

## Chapter 2: General Remarks on Securing Credit Risk in Polish Law

### I. Introduction

Traditionally Polish law differentiates between *claims secured* by a *personal security* or by *collateral*. Sometimes an additional group of *security held in trust* is also referred to, which covers pledged property and the assignment by security. Personal security<sup>6</sup> includes Civil Code regulated sureties; check and bill guarantees regulated in legislation on cheques and bills of exchange, and bank guarantees, which are regulated to a certain extent in banking legislation.<sup>7</sup> Although the cumulative assumption of debt is not expressly regulated in the Civil Code, it is recognized in established case law. Claims secured by collateral include pawns, registered liens and mortgages. The Banking Act provides expressly for the assignment as collateral. Although assignment by security is not regulated by law, it is often used by banks. The retention of title is also provided for in the Civil Code.

It must be emphasized that at first glance these legal institutions appear to be very similar to the German or Austrian equivalents. On closer examination, however, significant differences become apparent, especially with regard to realization proceedings, but also due to the divergent relationships between law of obligations and property law in the respective legal systems.

### II. The Significance of Academia for the Polish Legal System

These Guidelines often consider the *opinion of academia*. This is because academics play a very important role in the Polish legal system. On the one hand, legal practice is still in its infancy, which means that there is still no precedent for a large number of legal problems. With regard to the Polish banking sector it should be noted that many legal disputes do not come to court at all. This is due to the possibility of a *bank execution title* (*bankowy tytuł egzekucyjny*), provided that the contracting party has signed a written agreement to this effect and the recoverable claims form part of the bank's activities, such as for example lending, which is listed in Article 5 of the Banking Act. The submission in writing to the enforcement is rendered on standard forms. The bank execution title is an execution title, which can be issued by a bank on the basis of its banking books and other banking documents that are concerned with the performance of banking activities.<sup>8</sup> If the bank obtains an certificate of enforceability from a court, it may then initiate an execution in accordance with the Code of Civil Procedure.<sup>9</sup>

It must also be taken into account that decisions handed down by the Supreme Court of the Republic of Poland are often subject to amendments. In particular, the direct influence of university professors on rulings and interpretations should not be underestimated. Many university professors also serve as judges and therefore issue rulings, which conform to their legal opinions but

<sup>6</sup> Ustawa – kodeks cywilny of April 23, 1964 (Dz.U. no. 16, pos. 93 with amendments).

<sup>7</sup> Ustawa – Prawo bankowe of August 29, 1997 (Repromulgation of 2002, Dz.U. no. 72, pos.665 with amendments).

<sup>8</sup> Sect.96 Art.1 Banking Act.

<sup>9</sup> F. Zoll, Verfahrensrechtliche Aspekte der dinglichen Kreditsicherheiten im polnischen Recht, in: Drobnig/Roth/Trunk (Publ.), Mobilarsicherheiten in Osteuropa, Berlin 2002, p. 125.

are not necessarily in line with prevailing opinion. This uncertainty for banks will be made clear by making references to the opinion of academia.

### III. Procedures for Enforcing Claims

#### A. Overview

Polish law recognizes three forms of special proceedings, which aim to enforce debt collection quickly and efficiently.<sup>10</sup> They comprise: *summons proceedings*, *summary proceedings* and *simplified proceedings*, whereby the first two can overlap with the last one in some instances. This is due to the fact that the simplified proceedings have been developed for petty disputes. Commercial proceedings must also be considered as they play a significant role for banks. Furthermore, there is a special proceeding for commercial disputes.

Above all, the proceedings are important to ensure that the claims under a loan agreement are legally enforced. The realization of collateral does not always require a complaint filed with a court, it can also be effected for example by a bank execution title.

#### B. Summons Proceedings

The summons proceedings (*postępowanie nakazowe*) can only be initiated by request of the plaintiff in the statement of claim.<sup>11</sup> The aim of the summons proceedings is to obtain a *default summons*. This will be issued if the plaintiff has a pecuniary or fungible service claim that can be substantiated by the requisite documents in accordance with Article 485 Par. 1 Code of Civil Procedure.<sup>12</sup> The court also issues a default summons if the debt derives from a bill of exchange, check, warrant or covenant that has been duly completed and where there is no doubt about its content or correctness. The plaintiff must submit valid documents as evidence of the claim unless the title transfer arises directly from securities.<sup>13</sup> A default summons can also be decreed if the bank can assert a claim based on a statement of its bank books, if the statement of intent has been signed by authorized bank staff and is furnished with a bank seal and if there is evidence that a payment demand has been delivered to the debtor.<sup>14</sup> With the issue of the *default summons*, the defendant will be requested by the court to *satisfy the entire claim* and pay the legal costs within two weeks of receiving the summons or *lodge an appeal*.<sup>15</sup> The default summons may trigger the process of execution, which focuses on the collateral, without requiring a certificate of enforceability.<sup>16</sup> If the defendant duly lodges an appeal, a date for a hearing will be set down.<sup>17</sup> At the hearing a judgement will be rendered, in which the court will either uphold or set aside the default summons. In the latter case the court

