for claims of employees and obtain a statement by the seller concerning performance of the foregoing obligations under Labour Code Art. 231 or Trade Unions Act Art. 261 and the Employee Notification and Consultation Act.

2. Employers' liability to employees

The former and new employers are jointly and severally liable for obligations arising under the employment relationship prior to transfer of part of the employment establishment to the new employer. There are no specific regulations concerning joint and several liability of the former and new employers in the event of transfer of the entire establishment. It is accepted in the case law and the literature that an employer taking over an entire employment establishment is liable to the employees for new obligations as well as those arising prior to the transfer. However, this does not exclude the liability of the former employer for obligations arising prior to the transfer, under the principle of in solidum liability.

3. Work and pay conditions under internal regulations

Employees' entitlements arising out of their employment with the given employer are based not only on each employee's employment contract. Employees also have entitlements provided in the work rules, pay rules and collective agreements. Transfer of the employment establishment to a new employer under Labour Code Art. 231 does not, as a rule, result in the new employer's assumption of these internal regulations. Nonetheless, the employees will retain the entitlements they held thereunder up to the date of the transfer, generally until the terms of their employment are amended in this respect.

Enterprise collective bargaining agreement

Under Labour Code Art. 2418 §1, for one year following transfer of the employment establishment, the new employer is required to comply with the provisions of a collective bargaining agreement with respect to the assumed employees who were covered by the agreement at the time of the transfer. The new employer does not become a party to the collective bargaining agreement, but is bound by its terms.

The new employer may apply more favourable terms to the employees covered by the collective bargaining agreement than those arising under the existing arrangement.

When a year has passed following the transfer, the new employer is no longer required to comply with the collective bargaining agreement. However, the

individual employment relationships established by the provisions of the agreement remain in force until amended by a modifying notice or agreement.

Issues under finance and banking law

Existing debt/security interests

In order to obtain information about all security interests encumbering the assets of the company or its shares, it is important, in addition to obtaining statements from the seller, also to examine the relevant registers for intangibles and movables as well as the land and mortgage register for real estate.

From the buyer's point of view, it is particularly important to examine the pledge register in order to verify whether the shares or assets are subject to a registered pledge. If a registered pledge has been established and the pledge agreement prohibits sale of the asset, the sale will be invalid unless the buyer did not know and could not have known of the prohibition (which would be very unusual, since a prohibition on sale of a pledged asset is disclosed in the public pledge register).

As a result, failure to examine the register or obtain required consents or other statements may result in invalidity of the acquisition.

Share deal

In the case of a **share deal** it should be examined whether:

- The target company is a borrower or guarantor under a loan or credit agreement
- The assets or shares of the company are encumbered by security interests

Depending on the type of existing credit or loan agreement, and after the prospective buyer analyses its provisions (particularly the financial terms), the buyer and the seller will determine whether:

- The given financing will be continued, or
- The outstanding balance will be paid off by the buyer or the seller or refinanced by another bank

If the decision is to continue the financing, the specific provisions of the credit or loan agreement should be examined, particularly the borrower's rep-

resentations and warranties, as well as the circumstances constituting events of default, in terms of the feasibility of transferring the shares and operations of the borrower to a new capital group. (For example, the credit agreement may require that all the borrower's cash flows be conducted through the lender, but the acquirer's group may do business with a different bank.)

Of particular importance is the inclusion of any **change-of-control clauses**, and if so, the specific terms.

In consequence, prior to transfer of the shares it will sometimes be necessary to obtain consent to the transaction from the lender, or a waiver of certain rights under the credit agreement, or else amend certain provisions of the credit agreement.

When the financing is to be continued and there are encumbrances on the borrower's shares, it is important to make relevant modifications to the security instruments when the shares are transferred. It must also be determined whether there are any restrictions on sale and whether all consents required by the security instruments have been obtained.

If the decision is to pay off the outstanding borrowings of the target, the provisions of the credit or loan agreement concerning early repayment (e.g. with respect to fees and commissions) will be relevant, as will provisions concerning termination of the agreement (on notice or by agreement). An analysis of these aspects of the credit or loan agreement will enable the parties to prepare a repayment strategy before presenting the proposal to the lender.

From the buyer's point of view it is important to determine the conditions, and ideally the wording of the future declarations, with respect to repayment of obligations and release of existing security interests or confirmation that they have expired, as well as consent to deletion of the entry of the security interests from the relevant registers. Therefore prior to conclusion of the sale agreement, the buyer should obtain an undertaking by the lender to issue a release letter upon repayment (pay-off letter). The specific wording of the release letter including confirmation of repayment and expiry of the security interests is usually attached to the pay-off letter.

The type of security interest that is being released will determine the wording of the release letter. It is particularly important in the case of security based on disclosure in a register to assure that the security is precisely identified and that the release letter is worded correctly to enable deletion of the entry from the register.

The release letter should also contain an undertaking to return the original documents related to the principal forms of security, such as powers of attorney or declarations submitting to enforcement, and to prohibit the use of copies of such instruments.

Asset deal

In the case of an **asset deal**, first and foremost any security interests encumbering the acquired assets as a whole should be examined, as well as encumbrances on elements of specific assets (for example, the plant as such may not be encumbered but the production line may be subject to a pledge).

The wording of the release letter in this case is typically even more crucial than in the case of a share deal. Most often, because the secured claims are not being repaid, the release letter will not include provisions concerning expiry of the debt, but only a statement on waiver of the specific security interest.

From the seller's point of view, it is important to obtain the necessary consents and declarations from the lender for sale of the specific assets.

An exception to this structure in the case of an asset deal, closer to the structure described above, where the target is the borrower, is the situation where the seller's acquisition of the assets in question was financed by a bank or other specialised institution. In such case (if it is planned to pay down the existing claims of the target), the rules for repayment of the claims and the wording of the release letter should be similar to those described earlier.

Competition law issues

The main aspects of competition law applicable to M&A transactions — apart from **merger clearance by the competition authority** — concern contractual restrictions related to the transaction, particularly non-competition clauses and confidentiality

obligations. In other words, assuming that the concentration itself receives clearance, it then must be determined whether other restrictions on competition agreed by the parties are covered by the clearance or must be analysed and justified separately.

Permissible scope of restrictions on competition related to concentrations

Issues of contractual restrictions directly related and necessary to the implementation of concentrations—also known as “ancillary restraints”—are subject to self-assessment by the business entities involved. Polish competition law does not contain specific regulations in this respect. Therefore, under the practice followed by the Polish competition authority, the Office of Competition and Consumer Protection (UOKiK), in construing contractual provisions involving such restrictions businesses should rely on the approach adopted in European Union law.

European Commission guidelines

In order to provide legal certainty to businesses, the European Commission has issued guidelines for assessment of ancillary restrictions, entitled “Commission Notice on restrictions directly related and necessary to concentrations” (2005/C 56/03). Under the established practice, use of the EC guidelines is also accepted by UOKiK with respect to transactions that may cause effects in Polish territory.

Apart from contractual provisions concerning the main subject matter of the transaction, such as the transfer of the target's shares or assets, the parties to a concentration typically also agree on various other matters which are not an integral part of the concentration but may limit the freedom of the parties' behaviour on the market. Certain limitations agreed between the parties to an M&A transaction may be beneficial to both the seller and the buyer. As a rule, however, the acquirer has much greater need for additional assurances, because it must be certain that as a result of the transaction it will be in a position to exploit the full value of the acquired enterprise. Additional contractual provisions alongside the main transaction are thus typically aimed at protecting the value transferred, maintaining the continuity of supply, or enabling the start-up of a new entity.

Conditions for applying additional restrictions on competition in connection with the concentration

The restrictions agreed by the parties as part of an M&A transaction will be subject to the rules set forth in the Commission Notice only if they are directly related to the implementation of the concentration and necessary to the implementation (the merely subjective views of the parties in this respect are insufficient).

For restrictions to be considered directly related to the implementation of the concentration, they must be closely linked to the concentration itself. It is not sufficient that an agreement has been entered into in the same context or at the same time as the concentration. Restrictions that are directly related to the concentration are economically related to the main transaction and intended to allow a smooth transition to the changed company structure after the concentration.

In turn, agreements will be regarded as necessary to the implementation of the concentration if in the absence of those agreements the concentration could not be implemented or could only be implemented under considerably more uncertain conditions, at substantially higher cost, over an appreciably longer period or with considerably greater difficulty. In determining whether a restriction is necessary, it is appropriate not only to take account of its nature, but also to ensure that its duration, subject matter and geographical field of application do not exceed what the implementation of the concentration reasonably requires.

Non-competition clauses

The most frequently encountered restrictions related to concentrations involving acquisition of a business (in the form of shares, an enterprise or other assets, or other method of obtaining control over the target) are non-competition clauses imposed on the sellers. Such non-competition clauses guarantee the transfer to the purchaser of the full value of the assets transferred, which in general include both physical assets and intangible assets, such as the goodwill accumulated or the knowhow developed by the seller. These are directly related to the

concentration, but to be regarded as necessary to its implementation, their duration, geographical scope, subject matter, and the persons subject to them must not exceed certain reasonable limits.

