'21 YEARBOOK

WARDYŃSKI + PARTNERS

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Dear Readers,

It would be tempting to say that we are publishing this *Yearbook* in an entirely different world than the previous edition. But the question is whether the world has actually changed, or we simply find ourselves living in different circumstances.

The conditions under which we have functioned over the last year will impact the future of many of us. That future cannot be foretold, as it is always a function of chance, and changes result from slow, imperceptible processes until some dramatic event occurs, unleashing existential despair. In such situations, a single urgent issue—such as public health today—overshadows all of humanity's other problems and immobilises millions anticipating a panacea.

The situation may evolve in a similar fashion with environmental issues, which have been recognised by various bodies, but there is still insufficient social and political will to attempt to halt the degradation of our planet. An awareness of the danger will ultimately reach critical mass, but will it be too late? Destruction of the environment may also impact the economy, just as the pandemic has, but it will not be so easy to develop and roll out a vaccine.

Changes in the world around us are obviously accompanied by changes in legal systems. This generates a range of questions. Are these changes warranted, or only a pretext to limit the responsibility of public authority and shift this burden to the shoulders of citizens? Doesn't moving more and more of our activity online, where it can be exposed to surveillance, create new and broader opportunities for abuse of power? Is the main problem today protecting against abuses of authority, or protecting citizens against the unknown risks of unfolding changes?

Undoubtedly we have a duty to monitor these changes, to identify them as early as possible and respond in time. But in short, everything that seems like a novel change in the rules of the game has always existed. Short-sightedness and a lack of imagination are eternal problems, like the tendency to abuse power and the law. Human strengths and weaknesses will always be manifested in new fields of activity. We must observe how constants function in new arenas, and extrapolate from mechanisms that have functioned until now, onto new regions of our experience. This provides a workout for our common immune system. Only in this manner can we defend ourselves as a social organism.

As lawyers, obviously we listen and reflect first and foremost in the legal field. Hence the whole set of our firm's publications where we share our thoughts and observations with our readers. These include the practical approaches offered in the general legal and business portal "In Principle" and the employment blog hrlaw.pl, deeper explorations of technology (newtech.law) and public procurement (komentarzpzp.pl), and scholarship (*In Principle: Legal studies and analyses*). We not only advise on everyday business issues, but strive to make a positive contribution to the legal literature.

Observations of gradually occurring phenomena don't always lead to catastrophic conclusions. One highly desirable trend noticeable for years is the increasing accessibility of legal communication, writing about law with a view to a wider audience. Legal design, like plain language, is not just the latest fad. It is also a method of communicating that always places the audience and readers' experience front and centre. It is in this spirit that we have prepared this, our latest *Yearbook*. We would be interested to learn your views.

DR DOMINIK WAŁKOWSKI
adwokat, partner in charge of
the Environment practice

Business must make peace with nature

Preserving biodiversity, and protecting and rebuilding ecosystems, are the most important challenges facing humanity in the new decade, alongside the fight against climate change. They are also the source of the most serious risks for business operations.

Many words, few results

December 2020 marked five years since adoption of the Paris Agreement under the United Nations Framework Convention on Climate Change. On 2 December 2020, in an address entitled "The State of the Planet," UN Secretary-General António Guterres declared that the most important task of mankind in the 21st century is to "make peace with nature." This should become the top priority for everyone, everywhere. Human activity has driven the world toward chaos, but only humans can reverse this trend.

As Guterres stressed in his highly emotional speech, past climate policies have led to levels of greenhouse gas emissions now 60% higher than in the 1990s, when the climate accords that were supposed to halt the trend toward increased emissions were negotiated. Nor have any of the strategic aims for biodiversity in the plan for 2011–2020 (the Aichi Biodiversity Targets) been achieved.

Meanwhile, the natural environment feeds us, clothes us, quenches our thirst, generates oxygen, and shapes our culture and identity. The only solution can be full implementation of a sustainable economy based on renewable energy sources. We must take holistic action to adapt the economy to the consequences of climate change and to fortify the economy against the phenomena humanity will have to wrestle with in the years to come.