<sup>10</sup> For details see *F. Zoll*, in: *Beschleunigung des zivilgerichtlichen Verfahrens in Mittel- und Osteuropa*, Wien-Graz 2004, p. 140 ff. m.w.N.

<sup>11</sup> Sect.484<sup>1</sup> Art. 2 Code of Civil Procedure.

<sup>12</sup> This includes, e.g., an official document or a payment order accepted by the debtor which has been rejected by the bank due to a lack of cover on the account.

<sup>13</sup> Sect.485 Art. 2 Code of Civil Procedure.

<sup>14</sup> Sect.485 Art. 3 Code of Civil Procedure.

<sup>15</sup> Sect.491 Art. 1 Code of Civil Procedure.

<sup>16</sup> Sect. 492 Art. 1 Code of Civil Procedure.

<sup>17</sup> Sect. 495 Art. 1 Code of Civil Procedure.

must decide on the merits of the case. The lawsuit may be dismissed for formal reasons. In this case, the proceedings are to be discontinued.<sup>18</sup>

### C. Summary Proceedings

Summary proceedings (*postępowanie upominawcze*) are regulated in Articles 497<sup>1</sup>-505 of the Code of Civil Procedure. If the conditions are met, the proceedings *will be opened ex officio*. A default summons is issued if the plaintiff wants to recover a cash claim<sup>19</sup> and there are no *grounds for disqualification*. These would be

- The manifest *lack of merit* of the claim;
- *Doubt* about the *correctness* of the documents submitted by the plaintiff;
- *Dependence* of the satisfaction of the claim *on the provision* of a reciprocal *service*. Nonetheless, a default summons may be issued if the service has been performed by the plaintiff or the defendant is required to perform in advance.<sup>20</sup>
- The abode of the defendant is unknown and/or it is impossible to process the default summons in the Republic of Poland<sup>21</sup>, i.e., the abode is known but it is abroad.<sup>22</sup>

With the service of the *default summons*, the defendant will be requested to *satisfy the entire claim* and pay the legal costs within two weeks of receiving the summons or *lodge an appeal*. The lodging of an appeal results in the loss of the effectiveness of the default summons so that the subsequent proceedings deal with the claim itself only. Furthermore, the default summons in the summary proceedings differs from that in the summons proceedings in that it does *not constitute an independent title to secure the claim*.<sup>23</sup> If the default summons is *not effectively contested on appeal*, it has the *validity of a legal decision*.<sup>24</sup>

### D. The Simplified Proceedings

The legislator has regulated the simplified proceedings (*postępowanie uproszczone*) in Articles 505<sup>1</sup>-505<sup>13</sup> of the Code of Civil Procedure. As it is applied to cases where the value of the claim is low, a detailed description is therefore not necessary.<sup>25</sup>

<sup>18</sup> Sect. 496 Code of Civil Procedure.

<sup>19</sup> Sect. 498 Art. 1 Code of Civil Procedure.

<sup>20</sup> *Manowska*, *Postępowanie nakazowe i upominawcze* (Enforcement and Summary Procedures), Warszawa 2001, p. 130; *F. Zoll*, in: *Beschleunigung...*, p. 148.

<sup>21</sup> Sect. 499 Code of Civil Procedure.

<sup>22</sup> *F. Zoll*, in: *Beschleunigung...*, p. 149. See Supreme Court decision of November 13, 1970, (II CZ 193/70, OSP 7-8/1971, pos. 144).

<sup>23</sup> *F. Zoll*, in: *Beschleunigung...*, p. 150.

<sup>24</sup> Sect. 504 Art. 2 Code of Civil Procedure.