Under the Commission Notice, non-competition clauses are generally justified for periods of up to three years following the transaction, when the transfer of the undertaking includes the transfer of customer loyalty in the form of both goodwill and knowhow. When only goodwill is included, they are justified for periods of up to two years. In exceptional, economically justified circumstances, longer periods may sometimes be acceptable.

The geographical scope of a non-competition clause must be limited to the area in which the seller has offered the relevant products or services before the transfer, but can be extended to territories which the seller was planning to enter at the time of the transaction, provided that it had already invested in preparing this move.

With respect to the subject matter, non-competition clauses must be limited to products and services forming the economic activity of the business transferred (including those at an advanced stage of development at the time of the transaction, or fully developed but not yet marketed).

The entities bound by a non-competition clause may include the seller, its subsidiaries, and commercial agents. Similar restrictions on others would not be regarded as directly related and necessary to the implementation of the concentration.

Other restrictions on competition

Clauses which limit the seller's right to purchase or hold shares in a company competing with the business transferred are permissible under the same conditions as for non-competition clauses. They may not, however, prevent the seller from purchasing or holding shares in competing companies purely for financial investment purposes (where the seller does not have a right, directly or indirectly, to exercise management functions or exert a material influence over the operations of the competing company).

The permissibility of non-solicitation and confidentiality clauses should be evaluated in a similar way to non-competition clauses.

Real estate issues

When selecting the form of the transaction, it is important to reflect the benefits or limitations connected with transactions involving real estate located in Poland.

Asset deal

In an asset deal, due diligence with respect to proper acquisition of title to real estate may be restricted to a review of the legal status disclosed in the land and mortgage register for the property, with the limitations described below. This results from the fact that an acquirer of real estate as part of an enterprise or organised part of an enterprise enjoys the protection of the warranty of public reliance on the land and mortgage register. A condition for functioning of the warranty of public reliance is that the transfer of ownership or other rights to the property is made to the acquirer by the person entered in the land and mortgage register as the holder. It should be stressed that the warranty of public reliance does not protect the acquirer of real estate or perpetual usufruct by way of universal succession. However, the predominant view in the current case law is that sale of an enterprise or an organised part of an enterprise constitutes the totality of the transactions concerning sale of specific elements of the enterprise; therefore there is no universal succession and the warranty of reliance on the register applies.

The principle of the warranty of public reliance on the land and mortgage register means that if there is a discrepancy between the legal status of the real estate disclosed in the land and mortgage register and the actual legal status, the content of the land and mortgage register will decide in favour of a person who acquired ownership or other *in rem* right to the property in a transaction with the person disclosed in the land and mortgage register as the rightful holder. It should be stressed, however, that data concerning the real estate that are included in the first section of the land and mortgage register are of an informational nature only (e.g. the area of the property) and are not subject to the protection of the warranty of reliance on the register. Thus, while a third party may have full confidence in the entry of the right and therefore effectively acquire the right from a person entered in the land and mortgage register, even if the seller is not the true holder

of the right, at the same time the acquirer may not have certainty with respect to the boundaries or area of the real estate it is acquiring. There is also no information in the register about the designated use of the property in the zoning plan, and in the case of perpetual usufruct there is no information in the register about the obligations under the contract delivering the land in perpetual usufruct. Therefore, it is very important to verify the parameters of the real estate to be acquired, based for example on information included in the register of plots and buildings, registers maintained by the public administrative authorities and the zoning plan, and, in the case of perpetual usufruct, to examine the contract, which is binding on the acquirer.

A real estate acquisition transaction is covered by the warranty of public reliance on the land and mortgage register if it occurs for consideration and the acquirer acts in good faith. An acquirer is regarded as acting in bad faith if it knows that the content of the land and mortgage register is inconsistent with the true legal status, or could easily determine this. It is accepted that the acquirer need not conduct a detailed inquiry in order to determine whether the listed owner of the property acquired it properly, or whether reprivatization claims have been asserted to the property. An ordinary degree of diligence is sufficient, meaning that the acquirer should review the content of the land and mortgage register and determine who is in possession of the property. The warranty of reliance on the register is excluded when there is a notation in the register concerning a motion with respect to the property, a challenge to a ruling by a referendary, an appeal or cassation proceeding, or a reservation with respect to the legal status reflected in the register.

There are certain exceptions from the warranty of public reliance on the land and mortgage register. It does not operate against rights that encumber the real estate by operation of law without an entry in the register, a life estate, servitudes established pursuant to a decision of a competent public administrative authority, servitudes for a necessary access road, or servitudes created by crossing a boundary in erection of a building or other installation.

Some courts had previously held that the warranty of reliance on the register does not operate with respect to acquisition of the right of perpetual usufruct

to real estate in the case of defective entry in the land and mortgage register of the State Treasury or local governmental unit as the owner of the land. Ultimately, however, the principle of security of legal transactions prevailed, and priority has been given to the warranty of reliance on the register.

A significant restriction that must be considered in an asset deal is the statutory right of pre-emption with respect to real estate, under which certain public entities are provided a right of priority to acquire real estate. When there is a statutory pre-emption right, it is necessary for the parties first to conclude an agreement promising to sell the property on condition that the holder of the pre-emption right does not exercise the right. The regulations and case law have not clearly resolved whether the statutory right of pre-emption applies to a transaction involving sale of an enterprise or organised part of an enterprise which includes real estate as an element. There are arguments for the position that the statutory pre-emption right does not apply because the subject of the pre-emption right and the subject of the transaction are different: the right of pre-emption concerns the real estate, while the sale agreement concerns an enterprise of which the real estate is only one element. However, given the established position of the courts treating sale of an enterprise as the sale of its specific elements and requiring application to the sale of an enterprise of statutory restrictions or exclusions with respect to the permissibility of transfer of specific elements of the enterprise, for the sake of safety it is better to reflect the statutory right of pre-emption in deals concerning assets or an enterprise (or organised part of an enterprise). If a sale agreement is concluded in avoidance of a statutory right of pre-emption, the sanction is the invalidity of the transaction.

Most frequently encountered in practice is a statutory right of pre-emption on the part of the local commune in the case of sale of undeveloped land previously acquired from the State Treasury or local governmental unit, or in the case of sale of the right of perpetual usufruct of undeveloped land regardless of the form in which the seller acquired such right. For example, there is a statutory right of pre-emption in favour of the Agricultural Property Agency in the case of the sale of agricultural land

and in favour of the Polish State Forests in the case of forest land. Similarly, the administrator of a special economic zone has a right of pre-emption with respect to ownership or perpetual usufruct of real estate located in the zone.

Agricultural real estate

New regulations entered into force on 30 April 2016 significantly limiting trade in agricultural real estate. Only agricultural property with an area of up to 0.3 hectare may be freely traded, as well as land designated for non-agricultural uses in the local zoning plan or decisions on construction conditions issued prior to 1 May 2016. In other instances, agricultural property may be acquired only by farmers operating a family farm (up to 300 hectares). There are only a few exceptions to this rule, not applicable to businesses. Where there is no zoning plan in force, a business cannot acquire a plot of agricultural land larger than 0.3 hectares, even if it is only a small part of a larger property that has no connection with agriculture. It is similar with the sale of plots of land: if there is no zoning plan, only an individual farmer can be the acquirer of an agricultural plot larger than 0.3 hectare, even if it is part of an industrial or commercial property.

Acquisition of agricultural or forest land in violation of the right of pre-emption referred to above is subject to the sanction of invalidity.

Share deals and other forms

In share deals, and generally in transactions involving merger, division or conversion of companies, acquisition of real estate will not be protected by the warranty of public reliance on the land and mortgage register. In a share deal the subject of the transaction is the shares in a company, and not the company's assets, including real estate. In the case of a merger, division or conversion of companies, the warranty of reliance does not function because the transaction involves acquisition of the assets as an entirety of rights through universal succession. Thus, in such transactions due diligence should include an assessment of the correctness of the acquisition of real estate.

On the other hand, the restrictions arising out of the statutory right of pre-emption will not apply in such transactions.

But if a company (other than a listed company) is the owner of agricultural real estate with an area greater than 0.3 hectare, which is not designated for non-agricultural use in the local zoning plan or a decision on construction conditions issued before 1 May 2016, then the Agricultural Property Agency has a right of pre-emption to the shares, regardless of the subject of the company's business.

Issues of administrative approvals

For purposes of this chapter, we understand “administrative approvals” to mean any and all types of consents, confirmations, authorisations, entries in registers, permits, licences or concessions issued by public administrative authorities, required for performance of a given type of economic activity or for performance of specific actions within economic activity, or to make specific use of certain assets.

The variety of administrative approvals required across specific sectors results from the specific types of activity and associated risks. It is generally accurate to say that the greater the risk associated with a given activity, the greater the regulation of the activity and the intensity of oversight of the activity by public administrative authorities.