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Tangible risks for business

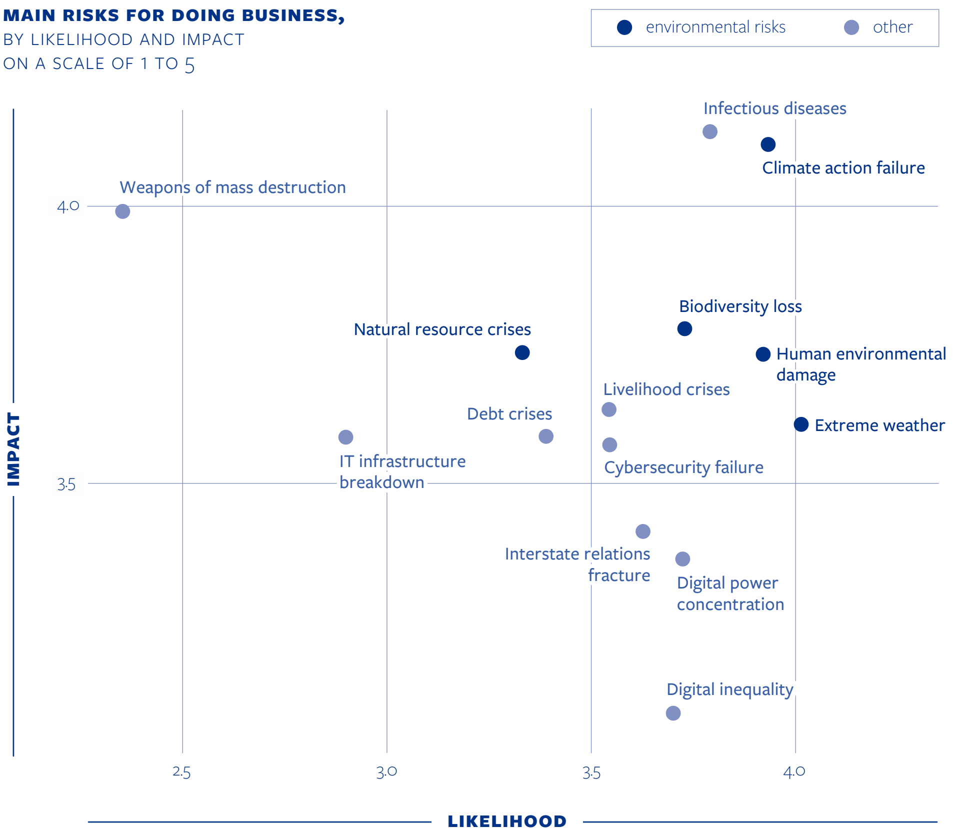
The speech by the UN Secretary-General offered no new substance or surprising statements. It merely provided an accurate summary of the situation around the world. Concerns associated with deleterious changes in climate and loss of biodiversity are also shared by the business community.

According to the recently published Global Risks Report 2021 from the World Economic Forum, almost half of the top ten most serious risk factors for the global economy in the next ten years are connected with the environment (the report divides risks into economic, geopolitical, societal, technological, and environmental). Environmental risks hold four of the top five positions in the list of the most likely risks. In the list of risks with the most serious potential impact for the global economy, climate action failure and biodiversity loss rank second and fourth, respectively. Further down that list are such items as natural resource crises, human-made environmental disasters, and extreme weather.

The report clearly shows that environmental risk is one of the greatest systemic threats to the global economy.

Under these circumstances, the findings of PWC's Annual Global CEO Survey come as no surprise. In 2018 the authors noted record-high optimism about anticipated global economic growth. Two years later, their mood hit a record low. In 2018 57% of CEOs believed that economic growth would improve, 5% thought it would decline, and the rest expected it to stay the same. In 2020 over half the respondents expected a slowdown, and less than a fourth expected further growth. The survey found that 24% of CEOs are very concerned about climate change and environmental damage—a much higher percentage than in previous years.

MAIN RISKS FOR DOING BUSINESS,
BY LIKELIHOOD AND IMPACT
ON A SCALE OF 1 TO 5



Source: *Global Risks Report 2021*, 19 January 2021, World Economic Forum.