<sup>25</sup> This type of procedure is applied, among other things, when a contractual claim is being demanded and the amount disputed does not exceed PLN 5,000 as well as in warranty and guarantee disputes in which the value of the object of the performance does not exceed the amount named above. The amendment of the Code of Civil Procedure includes a new maximum amount, namely, PLN10,000. Within the scope of the simplified proceedings complaints, objections, etc. are submitted by using special forms. Only one claim can be the object of a complaint, and it is not permitted to change a complaint. For more details see *F. Zoll*, in: *Beschleunigung* p. 150.

## E. Commercial Legal Proceedings

Commercial legal proceedings<sup>26</sup> (*postępowanie w sprawach gospodarczych*) are applicable to civil law *disputes between companies* engaged in economic activity.<sup>27</sup> In this context banks are regarded as companies.<sup>28</sup> Petty corporate disputes are not included within the scope of the regulation.<sup>29</sup> Due to the parties' expert knowledge, many regulations protecting plaintiff parties are waived. There are special rules on the serving of notices, provisions on mandatory attempts to reach an out-of-court settlement before initiating proceedings, adjudicative procedural options without holding oral proceedings etc.

## IV. Realization of Security

If the debtor does not attend to his or her obligation to pay, the creditor can gain satisfaction by realizing the collateral used to secure the claim. Polish law recognizes various options to realize security. The realization method availed of by the creditor is always dependent on the specific type of security. In the case of a *pawn* for example only judicial realization by *execution* is possible. For the *financial lien*, in contrast, there are several *out-of-court realization options*, such as for example the sale of the collateral security or its appropriation. As there are numerous out-of-court realization methods, they are described in the sections on the relevant types of security; the following section looks in general at the judicial realization of security.

### A. Realization of the Security by Execution

The basis for the execution is a writ of execution with clause of enforceability.<sup>30</sup> The clause of enforceability is issued by the competent court.<sup>31</sup>

#### 1. Priority Classes

In Polish law the principle of *pro rata satisfaction of claims* in the creditor classes applies in the execution. Claims that have been secured by a specific collateral security will be satisfied in these classes in accordance with their respective ranking. The existence of a group of preferential claims as against secured claims must always be taken into account. Article 1025 par. 1 of the Code of Civil Procedure contains the fundamental ranking in which claims in execution proceedings are satisfied. The *ranking of the classes* is as follows:

1. Legal costs;
2. Alimony claims;
3. Wage claims for three months up to the amount of the minimum wage<sup>32</sup> and social insurance claims for illness, work incapacity, disability or death as well as the cost of a decent funeral;

<sup>26</sup> Regulated in Sect. 479<sup>1</sup> Code of Civil Procedure.

<sup>27</sup> Sect. 479<sup>1</sup> Code of Civil Procedure.

<sup>28</sup> Sect. 479<sup>2</sup> Art. 1 Code of Civil Procedure.

<sup>29</sup> Sect. 479<sup>2</sup> Art. 2 Code of Civil Procedure.

<sup>30</sup> Sect. 776 Code of Civil Procedure (Ustawa – Kodeks postępowania cywilnego of October 17, 1964, Dz.U. no. 43, pos. 296 with amendments).

<sup>31</sup> Sect. 781 Code of Civil Procedure.

<sup>32</sup> The minimum wage is PLN 824.00, Rozporządzenie Rady Ministrów w sprawie wysokości minimalnego wynagrodzenia za pracę w 2004 r. (Decree of the Council of Ministers of September 9, 2003 on the amount of minimum wages in the year 2004, Dz.U. no. 167 pos. 1623).

4. Claims resulting from loans secured by a mortgage;
5. Claims secured by a mortgage or a registered lien or by liens recorded in another relevant register;
6. Wage claims that are not satisfied in the third class;
7. Claims applicable in accordance with the provisions in Part III of the Fiscal Code<sup>33</sup> in as far as they were not satisfied in the fifth class;
8. Claims secured by lien or such that do not have priority in the previous classes mentioned (pawns);
9. Claims of those creditors that have initiated the execution;
10. Other claims.