For example, the following administrative approvals might be involved:

- Concessions, licences or permits for conducting specific types of:
 - Concession to conduct business involving production and trade in explosives, weapons, ammunition, and goods and technologies for military or police purposes
 - Concession to operate air transport
 - Permit to operate a public pharmacy
 - Licence to provide road transport
- Permits to conduct specific activities as part of economic activity:
 - Permit for production of strictly controlled medicinal products
 - Permit for retail sale of specific types of alcoholic beverages at a specific location
- Consent for specific use of assets:

- Approval of an establishment for specific food production
- Consent to operation of machinery and equipment subject to technical oversight
- Entries in register of regulated activity:
 - Entry in the register of healthcare entities
 - Entry in the register of telecommunications enterprises
- Other approvals
 - Permit to operate in a special economic zone

As a rule, administrative approvals are issued in the form of an administrative decision, i.e. an act addressed to a specific entity which is the applicant and a party to the administrative proceeding. The decision resolves the matter on the merits and rules on the applicant's rights and/or obligations.

Administrative decisions are not transferrable unless otherwise provided by a specific regulation. This rule is based on the construction under which an administrative approval is issued to a specific entity which has been checked by the administrative authority in subjective and objective terms and given a positive rating as an entity ensuring proper performance of the specific activity or action.

Usually, during realisation of the transaction, there is an expectation that the transaction will not in any way affect the uninterrupted operations (production) of the entities involved in the transaction, whether during the transaction or after the closing.

But because the rights obtained under administrative approvals are held by a strictly defined entity and are not subject to automatic transfer, it must be verified whether and when the future acquirer will obtain comparable rights in order to make full use of the acquired assets.

There is no one single rule concerning transfer and continuing validity of administrative approvals as a result of transactions.

To assess the risk connected with administrative approvals, it is necessary in each case to consult the regulations governing the specific approval, in light of the type of transaction planned. These regulations specify the situations in which the administrative au-

thority must, or has the discretionary right to, withdraw or limit the approval. If the transaction will give rise to circumstances which under the regulations provide a basis for withdrawal or limitation of the approval, that is an identified risk.

Share deals

The least transaction risk associated with administrative approvals will occur in M&A transactions involving a change in shareholders (share deal).

As a rule, the addressee of an administrative approval is a legal person, i.e. the company. The administrative approval confirms the company's right to conduct a specific type of activity or specific action.

Thus, most often, a mere change in shareholders, without disrupting the integrity of the company that is the addressee of the approval, will not affect in any the entitlement awarded to the company.

Sometimes, however, depending on the type of administrative approval, a share deal can potentially affect the continuation of the entitlement. This will occur in situations where the identity of the shareholder, its attributes or qualifications, are relevant to retaining the approval.

An example would be a concession for radio or television broadcasting, which may be withdrawn if a different person assumes direct or indirect control over the broadcaster; similarly with respect to a concession for production and trade in explosives, arms, ammunition, or goods for military or police uses. When seeking such concessions, a list of shareholders is submitted along with the other elements of the application. After obtaining the concession, the holder is required to notify the authority within 14 days of a change in the state of facts or law with respect to the information contained in the application for the concession and the documents enclosed with the application, arising after issuance of the concession. If the authority finds that the change in ownership on the part of the concession holder will impact state defence and security or the safety of citizens, it may withdraw the concession.

Asset deals

Risks connected with administrative approvals generally arise in connection with transactions involving

transfer of assets, an enterprise or an organised part of an enterprise.

In the case of sale of an enterprise, the enterprise is carved out of the assets of the company that is the addressee of the approval. If the enterprise includes concessions, licences or permits (Civil Code Art. 551), such approvals are subject to general succession. Thus the acquirer may apply to the administrative authority for issuance of the same concessions, licences or permits to the acquirer. The concessions, licences or permits issued in this manner will constitute a continuation of the original approvals, but reflecting the change in the identity of the holder.

A more difficult situation arises when the functioning of the enterprise requires approvals other than those expressly identified in the Civil Code as concessions, licences or permits. These could involve for example a decision by the sanitary inspectorate approving an establishment for food production, or a decision of the technical supervision inspectorate permitting operation of specific equipment, marketing authorisation for a medicinal product, or entry in the register of telecommunications enterprises. These approvals, unlike those listed in Civil Code Art. 551, will not be subject to general succession. In that situation, the acquirer of the enterprise will have to apply for issuance of an approval in its own name.

Corporate merger, division or conversion

In the case of a conversion of corporate form, the transfer of administrative approvals will work similarly as in asset deals.

Within general succession, administrative permits, concessions and allowances pass to the acquiring, newly formed or converted company under Commercial Companies Code Art. 494, 531 or 551, respectively. But the list of approvals subject to succession is limited to the permits, concessions and allowances and there is no basis for freely expanding this list.

This means that newly created entities will have to expect the need to apply on their own behalf for approvals required for their activity which cannot be obtained under the rule of general succession.



Legal restrictions in the transaction

Introduction

In many transactions, it is necessary to obtain various types of approvals or permits, the lack of which may even affect the validity of the entire transaction. These include corporate approvals in the form of resolutions from specific corporate authorities (such as the shareholders' meeting or the supervisory board), consent of third parties (e.g. creditors), and approvals from relevant government authorities (e.g. the Minister of the Interior and Administration).

The most frequently encountered types of approvals are discussed below, together with the procedures for obtaining them and the consequences if they are not obtained or are not issued properly.

Corporate and other internal approvals

In instances provided for in the Commercial Companies Code, it may be necessary to obtain corporate consent to dispose of:

- **Shares in a company** (limited-liability company or joint-stock company)
- **Certain assets of a company**

Corporate consent usually means consent to the company's carrying out a specific transaction, as expressed by the shareholders, or less often by the management board.

Transfer of shares

Under the Commercial Companies Code, the articles of association or statute of the company may include restrictions on a shareholder's freedom to dispose of its shares—specifically, a requirement to obtain the company's consent to the transfer.

It should be pointed out that the provisions calling for obtaining the company's consent to the transfer of shares (Commercial Companies Code Art. 182 for a limited-liability company and Art. 337 for registered shares in a joint-stock company) are **optional**, and these restrictions will apply only if provided for in the company charter (the articles of association of a limited-liability company or the statute of a joint-stock company).

This does not apply to registered shares which are tied to repetitive cash benefits (Commercial Companies Code Art. 356)—in that case the company's consent cannot be excluded.

In particular, these limitations consist in a possible requirement for the shareholder to obtain the company's consent to sale of shares, or—as is often encountered in practice—consent of the supervisory board or shareholders' meeting.

If disposal of share rights is conditioned on consent of the company, then, unless otherwise provided in the charter, the company's consent to disposal of shares is given in writing by the management board.

A share sale agreement concluded without the required consent is an ineffective (suspended) transaction, with respect to the company and between the parties. Such an agreement may become effective only when the required consent is provided.

Transfer of assets

M&A transactions, broadly speaking, may involve not only shares but also assets (particularly in the form of an enterprise or organised part of an enterprise, real estate, or individual assets), and thus it is important in every transaction to determine whether there are additional restrictions on disposal of specific types of assets.

These restrictions may be divided into those of **mandatory applicability** and those of **optional applicability** (that is, restrictions that may be opted out of, e.g. in the company charter).

The restrictions of mandatory applicability include:

- Sale, tenancy or encumbrance of the enterprise or an organised part of the enterprise (Commercial Companies Code Art. 228(3) or Art. 393(3), applicable to limited-liability companies and joint-stock companies, respectively)
- Acquisition by the company from a founder or shareholder, or a company or cooperative controlled by a founder or shareholder, of any assets for a price exceeding one-tenth of the paid-in share capital, within 2 years after the registration of the company (Commercial Companies Code Art. 394 §11—applicable only to joint-stock companies).

There is a requirement to obtain the consent of the company, but only if the articles of association or statute does not provide otherwise, in the case of:

- Acquisition or disposal of real estate, perpetual usufruct or a share in real estate (Commercial Companies Code Art. 228(4) for a limited-liability company or Art. 393(4) for a joint-stock company)
- Acquisition by the company of (i) real estate, (ii) a share in real estate or (iii) fixed assets at a price exceeding one-fourth of the share capital but no less than PLN 50,000, within 2 years after registration of the company (Commercial Companies Code Art. 229—applicable only to limited-liability companies)
- Disposal of a right or incurring an obligation with a value equal to more than twice the share capital (Commercial Companies Code Art. 230—applicable only to limited-liability companies).

Legal effects of failure to obtain consent

Under Commercial Companies Code Art. 17, the legal effects of failure to obtain corporate consent differ depending on whether the requirement arises from the code or from the company charter.

If the requirement to obtain consent for the given transaction arises directly from the law, carrying out the transaction without the consent results in the **invalidity** of the transaction. This applies to transactions where consent is mandatorily required (e.g. sale of the enterprise) as well as where the requirement may be opted out of in the articles of association or statute (e.g. with respect to sale of real estate).

However, if the source of the requirement to obtain consent to the transaction is only the company charter (for example, if the articles of association of a limited-liability company impose restrictions on incurring obligations above a certain value), an action carried out without the required consent is **valid**, but the members of the management board may be liable to the company for violation of the charter.