RISING GLOBAL RISKS FOR DOING BUSINESS IN 2020	CHANGE IN RANKING
Spread of infectious diseases	+28
Biodiversity loss and ecosystem collapse	+8
Natural catastrophes	+7
Misuse of technologies	+5
Extreme weather events	+5
Unemployment or underemployment	+2
Asset bubble	+2
Human-made environmental catastrophes	+2
Failure of climate-change adaptation	+2
Food crises	+2

Source: *What are the biggest risks to business? New data shows climate concerns are rising*, 8 October 2020, World Economic Forum.
Environmental risks highlighted

Not just the climate crisis

While there has been talk of the climate crisis for many years, and its impacts are more and more starkly evident, the crisis of the loss of biodiversity, equally hazardous to the world economy, is not treated with the seriousness it deserves. The battle with biodiversity loss also seems much harder, as here there are no concrete, measurable solutions such as cutting greenhouse gas emissions. Losses to biodiversity are also not as readily apparent. Business can suffer even more from these losses if it is not prepared for the biodiversity crisis, while focusing corporate efforts only on combatting climate change.

Global business is the main consumer of natural resources, from heavy industry to fishing and agriculture. It is also, unfortunately, responsible for destruction and uncontrolled extraction of raw materials. But businesses must also face the costs generated by the loss of biodiversity and natural resources.

New costs, new risks

In the upcoming years, new economic conditions and modified legal frameworks will generate new business risks, increase operating costs, and restrict the availability and consumption of resources. Although no comprehensive new regulation has appeared recently in Polish law to introduce such restrictions, some existing legal solutions, often overlooked in practice, will assume new importance, and businesses should prepare accordingly.

The risk of legal liability for harm to the environment will grow, and it should be borne in mind that the current regulations provide a very limited list of circumstances allowing avoidance of such liability. Liability as such is generally unlimited in amount and only in the case of certain types of harm is conditioned on fault. There are more and more calls to limit or ban business operations exerting the most harmful impact on nature.

The duty to establish security against potential claims concerning the negative impacts of business operations will also be expanded. The number of legal regulations containing such duties has greatly increased in recent times, as have the amounts of security for claims demanded of businesses. A natural consequence is a greater risk on the part of entities financing businesses (banks, investors) and the need to verify the scope of insurance coverage.

Implementation of circular-economy principles, modification of certain business models, extended producer responsibility, and environmental assessment of product life cycles weighing natural factors will more greatly shape business operations. They will also have a more distinct impact on the criteria for selection of goods and services in the public procurement system, becoming conditions for obtaining support instruments and even modifying tax liabilities.

Restrictions on extraction of natural materials, and increased costs, are disrupting supply chains. Financing of development out of public funds is more and more dependent on environmental impacts. Private investors also pay increasing attention to issues of sustainable growth.

Changes are leading to stepped-up activity of non-governmental organisations. Under existing law, ecological organisations can assert demands for adoption of preventive measures or even cessation of operations posing a threat of harm. An awareness of threats to nature is resulting in increased social activism and consciousness of negative impacts, as can be clearly observed in the statistics for cases of this sort.

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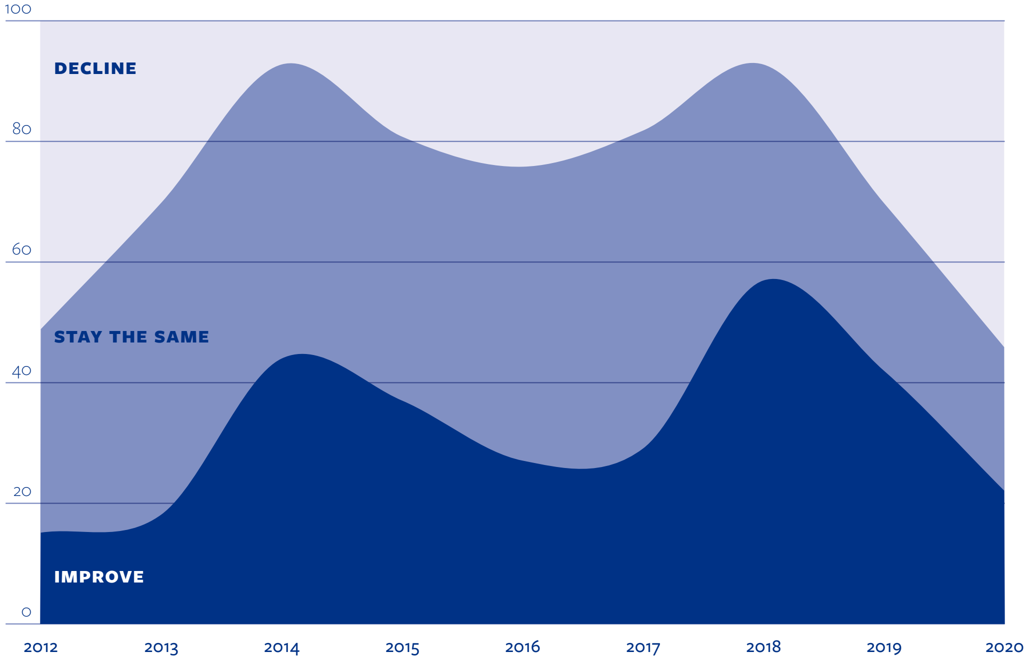
WILL GLOBAL ECONOMIC GROWTH…