These classes form, as already mentioned, the normal ranking for the satisfaction of claims. Interest and proceedings costs are satisfied in the same class as the claim. However, only interest for the two years before the conferral of ownership and proceedings costs enjoy the same treatment as the claims in classes 4, 5 and 8 (lien) of up to a maximum of 10% of the capital (claim). The other interest and costs are satisfied in the tenth class.<sup>34</sup> If the amount for the full satisfaction of all claims and rights of one class is insufficient, the claims in classes 4, 5 and 8 in their relevant priority according to ranking are satisfied, whereas other claims are satisfied in relation to their respective size.<sup>35</sup>

## 2. Execution Title

The Polish Code of Civil Procedure includes a list of permissible *execution titles*. Execution can only be carried out if it the title contains a certificate of enforceability.<sup>36</sup> Execution titles can be the following:

- A legally enforceable *judgment* or an immediately *enforceable judgment* or a *settlement* agreed-on in court;
- A *judgment* rendered by an *arbitration tribunal* or a *settlement* agreed before such court;
- Other judgments, settlements and legal instruments that can be legally enforced;
- A *notarial instrument*, in which the debtor has submitted to the execution and which contains an obligation to pay a cash sum or provide other fungibles – under the prerequisite that the quantity is determined in the notarial instrument, or an obligation to surrender a specific property listed in the notarial instrument; however, the term of payment, the term of service or the surrender, respectively, must be set out in the notarial instrument;
- A notarial instrument, in which the debtor has submitted to the execution and which stipulates the obligation to pay a cash sum directly set down in the notarial instrument or a sum determined with the help of a stable value clause as long as the notarial instrument has set down the conditions that entitle the creditor on the basis the certificate to execute the enforcement of the entire claim or part of the claim; furthermore, the notarial instru-

<sup>33</sup> Ustawa – ordynacja podatkowa of July 29, 1997 (Dz.U. no. 137, pos. 926 with amendments).

<sup>34</sup> Sect. 1025 Art. 3 Code of Civil Procedure.

<sup>35</sup> Sect. 1026 Art. 1 Code of Civil Procedure.

<sup>36</sup> Sect. 776 Code of Civil Procedure.

ment must set down the period within which the creditor may apply for an application of a certificate of enforceability.<sup>37</sup>

A special execution title, the bank execution title (*bankowy tytuł egzekucyjny*), is regulated in the Banking Act.<sup>38</sup>

## B. Realization of Collateral in the Event of Bankruptcy

### 1. General Remarks on Bankruptcy Proceedings

The realization of collateral in bankruptcy proceedings has several special features. The Bankruptcy and Composition Act<sup>39</sup> differentiates between *declarations of bankruptcy with the possibility of composition* and declarations that *end in liquidation*. Bankruptcy proceedings with the possibility of composition are undertaken if a credible case can be made that the creditor will receive a better settlement using this alternative than if bankruptcy proceedings ending in liquidation are initiated.<sup>40</sup> If this is not the case, then bankruptcy with liquidation is declared.<sup>41</sup> The court may amend its decision to conduct liquidation proceedings and initiate bankruptcy proceedings with the possibility of composition instead and vice versa,<sup>42</sup> if the basis for such bankruptcy proceedings become clear no earlier than during the course of the proceedings.<sup>43</sup>

Bankruptcy proceedings are *opened upon application*. Both the debtor and his or her creditors are entitled to submit an application.<sup>44</sup> Prerequisite is the insolvency of the debtor.<sup>45</sup> The court must *dismiss* a bankruptcy application (mandatory) if the assets of the debtor are insufficient to cover the costs of the proceedings (*insufficiency of assets*). In addition, the court can dismiss the application (optional) if it establishes that the debtor's property has been used as collateral to such an extent that the remaining assets of the debtor are insufficient to cover the costs of the proceedings. If the collateral proves to be invalid, the bankruptcy proceedings are not dismissed.<sup>46</sup>

### 2. Order of Creditor Satisfaction

The Bankruptcy and Composition Act regulates the satisfaction of creditors according to class. The classes are as follows:

1. *Costs of the bankruptcy proceedings*, employee social security tax, wage claims, claims for the past two years of farmers on contracts to deliver products from their own farm, alimony claims, pensions, claims arising from *legal transactions* undertaken by the *administrator*<sup>47</sup> of the *bankrupt's estate*

<sup>37</sup> Sect. 777 Art. 1 Code of Civil Procedure.

<sup>38</sup> Sect. 96-98 Banking Act.

<sup>39</sup> Ustawa – Prawo upadłościowe i naprawcze of February 28, 2003 (Dz.U. no. 60, pos. 535 with amendments).

<sup>40</sup> Sect. 14 Art. 1 Bankruptcy and Composition Act.

<sup>41</sup> Sect. 15 Bankruptcy and Composition Act.

<sup>42</sup> Sect. 17 Art. 1 Bankruptcy and Composition Act.

<sup>43</sup> Sect. 16 Bankruptcy and Composition Act.