For the sake of legal certainty, if there is a requirement to obtain corporate consent, the buyer will typically require that the consent be presented prior to the closing. (Corporate consent in this context refers to consent for the company itself to take a specific act as a party to a transaction—a separate concept from the consent of the company, as the subject of a transaction, to disposal of its own shares.) However, under the Commercial Companies Code, as a rule, consent need not be provided prior to the transaction. Under Art. 17 §2, it should be provided **no later than 2 months** after the company carries out the transaction. However, for obvious reasons, it should not be expected that the other party will enter into the transaction without obtaining prior consent, where lack of consent will impact the validity of the transaction.

Notification of concentration to the president of the Office of Competition and Consumer Protection

The rules for oversight of concentrations in Poland are set forth in the Competition and Consumer Protection Act of 16 February 2007. The competent authority under the act is the president of the Office of Competition and Consumer Protection (UOKiK).

When is notification required?

Under the act, a concentration is defined as:

- The acquisition by one or more undertakings, by purchase of shares or other securities, or by any other means, of direct or indirect control of one or more other undertakings
- Creation by undertakings of a joint undertaking
- Merger of two or more undertakings
- Acquisition by an undertaking of part of the assets of another undertaking, if the turnover achieved through the assets acquired in Poland in any of the two financial years preceding the notification exceeded the equivalent of EUR 10 million.

An intended concentration is subject to notification of the president of UOKiK if the combined turnover achieved by all of the undertakings participating in the concentration in the financial year preceding the notification:

- Exceeded the equivalent of EUR 1 billion worldwide, or
- Exceeded the equivalent of EUR 50 million in Poland

The turnover relevant to determination of whether the basic criteria requiring notification have been met includes:

- In the case of a merger of two or more undertakings or creation of a joint undertaking by existing undertakings, the turnover of the capital groups of the undertakings participating in the concentration
- In the case of acquisition of control, the turnover of the capital group of the acquirer (the undertaking assuming control) and the turnover of the acquired undertaking and its subsidiaries (excluding the turnover of the seller's capital group)
- In the case of acquisition of a portion of the property of an undertaking (asset acquisition), the turnover of the acquirer's capital group and the turnover generated by the acquired assets.

Exceptions and exclusions from notification requirement

An intended concentration involving transfer of control is not subject to notification if the turnover in Poland of the undertaking (or undertakings) over which control will be taken (i.e. the target) did not exceed the equivalent of EUR 10 million in either of the two financial years preceding the planned transaction.

If the concentration involves acquisition of control over an undertaking or undertakings belonging to one capital group and simultaneous acquisition of a portion of the property of an undertaking or undertakings belonging to the same capital group, the concentration will be excluded from the notification requirement if the combined turnover of the undertaking (or undertakings) over which control is being acquired, as well as the turnover generated by the acquired assets, did not exceed the equivalent of EUR 10 million in Poland in either of the two financial years preceding the notification.

The intended concentration is excluded from the notification requirement in the case of:

- Intra-group transactions (within the same capital group)
- Temporary acquisition or taking up of shares in another undertaking by a financial institution with a view to reselling them within one year, provided it does not exercise the share rights (except concerning the right to dividends or in order to prepare for resale of the shares)
- Temporary acquisition or taking up of shares in another undertaking in order to secure debts (provided that share rights are not exercised during such time, except for rights enabling sale of the shares)
- A concentration occurring within a bankruptcy proceeding (except where the undertaking intending to acquire control or acquiring a portion of the assets) is a competitor or belongs to a capital group that includes competitors of the enterprise which is being acquired or whose assets are being acquired.

Cross-border transactions and notification obligation in Poland

Foreign transactions are subject to merger review in Poland if they will exert or could exert consequences in Poland. Under the official guidelines issued by UOKiK, a transaction may exert consequences in Poland if at least one of the participants in the concentration (or the capital group which it belongs to) generates revenue in Poland.

It should also be added that in the case of international transactions, particularly those involving or affecting a large number of entities from various countries, with significant turnover in EU countries, it may be necessary to notify the European Commission.

Proceeding before the president of UOKiK — issuance of consent to the concentration

The Competition and Consumer Protection Act provides for a **two-stage proceeding in merger control cases**. When the concentration is not particularly complicated, does not raise a reasonable probability of a significant limitation on market competition and does not require a study of the market, the proceeding should be completed within **1 month** after filing of the notification with UOKiK (first stage). But if the concentration is particularly complicated or shows a probability of significantly limiting competition, or if UOKiK finds that it is necessary to study the market, the president of UOKiK will issue an order extending the proceeding by **another 4 months** together with a justification (second stage). Such an order is unappealable.

If the applicant is summoned by UOKiK to cure defects in the notification or supplement the information (which happens relatively often), the statutory period for issuance of a decision in the first or second instance is extended by the time UOKiK spends waiting for the response to such additional questions.

The parties to a transaction that is subject to the notification procedure must refrain from carrying out the transaction until issuance of a decision by the president of UOKiK, or until the deadline for a ruling on the matter (i.e. five months plus any extra time the authority provides for submission of additional information or documents).

As part of the proceeding leading up to issuance of a decision permitting the concentration, the president of UOKiK will examine whether the concentration will significantly limit competition on the market. In cases where it is found that there is a reasonable probability of a significant limitation of market competition if the concentration is carried out, the president of UOKiK will present reservations with respect to the transaction to the undertaking(s) participating in the concentration. The reservations must be justified, and the undertaking(s) may respond to the reservations asserted within the established time. The authority may issue a decision prohibiting the concentration only if the concentration would significantly limit competition, meaning more specifically the creation or strengthening of a dominant position on the market. If the planned transaction raises serious concerns under competition law, the authority may establish conditions that must be fulfilled by the parties in order to obtain consent to the concentration.

Issues related to the interim period

When the intended concentration requires notification, the transaction is typically divided into two stages. The first is the signing, in which the parties enter into a preliminary or conditional agreement. The second stage, the closing, occurs after successful completion of the proceeding before the competition authority.

Regardless of the construction adopted for the transaction, separating it into stages means that there will be an interim period between the signing, after the parties have negotiated the terms of the deal, and the closing, when the target will pass to the acquirer. During the interim period, the acquirer formally has no influence over the target (and cannot, for example, conduct the affairs of the target or otherwise manage it), but on the other hand the acquirer wants to be sure that when the target is delivered its condition is no worse than it was at the signing.

In consequence, in order to secure the interests of the acquirer, it is crucial to include appropriate provisions in the transaction documents governing the operations of the target during the interim period, in compliance with competition regulations.

Consent of the Minister of the Interior and Administration

Under the Act on Acquisition of Real Estate by Foreigners of 24 March 1920, acquisition by a foreigner of real estate or the right of perpetual usufruct of land in Poland, or rights to shares in a Polish company that is the owner or perpetual usufructuary of real estate in Poland, or acquisition of an enterprise or an organised part of an enterprise including such assets, requires a permit.

The competent authority for issuance of a permit under the act is the Minister of the Interior and Administration (MSWiA).

Transactions requiring a permit from MSWiA

A permit from MSWiA is generally required for a transaction involving:

- Acquisition or taking up of shares by a foreigner in a commercial company with its registered office in Poland, or any other transaction involving the shares, when the company is the owner or perpetual usufructuary of real estate in Poland, and:
 - As a result of the transaction the company will become a “controlled company” (i.e. controlled by a foreigner), or
 - The company is a controlled company but the shares will be acquired by a foreigner who is not already a shareholder of the company; or
- Direct acquisition by a foreigner of real estate or perpetual usufruct of land in Poland:
 - As part of the acquisition of an enterprise or organised part of an enterprise, or
 - Through universal succession in connection with merger or division of commercial companies

For purposes of the Act on Acquisition of Real Estate by Foreigners, a “foreigner” is defined as:

- A natural person without Polish citizenship
- A legal person with its registered office outside Poland

- A partnership of such persons without legal personality, established under foreign law
- A legal person or commercial company without legal personality (i.e. partnership) with its registered office in Poland, controlled directly or indirectly by the persons or companies referred to above.

Acquisition of shares by a foreigner in violation of the act is **invalid**.

No obligation to obtain permit

The obligation to obtain a permit to acquire real estate or shares **does not apply** to foreigners who are citizens or undertakings from:

- Member states of the European Economic Area, or
- Switzerland

unless the real estate is located in a border zone.

The period during which foreigners from these countries had to obtain consent to acquire agricultural or forest land expired on 1 May 2016. However, in acquiring such real estate, they are now subject to the general limitations connected with the right of pre-emption introduced from 30 April 2016.

Restrictions on transactions in strategic sectors

Notification of oversight authority (for strategic company)

In transactions involving companies operating in strategic sectors of the economy, it must also be examined whether the Act on Oversight of Certain Investments of 24 July 2015 is applicable.

The act requires notification of the oversight authority (currently the minister responsible for the Treasury, or with respect to energy companies, the Minister of Energy) of an intended transaction which the authority may object to.

What entities are subject to protection?

The Act on Oversight of Certain Investments introduces special restrictions on acquisition of shares or enterprises belonging to “protected entities.” The list of these entities is set forth in a regulation of the

Council of Ministers. It includes companies operating in key sectors of the economy (e.g. telecommunications, energy, chemicals, and defence) which require special protection in light of their significant market share, scale of operations, and fundamental interest to society.

Significantly, a protected entity need not be controlled by the State Treasury, but can be a private company.