Source: *23rd Annual Global CEO Survey*, PwC

Think of the bottom line —for the environment

> Every industrial activity, to a greater or lesser degree, directly or indirectly, exerts a negative impact on the environment.

The clearer and clearer asymmetry in obligations will be an impetus driving the introduction of legislative changes and imposition of duties on businesses connected with combatting biodiversity loss. It is primarily commercial activity that contributes to worsening of ecosystems, environmental harm and loss in natural values (particularly in the industrial and transportation sectors), but obligations to improve and recultivate the environment are imposed almost exclusively on states. The burden of taking specific actions will thus be shifted to commercial entities.

Business should appropriately estimate the threats, take action to minimise risk, and observe the new legal obligations. But in the eyes of many, that is not enough. Today corporate environmental policies are focused at most on a lack of negative impacts on the environment ("no net loss"—NNL). But the aim should be to pursue actions achieving positive change and overall improvement in nature ("biodiversity net gain"—BNG). After all, every industrial activity, to a greater or lesser degree, directly or indirectly, exerts a negative impact on the environment. This should be balanced by consciously undertaken measures supporting protection of natural resources, resulting in the final balance in benefits for nature. In the case of new development projects, such an instrument could be a specific obligation to include environmental protection aspects above and beyond the minimum requirements for conducting assessments of impacts on the environment or Natura 2000 areas.

But in essence, even actions aimed at generating natural benefits may prove insufficient. This is because biodiversity and the environment do not have a value that can be expressed economically. Thus, on the surface, their loss or destruction does not cause financial detriment. Only a recognition that the environment has value in and of itself, regardless of whether it can be economically exploited by humans for gainful, commercial or consumption purposes, can change the outlook on this issue. Only an understanding of the essence of these values—intrinsic values—will disclose the true balance of the environmental impact of activity, which may prove negative notwithstanding ambitious environmental policies.

Time for brass tacks

Concrete legal obligations increasing business's participation in the protection of nature will appear in the upcoming years. The biodiversity summit planned for 2020 in the Chinese city of Kunming has been postponed for a year, but the virtual meeting of heads of state and heads of government devoted to biodiversity during a session of the United Nations in September 2020 openly declared that the upcoming conference of parties to the UN Convention on Biodiversity must do for biodiversity what the Paris conference did for the adoption of climate obligations.

Halting biodiversity loss, and managing ecosystems on earth, must become a permanent element of political resolutions at the international level. Newly established targets for the period following 2020 will become a key component of obligations assumed by individual member states, which should translate directly into obligations for business. Financial markets will be engaged in these actions to ensure their responsibility for shaping the directions of investments. Protection of nature is to be a decisive factor on financing and permitting development.

The similarity to the Paris Agreement is to be manifest through the implementation of national biodiversity strategies and action plans (NBSAPs). Measures are intended to foster the growth of the circular economy, and green recovery policies should include recultivation of ecosystems and appropriate targeting of financial streams toward supporting environment-friendly solutions, in private financing as well as, for example, public procurement.

The conclusion of these deliberations is clear: there is no more room for business as usual. Combatting the impacts of climate change and biodiversity loss will not be enough to solve environmental problems. It will be essential to remodel economies and how enterprises function within them.

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Time for self-generation of electricity?

The European Union is striving to achieve climate neutrality by 2050, which is strongly impacting the costs of generating power from fossil fuels. This is particularly evident in Poland, where about 70% of electricity is still generated at coal-fired power plants. Moreover, the price of CO_2 emission rights have returned to the path of rapid growth, causing a dynamic increase in electricity prices. Firms are therefore seeking an alternative to buying all their electricity from grid suppliers.