<sup>44</sup> Sect. 20 Art. 1 Bankruptcy and Composition Act.

<sup>45</sup> Sect. 10 Bankruptcy and Composition Act.

<sup>46</sup> Sect.13 Bankruptcy and Composition Act.

<sup>47</sup> In the event of a declaration of bankruptcy, an administrator of the bankrupt's estate is appointed at the time of liquidation. An administrator in composition by contrast is appointed when the undischarged bankrupt is banned from administering the estate or when the undischarged bankrupt is charged with the administration of only part of the assets. Sect.156 par.1, 3 Bankruptcy and Composition Act.

or *the administrator in composition*, claims from the mutual contracts that were agreed before bankruptcy was filed by the undischarged bankrupt and which the assets' administrator or liquidator have deemed must be fulfilled, *claims* attributable to the *unjustified enrichment* of the *bankrupt's estate* as well as claims arising from legal transactions that the undischarged bankrupt in agreement with the judicial supervisor has undertaken;<sup>48</sup>

2. *Taxes*, other *fiscal charges* as well as social security contributions for the year prior to the declaration of bankruptcy that do not fall into the first class including interest and execution charges;
3. *Other claims*, which *do not fall into the fourth class*, including interest for the year prior to the declaration of bankruptcy, contractual claims for damages, proceedings and execution costs;
4. *Interest*, which *does not fall into the higher classes*, in order of satisfaction of the capital, as well as the court and legal fines, and claims from gifts and legacies.<sup>49</sup>

This is the basic order of satisfaction. There are exceptions, which will be examined in conjunction with the relevant types of security.

The legislation stipulates that the claims of one class will only be satisfied after the complete settlement of the claims of the preceding classes. If there are insufficient assets for the full satisfaction of one class then the claims in this class will be satisfied pro rata.<sup>50</sup>

### 3. Netting

Netting is not a form of realization in the sense of realization of collateral. However, as there are special netting features in Polish law, in particular, with regard to bankruptcy proceedings, the following will review them in brief.

#### a. Netting According to the Civil Code

In principle, netting is possible if two persons have a relationship in which they are both creditor and debtor at the same time and the object of the claim is either cash or just goods of equal quality specified according to its species. In addition, the claims must be due and enforceable in court or before a state body. On that conditions the one claim compensates the other up to the amount of the lower of the two.<sup>51</sup> The claim is netted in so far as one party issues a referring statement towards the other party. The legal effect of this statement is backdated to the time when the netting first became possible.<sup>52</sup>

It should be noted that not every claim can be netted. *Excluded* from this option are:

- Non-attachable claims;
- Alimony claims;
- Claims pertaining to illegal acts;

<sup>48</sup> The judicial supervisor is appointed when bankruptcy with the possibility of composition is declared, Sect.156 Art.2 Bankruptcy and Composition Act.

<sup>49</sup> Sect.342 par. 1 Bankruptcy and Composition Act.

<sup>50</sup> Sect.344 Bankruptcy and Composition Act.

<sup>51</sup> Sect. 498 Civil Code.

<sup>52</sup> Sect. 499 Civil Code.

- Claims that the provisions specifically exclude from the netting option.<sup>53</sup> These provisions include for example Article 89 of the Bankruptcy and Composition Act.

#### b. Netting in the Case of Bankruptcy

There are special netting features in bankruptcy proceedings. When *bankruptcy proceedings with the possibility of composition* are initiated, the netting of mutual claims of the creditor and the bankrupt is *basically permissible*.<sup>54</sup> If the creditor wishes to make use of his or her netting rights in bankruptcy proceedings with the possibility of composition, the creditor must declare this intention by the latest when filing the claim.<sup>55</sup>

If *proceedings to liquidate the bankrupt's assets are opened*, then the netting of a claim of the bankrupt with that of a claim of the creditor is permissible *if both claims existed on the day that bankruptcy was declared*, even if one of the two claims was not yet due. The total sum of the claim of the undischarged bankrupt is used for the netting, i.e., the principal claim as well as the interest due<sup>56</sup> on the netting day; while the amount of the creditor's claim comprises the principal claim including the interest calculated up to the day bankruptcy was declared only. If the undischarged bankrupt has a non-interest bearing loan that is not yet due on that day, the netting is based on the principal amount less the statutory interest, but not more than 6%, which accrues for the period from the day bankruptcy is declared to the day of maturity (that is the day on which the claim must be settled as per the contract), but with the restriction of not more than two years of accumulation.<sup>57</sup> In cases where *claims arise after the declaration of bankruptcy*, the Supreme Court states that the admissibility of netting is evaluated in accordance with general netting provisions of the Civil Code<sup>58</sup> but not in accordance with the provisions in the Bankruptcy and Composition Act.<sup>59</sup> This means that netting is permitted without any further restrictions.<sup>60</sup> The judgment gained wide approval in legal academic circles.<sup>61</sup>