Thus if a transaction involves companies operating in the industries indicated in the act, whether the entity is protected should be verified at each stage of the transaction, as the regulations issued by the government under this act have generally entered into force the day after publication in the Journal of Laws.

When does the oversight authority have to be notified of a transaction?

The duty to notify the oversight authority applies to asset deals and share deals resulting in:

- Acquisition or achievement of a major stake, meaning acquisition of rights enabling exercise of 20%, 25% or 33% of the votes at the meeting of shareholders, or acquisition of the enterprise or an organised part of the enterprise of a protected entity, or
- Acquisition of control, understood to mean reaching or exceeding 50% of the votes in the authority establishing the entity or in its share capital, by acquiring or taking up shares or rights to shares

The act also applies to indirect acquisition (e.g. by a subsidiary) or secondary acquisition (e.g. as a result of division or merger of a protected company or redemption of its shares).

Proceeding before oversight authority

The intention of carrying out a transaction resulting in acquisition or achievement of a major stake or control of a protected entity must be notified in each instance to the oversight authority.

The notification must generally be submitted before taking any action resulting in acquisition or achievement of a major stake or control, that is, before conclusion of the agreement on sale of the shares or the

enterprise, or before the meeting of shareholders is held to adopt a resolution on increase of the share capital or merger of the companies.

The required content of the notice is set forth in the act. Apart from a description of the transaction subject to notification, detailed information about the entity filing the notice must be provided, such as:

- A description of its economic activity (nature, location and history)
- Information about the education held by the persons who are members of the management and supervision authorities (or the applicant himself, if it is an individual)
- Information about the capital group which the applicant belongs to (or if the applicant is not a commercial company, information about the entities entitled to decide on the membership of its management and supervision authorities, entities entitled to receive distributions from its assets, and entities entitled to receive its assets in the event of dissolution or other termination of its existence)
- A description of its economic and financial condition
- A description of the applicant's intentions with respect to the protected company, in terms of investment plans, long-term operating plans, anticipated changes in organisation, in particular any mergers, the financing of its operations, dividend policy and employment policy.

The oversight authority has 90 days to consider the notification and issue a decision objecting to the transaction. In practice, this period can be prolonged significantly, as the authority may summon the applicant to submit additional information.

The authority will issue a decision objecting to the transaction where justified by one of the following considerations:

- Ensuring protection of independence and territorial integrity, human and civil rights and freedoms, safety of citizens, or environmental protection
- Preventing actions or social or political phenomena preventing or hindering performance of NATO obligations

- Preventing actions or phenomena that could interfere with foreign relations
- Ensuring public order and state security, and meeting essential needs for protection of human life and health

or if the applicant failed to cure formal defects in the notification or failed to submit additional written information within the time specified by the authority.

Actions taken contrary to an objection by the authority, or without filing the notification, are invalid.

In addition, failure to file notification is subject to a fine of up to PLN 100 million. This fine may be imposed not only on the entity required to file the notification, but also on persons carrying out the transaction for the entity (management board members, proxies). These individuals may also be sentenced to up to 5 years' imprisonment.

Change-of-control clauses

One of the key issues that require close attention by the acquirer at the due diligence stage and during negotiation of the transaction documents is the ability to transfer the target's contract rights to the acquirer.

Commercial contracts (e.g. cooperation agreements, licences for key technology, etc.) and agreements with financial institutions (credit for financing operations, leasing agreements and the like) are often elements of the target essential for its continued uninterrupted functioning, and thus the issue of effective assumption of rights under such contracts is crucial to the investor.

In the case of a transaction involving acquisition of shares, the issue of the change in the parties to contracts does not arise. Thus contract provisions that prohibit assignment of rights under contracts do not apply to share deals. Nonetheless, even though the identity of the parties to the contract does not change as a result of the transaction, when a capital group sells shares in a subsidiary to another group, in practice this results in a change in control of the target—something which the other party to the contract may care about strongly.

Thus parties will often include change-of-control clauses in contracts, governing issues of the parties'

mutual rights and obligations in the event of a change in the ownership structure of one or both of them. Most often such clauses include provisions under which a change in the ownership structure of a party requires consent of the other party, or entitles the other party to terminate the contract early. Clauses of this type are routinely included in agreements with banks and other financial institutions.

Change-of-control clauses often arise out of connections with larger capital structures (holding companies, capital groups or the like). Consequently, membership in such a structure may also be a condition for maintaining or breaking off commercial relations with a given entity. Membership in a group may give the other party an additional guarantee of reliability or solvency. Conversely, acquisition of the other party by a competitor of the other party obviously might justify a decision to end the cooperation immediately.

Regulations under Polish law

Change-of-control clauses are not specifically regulated under Polish law, but the permissibility of their use may be clearly inferred from the principle of freedom of contract set forth in Civil Code Art. 3531.

Because the concept of “change of control” is also not defined in Polish law, the wording of the clause itself will be of key significance.

Under Polish law, a change-of-control clause may be interpreted under Civil Code Art. 353 §2 as an undertaking by a party to act or refrain from acting, i.e.:

- To notify the other party before or after the fact of a change in its ownership structure (involving acquisition of control over it by a third party), or obtain prior consent to such a change from the other party, or
- Not to make changes involving control over the party without notifying or obtaining the consent of the other party.

If the parties did not define the concept of change of control in the agreement, it is necessary to interpret the concept under Civil Code Art. 65 and determine the meaning the parties would have assigned to it. For this purpose, reference may be

made to other definitions used in Polish law in relation to concepts of control, particularly under corporate law, competition law and securities law.

Content of change-of-control clauses

In order to avoid ambiguity or the need to interpret a change-of-control clause, it is beneficial for the parties to specify by contract what circumstances they regard as change of control. In commercial practice, several types of change-of-control clauses may be distinguished.

The parties may agree that the clause will cover both a direct change in control, involving acquisition of shares in the company that is a party to the contract, and an indirect change, where the ownership of the parent company changes.

A change-of-control reservation may apply to sale of shares to a third party (not previously a shareholder) and to sale to a current shareholder (e.g. in the event of a transaction between shareholders).

Moreover, the clause may contain provisions excluding or limiting its use, e.g. providing that sale of shares to specifically identified entities or within a specific period will not be regarded as a change of control.

The parties may also agree that while neither party may transfer its shares without consent of the other party, consent may not be refused without serious grounds.

Finally, the essence of the clause is the consequences provided for breach of the clause. Most often it is provided that a change of control in violation of the clause entitles the other party to terminate the agreement without prior notice or on very short notice, or may, for example, expose the breaching party to a contractual penalty.

Given the possible sanctions for violating change-of-control clauses, such as loss of valuable contracts or acceleration of repayment of credit, it is in the interest of the acquirer of the shares to perform a due diligence review of commercial agreements to which the target is a party, prior to the transaction.

Other restrictions

In addition to the requirements to obtain consent from the company, administrative authorities or

third parties, there are several additional issues to be considered in the case of transactions involving individuals.

Consent of spouse

It is generally in the interest of the other party to the transaction to obtain consent from the spouse if:

- A party to the transaction (either the seller or the buyer) is a married individual, and
- The subject of the transaction (if the individual is the seller) or the funds applied to the purchase price (if the individual is the buyer) are part of the joint marital assets of the party and his or her spouse

Unfortunately, the buyer has a very limited possibility of determining or verifying on the basis of documents provided by the seller what is the seller's marital status and whether the given transaction requires the consent of the seller's spouse. Thus it is reasonable to expect that the seller will provide representations and warranties in the sale agreement with respect to the seller's marital status, and if the seller is married, also concerning the nature of the marital property regime observed by the couple.

In the case of an **asset deal**, particularly where the subject of the transaction is an enterprise or real estate, under Art. 37 §1 of the Family and Guardianship Code the lack of spousal consent may result in the invalidity of all or part of the transaction.

With respect to a **share deal**, consent of the spouse is not a condition for the validity of the transaction, but it should be pointed out that lack of such consent may significantly impede or prevent altogether enforcement of claims against the spouse who is a party to the transaction (e.g. for contractual penalties in the sale agreement or warranty claims for defects). This results from limitations on satisfying claims out of the joint assets of spouses where one spouse incurs an obligation without the consent of the other spouse, as specified in Family and Guardianship Code Art. 41.

The consent by the spouse generally requires the same form as that provided for the transaction affected by the consent. In order to avoid doubts as to the authenticity of the consent, however (i.e. to be sure it is given by the right person), it is in the

interest of the other party to the transaction for the consent to be issued in all cases in a form at least as rigorous as a notarised signature.

Under Family and Guardianship Code Art. 38, a transaction concluded with an individual involving assets or rights specified in Art. 37 §1 will be effective notwithstanding the lack of spousal consent if the other party acted in good faith (e.g. did not know and could not have known that the party was married). Regulations concerning protection provided to a good-faith purchaser (Civil Code Art. 169 ff.) will apply as relevant.

It should also be pointed out that if consent of the seller's spouse is not obtained, the buyer's enforcement of claims against the seller (e.g. for contractual penalties provided for in the sale contract or claims for warranty for defects in the subject of the transaction) can be rendered difficult or impossible. This is because of the limitations provided in Art. 41 §2 of the Family and Guardianship Code on satisfaction out of the spouses' joint marital property of an obligation incurred by one spouse without the consent of the other spouse.