No more cheap power for end users

At the end of 2020, the European Union decided to raise its climate ambitions and cut CO_2 emissions not by 40%, but 55%, from 1990 levels. According to the National Centre for Emissions Management (KOBiZE), this will cause an increase in the price of emission rights to EUR 52 per tonne of CO_2 equivalent, contributing to further growth in costs for the industrial sector.

Another driver of the increase in electricity prices is the launch of collection of capacity fees introduced by the Capacity Market Act of 8 December 2017, designed to finance the availability of electricity supplies in critical instances. From 1 January 2021, electricity customers other than households will have to pay a capacity fee of PLN 76.20 for each MWh taken from the grid during the hours of 7:00 am – 10:00 pm.

These factors, combined with technological development, affordability and ease of operation of devices for generating electricity, are leading enterprises consuming significant quantities of electricity to decide on self-generation—producing electricity for their own needs.

A factor not previously observed in Poland, but driving the growth in self-generation in more developed countries, is consumer preferences and corporate policies, favouring or explicitly requiring products to be produced exclusively from energy from renewable sources.

Cogeneration

A common solution, particularly at industrial and manufacturing plants, is cogeneration, i.e. combined production of electricity and heat. One motivation for enterprises to build their own cogeneration facilities was the introduction of best available techniques (BAT) at the EU level, forcing a reduction in polluting emissions and replacement of old boilers producing steam for industrial uses.

Production of power and heat in high-efficiency cogeneration is an activity that requires a cogeneration concession from the Polish regulator (the president of the Energy Regulatory Office (URE)). Unlike generation of electricity from renewable sources, cogeneration of power and heat requires a concession regardless of the capacity of the installation.

The Act on Promotion of Electricity from High-Efficiency Cogeneration of 14 December 2018 distinguishes between cogeneration facilities based on the installed capacity and degree of modernisation of the unit. Depending on these characteristics, support may take the form of:

- Cogeneration bonus awarded by auction
- Bonus guaranteed by the regulator based on an application
- Guaranteed individual bonus awarded each year by the regulator
- Individual cogeneration bonus awarded each year by the regulator.

Concession-holders producing electricity in high-efficiency cogeneration must file an annual report with information on the quantity of power generated, introduced into the grid, and sold.

Renewables

The growth in self-generation has accelerated greatly along with the dynamic growth of the renewables sector and the affordability of renewables installations. The ease and automation of operating such installations, particularly photovoltaic units, has encouraged enterprises to begin making use of available areas or neighbouring properties for balancing their electricity needs. These factors, combined with low borrowing costs, have driven growth in the interest in renewables installations acquired on credit, repaid from the savings in the costs of buying electricity. The ecological aspect of these solutions is also relevant.

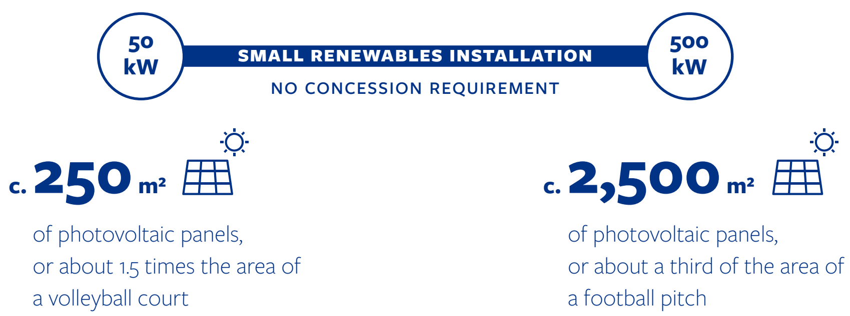
Generation of power from one's own renewables installation, unlike high-efficiency cogeneration, under current law requires a concession for generation of electricity only for installations with a capacity greater than 500 kW. This figure is expected to be increased soon to 1 MW, as work is currently underway in the parliament to raise the threshold for this requirement. As a rule, large consumers of power consider installations with a capacity of several megawatts.

With a view to investors seeking to save on their power bills but not wanting to be subject to concession duties, the law defines a small renewables installation as a device with an installed capacity of greater than 50 kW but no greater than 500 kW (soon, no greater than 1 MW). Operators of such installations must apply to the regulator for entry in the register of generators of electricity at small installations. Unlike a decision to issue a concession, entry in the register is a decision binding on the regulator. This means that if the application is complete, the president of the Energy Regulatory Office cannot refuse to enter the producer in the register.