Netting is *not permissible* if the debtor of the undischarged bankrupt acquired the claim via an assignment or endorsement after the declaration of bankruptcy or if the claim was acquired within the last year before the day bankruptcy was declared and the debtor had knowledge of the declaration of bankruptcy. Netting is, however, *possible* if the acquirer becomes a debtor vis-à-vis the bankrupt due to the redemption of a debt of the undischarged bankrupt for which he or she was liable personally or with specified assets, and the acquirer did not have any knowledge of the reasons for the declaration of bankruptcy at that time.<sup>62</sup> In this context, we are looking at the repayment of a debt, e.g., by the guarantor or by a debtor being liable in rem, such as

<sup>53</sup> Sect. 505 Civil Code.

<sup>54</sup> Zedler, in: Jakubecki/Zedler, Prawo..., Sect.89 note 1.

<sup>55</sup> Sect.89 Bankruptcy and Composition Act.

<sup>56</sup> Jakubecki, in: Jakubecki/Zedler, Prawo..., Sect.93 note 5.

<sup>57</sup> Sect.93 Bankruptcy and Composition Act.

<sup>58</sup> Sect.498-505 Civil Code.

<sup>59</sup> Supreme Court decision of February 20, 1997 (I CKN 3/97, OSN 8/1997, pos. 109).

<sup>60</sup> Jakubecki, in: Jakubecki/Zedler, Prawo..., Sect.93 note 8.

<sup>61</sup> See e.g. Torbus, in: Przegląd Sądowy 3/1998, p. 90; Wąsowicz, in: Państwo i Prawo 3/1998, p.109.

<sup>62</sup> Sect.94 Art.1, 2 p. 1 Bankruptcy and Composition Act.



for example the mortgage debtor.<sup>63</sup> If a third party has entered into the rights of the satisfied creditor up to a year before the declaration of bankruptcy, the acquirer of the satisfied claim can always net said claim with that of the undischarged bankrupt.<sup>64</sup> Netting is not permissible if the creditor became the debtor of the undischarged bankrupt after the day bankruptcy was declared.<sup>65</sup>

If a creditor wishes to make use of the right to net claims in liquidation proceedings, said creditor must declare this intention *by the latest when filing the claim*.<sup>66</sup>

#### 4. Ineffectiveness of Legal Transactions in Bankruptcy Proceedings

##### a. Ineffectiveness According to Sect. 127 ff Bankruptcy and Composition Act

Section 127 ff of the Bankruptcy and Composition Act regulates which legal transactions concluded by a debtor shall not be effective with respect to the bankruptcy estate. The Bankruptcy and Composition Act considers the following *legal transactions to be ineffective*:

- *Legal transactions* that were undertaken by the undischarged bankrupt one year before filing the bankruptcy petition and which had the purpose of a disposition of his or her estate on the condition that the *legal transaction* was free-of-charge or if it involved charges and the volume of the *obligation* to be performed by the undischarged bankrupt was *grossly disproportionate* either to the *service rendered in return* for the undischarged bankrupt or for a third party. This holds true for court settlements, acceptance of lawsuits and the waiver of claims as well;<sup>67</sup>
- Furnishing security and *payment of a debt that is not yet due* if this occurs in the two months before the bankruptcy petition is filed. However, the person that received the payment or security can request that this legal transaction be seen as valid in the case of a lawsuit or an objection if said person had no knowledge of the grounds for the declaration of bankruptcy.<sup>68</sup>
- *Legal transactions against payment*, which have been concluded with *close relatives*<sup>69</sup> within six months of filing the bankruptcy petition. This is also true if the undischarged bankrupt is a company or a legal entity and a legal transaction has been executed with its *stockholders, representatives* or their *spouses* or if the legal transaction has been concluded with an *associated companies*, its stockholders, representatives or their spouses.<sup>70</sup>

<sup>63</sup> *Jakubecki*, in: *Jakubecki/Zedler, Prawo...*, Sect.94 note 4.

<sup>64</sup> Sect.94 par.2 p. 2 Bankruptcy and Composition Act.