Consent of co-owner

When shares or assets are acquired from individuals, it often happens that there are two or more co-owners authorised to dispose of the property. This is particularly the case where they inherited the property but did not divide the property or eliminate co-ownership.

In this situation, Civil Code Art. 199 is relevant. It provides that disposal of jointly owned property requires the consent of all of the co-owners.

If all of the co-owners do not appear at the signing of the transaction documents, it is necessary to obtain their prior consent to dispose of the joint property. Such consent should be given in a form at least as rigorous as that provided for the agreement trans-

ferring ownership of the property (e.g. with notarised signatures in the case of transfer of shares in a limited-liability company, or in the form of a notarial deed if the transaction involves real estate).

To avoid doubts or potential future disputes concerning the target and the effectiveness of the acquisition, it is in the interest of the buyer to assure that the consent reflects as fully as possible the terms agreed between the parties, particularly that the consent clearly indicate the buyer and the main terms under which the transaction is to be carried out (particularly the price).

Estate and gift tax

In addition to the issue of co-ownership of the property, particularly when the seller is an individual and the transaction documents are to be made with notarised signatures or in the form of a notarial deed, it is crucial to pay attention to Art. 19(6) of the Estate and Gift Tax Act of 28 July 1983.

Under this act, if the subject matter of the act in which a notary participates involves inter alia disposal of property obtained through inheritance, gift or bequest, the notary may conduct such activity only after the notary has first been presented with:

- Written consent of the head of the tax office, or
- A certificate issued by the head of the tax office confirming that (i) the acquisition was free of tax, (ii) the tax due was paid, or (iii) the tax obligation is time-barred

The foregoing list of consents and formalities required for the effectiveness of transactions is not intended to be exhaustive. In addition to the issues addressed above, under the specific conditions of the given transaction it may be necessary to comply with other requirements under generally applicable law, as well as contractual or organisational requirements.



Tax aspects of the transaction

Introduction

Sources of tax law in Poland

As a member state of the European Union, Poland is required to apply EU law. Some EU regulations are applied in Poland directly while others are implemented within the Polish legal system.

Among the taxes of particular transactional importance, the most far-reaching harmonisation has occurred with respect to VAT.

EU law also has a major impact on income taxes and indirect taxes other than VAT, including capital duty or indirect taxes on raising capital (in Poland, the tax on civil-law transactions functions as a form of capital duty). Based on EU directives, tax neutrality has been introduced in Poland, upon fulfilment of certain conditions, with respect to dividends paid or received, under the Parent-Subsidiary Directive (90/435/ECC), as well as the possibility of exemption from withholding in Poland on interest and royalties paid abroad to certain related entities under the Interest and Royalties Directive (2003/49/EC).

Another result of implementation of EU law in Poland is the introduction of solutions that enable tax-neutral treatment of restructuring transactions, such as corporate mergers, divisions and conversions, under the Merger Directive (2009/133/EC) and Council Directive 2008/7/EC of 12 February 2008 concerning indirect taxes on the raising of capital.

Tax interpretations in transactions

Interpretations issued by the tax authorities as well as rulings in tax cases issued by the administrative courts are of great importance in the process of interpreting and applying tax law. While it is true that in the Polish legal system tax interpretations and ju-

dicial rulings do not constitute a source of universally binding law, they nonetheless have an impact on how the law is applied by the tax authorities and by taxpayers—particularly in the case of judgments and resolutions issued by the Supreme Administrative Court.

Given the high degree of complexity of tax regulations, the frequent problems in their interpretation and application, and the potentially significant risks associated with improper application, the Tax Ordinance in Poland provides for issuance of interpretations of tax regulations (including tax treaties).

There are two types of tax interpretations: general interpretations, issued by the Minister of Finance, which are generally addressed to the tax authorities and are designed to unify the application of tax regulations, and individual interpretations, issued upon application of the interested parties (tax payers, remitters or collectors as well as entities that may potentially be required to pay tax). Individual interpretations are technically issued by the Minister of Finance, but the minister has authorised five directors of tax chambers to issue them. An exception to this system is individual interpretations concerning local taxes (e.g. real estate tax), which are issued by the local tax authorities. Authorities issuing interpretations are required to publish them online (with identifying details of the taxpayers redacted).

The procedure for applying for an individual interpretation is fairly cheap and simple, and provides a high degree of security if the party follows the interpretation. For this reason, tax interpretations have become a commonly used tool for managing tax risk in Poland. In the case of complex, multifaceted transactions which may also entail major tax exposure, applying for a tax interpretation is often

standard operating procedure for the parties prior to carrying out the transaction.

The process of obtaining a tax interpretation begins with drafting the application, in which the applicant describes the planned transaction or event, formulates its query concerning the tax effects of the transaction or event, and presents its own position on the tax effects of the transaction or event. When the interpretation is issued, it will state that the applicant's position is correct or incorrect, generally with a justification. The interpretation may be challenged by the party, first by calling on the authority issuing the interpretation to correct the legal errors in the interpretation, and then through the administrative courts.

An interpretation should be issued within 3 months after receipt of the application, but this deadline may be extended when the tax authority requests additional information concerning the application. The application bears a fee of PLN 40 (about EUR 10) for each state of facts or future event.

Individual interpretations are binding on the tax authorities, which means that an entity that follows an interpretation it has received concerning a future event cannot bear negative consequences if the interpretation is later found to be incorrect. More specifically, if the interpretation is later held to be incorrect, the taxpayer is not required to pay tax or interest. This protection also means that the authorities are not permitted to commence fiscal penal proceedings, and proceedings that are commenced should be dismissed. However, if the interpretation concerns events or transactions occurring before issuance of the individual interpretation (rather than a future event), the taxpayer is not released from paying the tax.

This protective function of individual tax interpretations is excluded if the decision is issued as a result of application of the general anti-avoidance rule. This now effectively limits the role of individual interpretations in tax planning. It should be stressed that the Minister of Finance is authorised to amend a general or individual interpretation that has been issued if he finds that the interpretation was unlawful. In such case, however, a taxpayer who followed the interpretation before it was amended will not

suffer negative consequences because of the amendment.

Tax avoidance

A general anti-avoidance rule was introduced into the Polish tax system on 15 July 2016. Under Art. 119a of the Tax Ordinance, an action made primarily with the aim of achieving a tax advantage (that is, an action in which the economic or commercial aims are of little importance), inconsistent in the given circumstances with the subject and aim of a tax regulation, will not achieve the intended tax advantage if the manner in which the action was taken was “artificial.”

The manner in which an action is taken is regarded as artificial if it would not have been applied by an entity acting reasonably, guided by lawful aims other than achieving a tax advantage inconsistent with the subject and aim of a tax regulation. In determining whether an action was artificial, the particular factors to consider include the involvement of intermediaries without economic or commercial justification, and an economic or commercial risk outweighing the anticipated non-tax benefits to a degree that a rationally acting entity would not have chosen to act in that manner.

In this situation, the tax consequences of the action are determined on the basis of the state of affairs that would have existed if the entity had acted reasonably in the situation, guided by lawful aims other than achieving a tax advantage inconsistent with the subject and aim of a tax regulation. But if achievement of a tax advantage was the only aim of the action, the tax consequences are determined on the basis of the state of affairs that would exist if the action had not been taken.

Considering the vagueness of the concepts used in the Tax Ordinance, it can be expected that not only actions aimed exclusively at tax optimisation will be questioned, but also actions with a business rationale if their form does not result in maximisation of tax burdens. To eliminate this risk, an application can be filed with the Minister of Finance for issuance of a “precautionary opinion.” The application includes a detailed description of the transaction, an indication of the entities participating in the transaction, including the capital or personal ties between them,

and an indication of the aims and economic or commercial justification for the transaction. The application should also contain a description of the tax consequences, including the tax advantages, that will be achieved as a result of the transaction, along with the applicant's position on the matter.

A precautionary opinion should be issued within 6 months after receipt of the application (this period may be extended if the Minister of Finance submits additional questions to the applicant concerning the transaction). The cost of issuance of the opinion is PLN 20,000 (about EUR 5,000).

In cases in which the anti-avoidance rule may be invoked, the proceeding is conducted by the Minister of Finance. During the course of the proceeding, the minister may at his own initiative (before issuance of a decision) or at the request of the taxpayer (in its appeal from the decision) seek an opinion from the Tax Avoidance Council on the justification for applying the anti-avoidance rule. Before the council issues an opinion, the taxpayer may submit additional documents to the council and presents its position in writing. The council is an independent body whose members are appointed by the Minister of Finance for a 4-year term.

The Polish tax authorities may also dispute transactions under Art. 199a of the Tax Ordinance if they can prove that the given right or legal relationship from which a party derives tax effects is non-existent (that is, did not occur). If the tax authorities have doubts with respect to the existence of a legal relationship or right, they should seek a declaratory judgment to that effect from the common court.