Self-balancing

Unfortunately, generation of power at a photovoltaic installation rarely coincides with an enterprise's need for electricity. This is because generation depends on variable weather conditions, which cannot be predicted over a longer timeframe. Thus generators of electricity from photovoltaics often must limit their production of power to avoid the need to release their overproduction into the grid, or sell unused power to a buyer of their choosing or on the Polish Power Exchange (TGE).

Battery storage for power, more and more common and affordable, offers a solution to this dilemma. These systems absorb electricity during periods of overproduction and release it when there is increased demand. Thanks to their flexible operation, they can immediately start powering devices when the photovoltaic generation ceases to function efficiently due to the time of day or the weather. Thus teams of generating devices and batteries can guarantee constant and increasingly affordable independence from steadily rising electricity prices.



The recast Renewable Energy Directive (Directive (EU) 2018/2001 on the promotion of the use of energy from renewable sources), known as RED II, imposes on member states an obligation to simplify procedures for storage of energy from renewable sources, and also to allow private entities to use storage facilities without being subject to double fees, including grid fees for storing electricity remaining within the private entities' structures.

Tenancy or leasing of installations

Enterprises without sufficient funds on hand and not wishing to take out loans to purchase a self-generation installation still have opportunities to optimise their electricity costs—thanks to Art. 9 of the Renewable Energy Sources Act of 20 February 2015. Under this provision, the owner of a renewables installation only needs to hold "legal title" to the installation. This is a much broader notion than outright ownership. The installation may also be used on the basis of a tenancy or leasing contract. There are now many entities on the market offering services of this type.

Lessors often offer additional services of upkeep and maintenance of installations, and also assist in completing the administrative duties, which, although greatly simplified, still may pose difficulties. Unfortunately, in a position issued on 12 February 2021, the president of the Energy Regulatory Office equated such lessors with energy undertakings, which may mean that many additional duties will be imposed on them, such as the requirement to obtain a concession for trading in electricity. Under a contract for lease or tenancy of the installation, the rates can also be set with great flexibility, either as a fixed price adjusted by the inflation index, or indexed to the market price of electricity, allowing for lower bills in a fixed amount. The rates also often depend on the period for which the contract is concluded.

Entrusting self-generation to external operators

In the case of complex self-generation systems of higher capacity (which require a concession from the regulator), or where a prospective generator has a more complex international ownership structure (often requiring submission to the regulator, and updating, of documents from multiple jurisdictions), users of electricity often outsource self-generation at their own plants to Polish entities as operators of such installations. In that case, the equipment is sourced and installed by the user of power and heat, while full technical staffing, servicing, aid in obtaining a concession, and fulfilment of reporting obligations is provided by the external operator. Because of the scale of their business, the operator can offer reasonable fees and responsive, professional service. As the installation is located on or adjacent to the customer's property (onsite or near-site), the power or heat can be sold directly into the customer's network. For these reasons, the price is not subject to high distribution fees and there is no inconvenience associated with the presence of a third party in the entire arrangement.

Generation and demand are settled between the customer and the external operator based on typical commercial contracts, under which the customer receives cheaper electricity and the operator receives an appropriate fee for operating and maintaining the installation.

Demand-side response and sale of electricity on the market

An undoubted advantage of self-generation is the opportunity for enterprises with such units to participate in the demand-side response (DSR) market. DSR programmes are designed to encourage customers to adjust their consumption of power to fit the capabilities of generating resources, facilitating the balancing of the power system in extreme situations or when there is such a need. The enterprise receives an appropriate annual fee for its readiness to reduce demand. An enterprise with its own self-generation units, particularly cogeneration, has a broader spectrum of tools at its disposal to offset its demand for power from the grid, and thus can participate more actively in the DSR market.

Another potential advantage of having self-generating units is simply the ability to sell electricity to the grid, particularly at periods of peak demand, i.e. at the highest price.

Summary

Technological progress and the unprecedented growth in the use of digital technologies is occurring across countless areas. This is visible in the energy sector. After decades of hegemony by a few giant enterprises, personified by huge power plants, the time has come for change. By tailoring their generation of electricity to their own consumption levels, enterprises can not only save money, but also have a real impact on their environment.