<sup>65</sup> Sect.95 Bankruptcy and Composition Act.

<sup>66</sup> Sect.96 Bankruptcy and Composition Act.

<sup>67</sup> Sect.127 par.1, 2 Bankruptcy and Composition Act.

<sup>68</sup> Sect.127 par. 3 Bankruptcy and Composition Act.

<sup>69</sup> The law expressly specifies the respective persons – e.g. spouses.

<sup>70</sup> Sect.128 Bankruptcy and Composition Act.

There are also legal transactions that do not become ineffective by operation of law, but can be declared as such *upon request of a bankruptcy judge (sędzia-komisarz)*<sup>71</sup> by the issuance of a *ruling*. This delegated authority is accorded in Article 129 ff of the Bankruptcy and Composition Act.<sup>72</sup>

#### b. Ineffectiveness According to the Civil Code

The Bankruptcy and Composition Act refers to the Civil Code<sup>73</sup> for the authority to rescind legal transactions, but only if no regulation can be found in the Bankruptcy and Composition Act (principle of subsidiarity).

Article 527-534 of the Civil Code makes a reference to contestable transactions under *actio pauliana*. Accordingly, if a *debtor's legal transaction*, which *disadvantages the creditors*, gives a third party pecuniary benefit, every creditor may demand that the legal transaction be made *invalid in respect to him or her* (relative invalidity) if the debtor acted in the *knowledge of the disadvantage to the creditors* and the *third party* could have gained *knowledge* thereof by exercising due diligence. A *legal transaction* is to the disadvantage of a creditor if its execution caused the debtor to become *insolvent* or aggravated this *insolvency*. If, as a result of the legal transaction mentioned, a person, which has a *close relationship* with the debtor or an entrepreneur with whom the debtor maintains a stable business relationship, has gained pecuniary benefit, then it is assumed that this person or legal entity has acted in bad faith.<sup>74</sup> The relationship is deemed as close if it can be assumed that the third party has information about the financial situation of the debtor.<sup>75</sup> This is true, in particular, for fiancées and companions in life.<sup>76</sup> However, close relatives are not automatically subsumable under this legal provision.<sup>77</sup> If the third party gained pecuniary benefit from the legal transaction free-of-charge, the creditor may request an annulment without the third party having acted in bad faith.<sup>78</sup> If the debtor was insolvent at the time of making a gift or became insolvent as a result, it may be assumed that the debtor acted consciously to the detriment of the creditor.<sup>79</sup> A decision

<sup>71</sup> After the declaration of bankruptcy, the bankruptcy judge conducts the bankruptcy proceedings with the exception of activities that fall into the jurisdiction of the bankruptcy court, Sect.151 Bankruptcy and Composition Act.

<sup>72</sup> This refers to the amount of the wages of employees who work in the administration of the company or of persons who supply services related to the administration of the company. A gross discrepancy to the usual wages for this type of activity must be given. The same applies to severance charges granted to such persons on the termination of the employment contract (Sect.129 par.1, 3 Bankruptcy and Composition Act). Furthermore, this refers to collateral encumbered by liens on the assets of the undischarged bankrupt, if said bankrupt was not the personal debtor and the establishment of the lien took place within one year prior to the filing for bankruptcy and the undischarged bankrupt did not receive any consideration or a relatively small one. Regardless of the amount of the consideration, the bankruptcy judge declares the security given as invalid if these debts are secured by close relatives, partners, representatives or their spouses (Sect.128 Bankruptcy and Composition Act and Sect.130 par.1-3 Bankruptcy and Composition Act).

<sup>73</sup> Sect.131 Bankruptcy and Composition Act.

<sup>74</sup> Sect.527 Civil Code.

<sup>75</sup> Supreme Court decision of April 10, 1964 (III CR 39/64, OSN 5/1965 pos. 75).

<sup>76</sup> Supreme Court decision of May 11, 1951 (C. 213/46, Państwo i Prawo 9-10/1964, p. 176).

<sup>77</sup> *Jakubecki*, in: *Jakubecki/Zedler, Prawo upadłościowe i naprawcze (Bankruptcy and Composition Act)*, Sect.131 note 4.

<sup>78</sup> Sect.528 Civil Code.

<sup>79</sup> Sect.529 Civil Code.

on the relative ineffectiveness shall be reached by a court in legal proceedings against the third party.<sup>80</sup>

It should be noted that the above mentioned *actio pauliana* is enforceable not only within the framework of the bankruptcy proceedings, but is also generally valid.