Share deals

Corporate income tax effects

Under the Corporate Income Tax Act of 15 February 1992, expenditures on acquisition of shares are not deductible as revenue-earning costs at the time of acquiring or taking up the shares. Such expenditures may be recognised as revenue-earning costs only upon sale of the shares. Shares that are held by the taxpayer are also not subject to amortisation.

When a company sells shares it holds, it is required to pay CIT on the income earned from sale of the shares, calculated as the difference between the revenue obtained from sale of the shares (typically the

sale price) and the revenue-earning costs, which generally include the expenditures incurred in acquiring or taking up the shares, i.e. the purchase price for the shares plus expenditures directly related to the acquisition, such as notary fees, brokerage fees and the like.

There are special rules for calculating revenue-earning costs in the case of sale of shares that were taken up in exchange for an in-kind contribution. In such case, the method for recognising revenue-earning costs depends on the subject matter of the in-kind contribution (i.e. whether it was in the form of an enterprise or organised part of an enterprise, or in some other form).

Income from the sale of shares is taxed according to general rules at the CIT rate of 19%.

If the seller of the shares does not have Polish tax residency, the income from sale of the shares may be taxed in Poland only if the income is deemed to be earned in Poland. Effective from 1 January 2017, the CIT Act provides that income from the sale of shares on the Warsaw Stock Exchange is deemed to be earned in Poland. Income from transfer of title to shares in a company in which at least 50% of the value of the assets, directly or indirectly, constitutes real estate located in Poland or rights to such real estate is also deemed to be earned in Poland.

The rules for taxation of income earned on the sale of shares by such persons are then analogous to those applicable to persons with Polish tax residency, except as modified by applicable tax treaties.

Typically the tax treaties to which Poland is a party provide that income from the sale of shares may be taxed only in the country in which the seller has its residence, registered office or management. An exception is tax treaties containing a real estate clause, permitting Poland to tax the income on the sale of shares in companies whose principal assets are made up of Polish real estate (for example, the tax treaty between Poland and Germany).

Effect for purposes of indirect taxes (VAT, transaction tax)

Sale of shares in a limited-liability company or joint-stock company is generally not subject to VAT.

Sale of shares in a Polish limited-liability company or joint-stock company is subject to the tax on civil-

law transactions at the rate of 1% of the market value of the shares. The taxpayer is the acquirer of the shares. However, there is an exemption from transaction tax for sale of shares in a Polish joint-stock company:

- To domestic or foreign investment firms
- Via domestic or foreign investment firms
- In organised trading, or
- Outside organised trading, by domestic or foreign investment firms, if they acquired the shares in organised trading.

Asset deals

Definition of an enterprise and an organised part of an enterprise

Correct classification of the subject of the transaction (i.e. as an enterprise or organised part of an enterprise or as specific assets) is of decisive importance for proper determination of the tax effects of an asset deal.

The tax regulations do not contain their own definition of an enterprise, and thus the provisions of the Civil Code are applied in this respect, under which an enterprise is an organised set of tangible and intangible assets intended for conducting business activity.

The concept of an organised part of an enterprise is defined in the tax regulations as an organisationally and financially distinct set of tangible and intangible assets within an existing enterprise, including liabilities, intended for carrying out specific economic purposes, which could also constitute an independent enterprise carrying out such purposes.

In practice, determining whether the specific subject of the transaction constitutes an enterprise or organised part of an enterprise may raise numerous doubts, which are exacerbated by the unclear and conflicting interpretations issued by the tax authorities. For this reason, transactions of this type should be preceded by a detailed legal and tax analysis to determine whether the assets in question meet the definition of an enterprise or organised part of an enterprise, particularly when certain assets (such as real estate, liabilities, etc.) are being excluded from the transaction.

Sale of a set of assets and liabilities that do not meet the conditions for recognition as an enterprise or organised part of an enterprise will be treated for tax purposes as the sale of specific assets, even if they are sold within a single transaction.

Sale of an enterprise or organised part of an enterprise

1. Corporate income tax effects for the seller

Income generated as a result of sale of an enterprise or organised part of an enterprise is subject to taxation under general rules at the CIT rate of 19%. The income is the difference between the revenue from sale of the enterprise or organised part of an enterprise and the book value (In the case of fixed assets and intangibles, this is the initial basis as reduced by amortisation; in the case of other assets, this is most often the acquisition cost).

The revenue from sale of an enterprise or organised part of an enterprise is generally the sale price, provided that it should be determined at market value. For this reason it is recommended to obtain an independent appraisal confirming that the sale is made at market value (in case of a potential dispute with the tax authorities).

2. Corporate income tax effects for the buyer

Acquisition of an enterprise or organised part of an enterprise may generate goodwill, which is the excess of the purchase price for the enterprise or organised part of an enterprise over the market value of its assets. Goodwill is subject to amortisation.

If goodwill is generated, the initial tax basis of the acquired assets making up the enterprise or organised part of an enterprise is established for purposes of amortisation at their market value. Otherwise, the initial tax basis will be the purchase price minus the value of assets included in the enterprise or organised part of an enterprise that are not subject to amortisation as fixed assets or intangibles.

3. Indirect taxes (VAT, transaction tax)

Sale of an enterprise or organised part of an enterprise is not subject to VAT.

Sale of an enterprise or organised part of an enterprise is subject to the tax on civil-law transactions under general rules, i.e. the sale of each asset in-

cluded in the enterprise or organised part of an enterprise is subject to tax (at 1% or 2% of the market value, depending on the type of asset). The taxpayer is the acquirer of the enterprise or organised part of an enterprise.

4. Liability of acquirer of enterprise or organised part of enterprise

The acquirer of an enterprise or organised part of an enterprise is jointly and severally liable with the seller for the seller's tax arrears arising through the date of acquisition in connection with business operations, but the acquirer's liability is limited to the value of the enterprise or organised part of an enterprise acquired.

In order to limit or exclude the liability of an acquirer of an enterprise or organised part of an enterprise, it is possible to obtain a certificate stating the amount of the seller's tax arrears (following the procedure set forth in Tax Ordinance Art. 306g). The acquirer will then not be liable for tax arrears of the seller that were not indicated in the certificate. However, if the sale of the enterprise or organised part of an enterprise occurs more than 30 days after issuance of the certificate, the acquirer may be liable for the seller's tax arrears arising after issuance of the certificate.

Sale of assets

1. Corporate income tax effects for the seller

Income from the sale of assets is subject to taxation under general rules at the CIT rate of 19%. The income is the difference between the revenue from sale of the assets and the tax basis in the books (the initial basis as reduced by amortisation).

The revenue from the sale of assets is generally the sale price, provided that it should be determined at market value. For this reason, in the case of transactions at a significant value, it is recommended to obtain an independent appraisal confirming the sale price is at market value (in the event of a potential dispute with the tax authorities).

2. Corporate income tax effects for the buyer

Goodwill cannot be generated in the case of the sale of specific assets. The acquired assets are generally subject to amortisation if their initial basis exceeds PLN 3,500. In the case of assets with a lower initial

basis, the expenditures for acquisition of the assets may be recognised as deductible revenue-earning costs upon acquisition. It is important to bear in mind that certain assets (such as land) are not subject to amortisation.

3. Liability of the acquirer of assets

Under the Tax Ordinance, only the acquirer of an enterprise or organised part of an enterprise is jointly and severally liable with the seller for the seller's tax arrears arising through the date of acquisition. This means that the acquirer of assets is not liable for the seller's tax arrears.

4. Indirect taxes (VAT, transaction tax)

The sale of specific assets that constitute goods or services under the VAT Act is subject to VAT at the basic rate (23% as of 2017), unless a reduced VAT rate or VAT exemption is available in the specific instance (e.g. the exemption for buildings and other structures under certain conditions).

In the case of a VAT exemption for specific items (e.g. real estate), their sale will be subject to the tax on civil-law transactions at the rate of 2%. Transaction tax is payable by the buyer.

Merger

Legal succession

The Tax Ordinance provides for universal succession, under which a legal person formed through a merger of legal persons and/or commercial companies or partnerships, or a legal person taking over a legal person or commercial company or partnership, enters into all of the rights and obligations provided under tax law, including rights and obligations arising out of decisions issued under tax regulations.

An exception to the rule of universal succession in the case of a merger is that the acquirer or newly formed company is not entitled to use the tax losses generated by the acquired company.

Corporate income tax effects

As a rule, a merger of capital companies with their registered office in Poland or elsewhere in the EU or EEA is tax-neutral for both the acquirer and the target and for the shareholders of the target or the merging companies (so long as they do not receive additional consideration in cash). Tax neutrality will

not be maintained if the merger is not conducted for valid economic reasons, but the main reason or one of the main reasons for the transaction is tax avoidance.

In the case of a merger in which the acquirer or newly formed company obtains assets whose value is higher than the par value of the shares allocated in exchange to the shareholders of the target, the excess in the value of the assets of the target received by the acquirer or newly formed company over the par value of the shares allocated to the shareholders of the target also does not constitute income, unless the acquirer holds less than 10% of the share capital of the target.

The process of merger does not allow the acquirer or newly formed company to step up the basis of the acquired assets for tax purposes. In this respect, the rule is that the existing tax basis is carried forward, under the principle of continuation.