In the event of the ineffectiveness of a legal transaction of a debtor (includes all of the above mentioned instances) everything, which due to this legal transaction reduces the assets of the bankrupt debtor, must be *surrendered to the bankruptcy estate*, and if this is not possible, the equivalent must be contributed in cash.<sup>81</sup>

### 5. Excursus: Legislation on Substitute Share Capital

According to Article 14 par. 3 of the Polish Commercial Companies Code<sup>82</sup> a claim by a shareholder of a corporation (joint stock company and private limited company) to which such shareholder has extended a loan will be regarded as capital invested by the shareholder should the company declare bankruptcy. But this is only the case if bankruptcy is declared within two years from the day the loan contract was concluded.<sup>83</sup> This means that the lending shareholder cannot be satisfied without infringing upon the rights of the creditors of the company. The lender is thus only able to satisfy his or her claim pertaining to the loan contract after the third party has been satisfied.<sup>84</sup>

It is not clear whether “credits” are also subsumed under “loans”. Academics seem to lean towards a narrower interpretation.<sup>85</sup> Despite this, there is also the view that credit should be covered by this regulation,<sup>86</sup> as the ratio legis of the discussed provision is the protection of the creditors of a company, which justifies the exception to the rule.

### 6. Discharge of Residual Debt

If the undischarged bankrupt is a natural person, a ruling on the termination of liquidation proceedings may on the *application of the undischarged bankrupt*, declare a discharge of residual debt. By this one understands the settlement of the entire or part of the unsatisfied obligations of the undischarged bankrupt in the bankruptcy proceedings. A discharge from the remaining debt may be granted when:

<sup>80</sup> Sect.531 Art. 1 Civil Code.

<sup>81</sup> Sect.134 par.1 Bankruptcy and Composition Act.

<sup>82</sup> Ustawa – Kodeks spółek handlowych of September 15, 2000 (Dz.U. no. 94, pos. 1037 with amendments).

<sup>83</sup> Sect.14 Art. 3 Polish Commercial Companies Code.

<sup>84</sup> *Szumański*, in: Sołtysiński/Szajkowski/Szumański/Szwaja, Kodeks spółek handlowych. Tom I. Komentarz do artykułów 1-150 (Polish Commercial Companies Code. Volume I. Comments on Sections 1-150), Warszawa 2001, Sect.14 Rn. 30.

<sup>85</sup> Cf. *Szumański*, in: Sołtysiński/Szajkowski/Szumański/Szwaja..., Sect.14 Rn. 29; *Kidyba*, Kodeks spółek handlowych. Tom I. Komentarz do art. 1-300 k.s.h. (Polish Commercial Companies Code. Volume I. Comments on Sect.1-300), Kraków 2002, Sect.14 note 7. These authors make a reference to Sect.720-724 Civil Code, i.e., to the rules for loans.

<sup>86</sup> Cf. also *Kwaśnicki*, Pożyczki udzielane spółce kapitałowej przez wspólnika lub akcjonariusza (Loans granted to a stock company by a partner or a shareholder), in: Monitor Prawniczy 23/2001, p. 1169. Cf. also *Oplustil*, Pożyczki wspólników udzielane spółkom kapitałowym. Analiza regulacji art. 14 § 3 i art. 189 § 2 k.s.h. (Loans granted by partners to a stock corporation. An analysis of the rules in Sect.14 Art. 3 and Sect.189 Art. 2 Polish Commercial Companies Code), Kraków 2001, p. 70-72.

- The insolvency resulted from extraordinary circumstances, which were not the fault of the undischarged bankrupt;
- There are no circumstances that give reason to suspend the right to undertake economic activity on one's own account or the right to represent a trading corporation, a company, a cooperative, a foundation or an association; and
- The undischarged bankrupt met his or her obligations in the bankruptcy proceedings honestly.<sup>87</sup>

Included in the discharge of residual debt are claims on the claims list as well as claims that can be registered if their existence is established in the documents of the undischarged bankrupt.<sup>88</sup> The court must take into account the earnings potential of the undischarged bankrupt, the size of the unsatisfied claims and the probability of their future satisfaction in its deliberations when reaching to a decision.<sup>89</sup>

<sup>87</sup> Sect.369 par.1 Bankruptcy and Composition Act.

<sup>88</sup> Sect.369 par.2 Bankruptcy and Composition Act.

<sup>89</sup> Sect.370 par.1 Bankruptcy and Composition Act.