Indirect taxes (VAT, transaction tax)

As a rule, a corporate merger is not subject to VAT, and is also neutral for purposes of the tax on civil-law transactions.

Division

Legal succession

The Tax Ordinance provides for universal succession in the event of division of a legal person if the assets assumed as a result of the division (and in the case of a division by split-off, also the assets of the divided legal person) constitute an organised part of the enterprise. In such case, effective on the division date the acquirers or the legal persons formed as a result of the division enter into all of the rights and obligations provided under tax law of the divided legal person connected with the assets allocated to them in the division plan, including rights and obligations arising out of decisions issued under tax regulations.

If the assets acquired as a result of the division (or in the case of a division by split-off, also the assets of the divided legal person) do not constitute an organised part of the enterprise, the acquirers or the legal persons formed as a result of the division are jointly and severally liable with all of their assets for

the tax arrears of the divided legal person, up to the net value of the assets acquired pursuant to the division plan. In addition, in the case of a division by split-off, such liability is limited to tax arrears arising through the date of the split-off.

An exception to the rule of universal succession in the case of a division is that the acquirer or newly formed company is not entitled to use the losses generated by the divided company.

Corporate income tax effects

As a rule, the division of capital companies with their registered office in Poland or elsewhere in the EU or EEA is tax-neutral for both the acquirer or newly formed company and for the divided company, and for the shareholders of the acquirer or newly formed company and of the divided company (so long as they do not receive additional consideration in cash), if the assets assumed as a result of the division (and in the case of a division by split-off, the assets assumed as a result of the division or the assets remaining in the company) constitute an organised part of the enterprise. Otherwise, income may arise on the part of the shareholders in the form of the excess in the value of the shares allocated in the acquirer or newly formed company over the costs of acquiring or taking up the shares in the divided company, but if certain conditions are met this income may be exempt from taxation.

In the case of a division, the acquirer or newly formed company may obtain assets whose value is higher than the par value of the shares allocated in exchange to shareholders of the divided company. Such excess in the value of the assets of the divided company received by the acquirer or newly formed company over the par value of the shares allocated to the shareholders of the divided company does not constitute income (except for a situation where the acquirer holds less than 10% of the share capital of the divided company), unless the division is not conducted for economically justifiable reasons.

The process of division does not allow the acquirer or newly formed company to step up the basis of the acquired assets for tax purposes. In this respect, the rule is that the existing tax basis is carried forward, under the principle of continuation.

Indirect taxes (VAT, transaction tax)

As a rule, the division of a capital company is not subject to VAT, and is also neutral from the point of view of the tax on civil-law transactions.

Exchange of shares

Definition of exchange of shares

An exchange of shares is a transaction in which a company acquires shares of another company from a shareholder of the other company in exchange for the company's own shares, resulting in obtaining an absolute majority of the voting rights of the other company, or increasing the number of shares in the company if prior to the transaction it already held an absolute majority of the voting rights in the other company. Cash consideration, if any, may not exceed 10% of the par value of the company's own shares, or if the shares have no par value, the market value of the shares.

Corporate income tax consequences

As a rule, the transaction is neutral from the perspective of income tax if (i) the transaction is conducted for valid economic reasons and (ii) the entities taking part in the transaction are subject to taxation on all of their income, wherever earned, in a member state of the European Union or the European Economic Area.

Indirect taxes (VAT, transaction tax)

An exchange of shares is not subject to VAT or the tax on civil transactions.

Conversion

Legal succession

The Tax Ordinance provides for universal succession, under which a converted company enters into all the rights and obligations of the entity in its previous legal form provided under tax law, including rights and obligations arising out of decisions issued under tax regulations.

Conversion from one form of capital company into another form of capital company does not result in loss of the right to use losses generated by the converted company.

Corporate income tax effects

As a rule, conversion from one form of capital company into another form of capital company is neutral from the CIT point of view. The converted company settles CIT under the principle of continuation.

Indirect taxes (VAT, transaction tax)

Conversion of a capital company is neutral from the point of view of VAT and the tax on civil-law transactions.

State aid issues

Under Art. 107(1) of the Treaty on the Functioning of the European Union, any aid granted by a member state or through state resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods is incompatible with the internal market.

As a rule, state aid must be presented to the European Commission for approval, unless it falls within the range of *de minimis* aid or the derogation set forth in the Commission's Block Exemption Regulation. When state aid is granted unlawfully, negatively impacting the internal market, the member state is obliged to recover the aid from the beneficiary.

According to case law from the Court of Justice of the European Union, only state aid approved by the Commission creates a justified expectation on the part of beneficiaries, and a reasonable undertaking should examine whether aid was granted to it lawfully.

An undertaking that has received state aid is required to use it in compliance with the rules set forth in national law, EU law and the funding agreements with the institutions providing the aid. Violation of these conditions for use of state aid may result in an obligation to refund the aid.

Because state aid may be subject to recovery, together with interest, in M&A transactions it is necessary in each case to examine the existence of state aid on the part of the undertakings involved in the transaction and the effect that the transaction may have on the conditions for use of any state aid received by the parties.

Preliminary examination

The examination of the existence of state aid and the related risk most often boils down to an analysis of the conditions set forth in funding agreements. But it should be borne in mind that state aid can also occur in connection with relief or reductions in public charges (e.g. state aid for restructuring).

State aid may also result from regulations conditioning advantages on the location of the undertaking (e.g. in special economic zones, or prohibiting relocation), the size of the undertaking (e.g. SMEs), the business profile (e.g. services performed in the general economic interest) or for example on establishing and maintaining certain corporate governance rules (e.g. fruit and vegetable producer organisations).

An undertaking may also be the beneficiary of impermissible state aid. Then there is a high risk that an obligation to refund the state aid could be passed on to the legal successors (in share deals) or the acquirers of the assets (in asset deals).

Funding agreement

The examination of the conditions for award of state aid most often involves an analysis of the funding agreement between the institution providing the funding and the beneficiary. The application for funding is also subject to analysis.

Such agreements provide for rules and conditions and aims related to realisation of the project in question, defining the rights and obligations of the parties and the rules for cooperation between the beneficiary and the funding institution.

Analysis of funding agreements requires particular attention to the risks for the parties to the transaction. As a rule, frank cooperation with the institution providing the funding can help avoid consequences connected with withdrawal of the funding in whole or part or termination of the funding agreement for breach of obligations connected with realisation of

the project financed with public funds, resulting from the transaction.

Funding agreements in projects financed out of European funds

In connection with Poland's absorption of EU funds pursuant to the EU's cohesion policy, national and regional operational programmes provide funding for businesses carrying out projects consistent with the goals of these programmes.

The expenditure of EU funds should ensure lasting improvements in the economies of the member states. For this reason, funding agreement in projects financed out of EU funds impose obligations connected with the project durability period, continuing for several years after completion of the project.

The definition of project durability is set forth in Council Regulation 1083/2006 (EC) for projects carried out under the 2007–2013 financial perspective and Regulation 1303/2013 (EU) for projects in the 2014–2020 financial perspective.

First and foremost, it must be borne in mind that cessation of productive activity or a change in the ownership of an element of infrastructure (whether in a share deal or an asset deal) may constitute an infringement of project durability, requiring repayment of the funding.

In the case of entities that have obtained financing out of EU funds, in the case of either a share deal or an asset deal, during the project durability period particular care is required to maintain the character, purposes and conditions of the project and to ensure that the shares or assets are sold at market prices.

These requirements impose special obligations to reach the appropriate understanding with the institutions providing the state aid and to make a detailed and transparent valuation of the subject of the transaction.



M&A Practice

For over 20 years we have been advising on transactions of international scope and local projects in various sectors of the economy. Alongside dispute resolution, transactional advice is a core practice of the law firm, representing a significant proportion of the matters we handle.

We act for all parties of transactions: sellers, buyers, and other stakeholders, as well as financial institutions and the management board of target companies. We are thoroughly familiar with the Polish and CEE markets, where we assist foreign investors in establishing a presence. We also assist Polish investors abroad. Thanks to our many years of experience cooperating with the top foreign law firms in M&A, we provide support for cross-border transactions in Poland and across Europe.

We help structure transactions and formulate the documentation to properly secure the interests of our clients and limit the risk of disputes arising between the parties. If the company operates in

a regulated industry, we reflect the specifics of the industry and its regulations in the transaction. Our goal is to minimise the time and expense necessary to close the transaction.

We advise at all stages of transactions. We prepare full due diligence reports. We draw up framework agreements governing the structure and specific stages of the transaction, letters of intent, heads of agreement, confidentiality agreements, preliminary agreements, contractual undertakings and dispositive agreements, involving shares, enterprises, organised parts of enterprises, and specific assets. We assist in the changes necessary to spin off companies and for the company or enterprise to pass from the control of one capital group to another, including transfer of rights and obligations under existing contracts. After closing, we advise on matters related to performance of the obligations under the transaction documents as well as public-law obligations connected with the transaction.

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Wardyński & Partners

Wardyński & Partners was established in 1988. Drawing from the finest traditions of the legal profession in Poland, we focus on our clients' business needs, helping them find effective and practical solutions to their most difficult legal problems.

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