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Control of investments in Poland: Additional protection against takeovers

Shield 4.0 has significantly expanded the system for control of investments in Poland. The new instrument is intended to protect against takeovers during the uncertain times caused by the COVID-19 pandemic. M&A transactions will require caution and careful verification whether the proposed transaction is subject to the new regime and the obligation to obtain additional prior approval from the competition authority, irrespective of any potential concentration-related approval.

The COVID-19 pandemic has been a period of intense changes in law in response to the new reality. Part of this has been the government's introduction of a series of "shields" protecting the economy from the effects of the pandemic, including Shield 4.0, which, among other things, changed the rules for control of investments.

In Poland, the investment control system was in place prior to the pandemic. It was created by the Act on Control of Certain Investments, adopted in 2015, requiring review of acquisitions of companies deemed vital to the Polish economy. That act created a control mechanism independent of the concentration control carried out by the Polish competition authority (the president of the Office of Competition and Consumer Protection (UOKiK)) to combat consolidation resulting in a significant reduction of market competition. Shield 4.0 has significantly expanded this system by amending the Act on Control of Certain Investments.

In its original form, the 2015 act covered entities of strategic importance for the Polish state. In this respect, control has been and still is exercised by the ministers indicated in the act. It is aimed at assessing whether obtaining dominance or significant participation in a protected Polish entity by an entity from outside the European Union is a threat to:

- Public order or security
- The country's defence capabilities
- Satisfaction of vital needs for protection of the life and health of the population.

SHIELD4.0

Act on Interest-Rate Subsidies for Bank Loans to Businesses Affected by COVID-19 and the Simplified Procedure for Approval of Arrangements in Connection with Occurrence of COVID-19

The entities considered strategic under the detailed criteria set out in the act were included in a list of entities subject to protection, established by a regulation of the Council of Ministers. Currently, the list includes 13 companies of strategic importance for the state, such as KGHM Polska Miedź SA (copper), PKN Orlen SA (petroleum), and Grupa Azoty SA (fertilizers). As this is an exhaustive list, there is no doubt which companies are covered by the act.

The existing control mechanism for foreign investments will remain in place. Investment control in relation to strategic companies, protected under the government regulation, will continue to take place in accordance with the control criteria currently in force, in proceedings conducted by the same competent ministers.

Shield 4.0 has created a new, standalone control system. It will apply only to entities not subject to investment control under the existing rules.

Who will be covered by the new rules, and for how long?

The new investment control procedure related to the COVID-19 pandemic will remain in force for two years, and is implemented by the president of UOKiK. Its aim is to ensure that public order, security and health considerations are respected when significant participation or dominant status is obtained in protected companies. Investment control in connection with the COVID-19 pandemic applies to investors from outside the European Union who have not had a registered office for at least two years preceding the notification within the European Economic Area or in member states of the Organisation for Economic Co-operation and Development.

The list of countries from which investors will be subject to control is long. In particular, it includes Asian countries with the exception of Japan and Korea, as well as Russia, Ukraine, all African countries, most South American countries (including Brazil), all Middle Eastern countries with the exception of Israel and Turkey, and a number of other countries.

The control procedure does not contain an exhaustive list of the entities to which it applies. Protection is extended to all entities that meet both of two criteria.

The first criterion is revenue from sales and services in Poland equivalent to EUR 10 million or more in either of the two financial years preceding the notification. This value is comparable to the criterion relevant to merger-control proceedings conducted by the president of UOKiK.

The second criterion is that the protected entity meets any one of the following characteristics:

- It is a public company
- It holds property included in the consolidated list of facilities, installations, equipment and services deemed to be critical infrastructure
- It conducts business in an area defined extremely broadly by the new regulations:
  - Developing or modifying software with applications for meeting public needs
  - Provision of data collection or processing services in cloud computing
  - Production or distribution of electricity, natural gas, or heat
  - Production, certain types of transport, transmission, storage and trade in petrol, diesel, natural gas, or gas fuels
  - Manufacture of chemicals and chemical products
  - Manufacture and trade of certain products and technology for military or police purposes
  - Extraction and processing of metal ores used in the manufacture of the aforementioned products
  - Transhipment in ports of fundamental importance to the national economy
  - Transhipment in inland ports
  - Telecommunications
  - Production of medical devices, apparatus and instruments
  - Production of medicines and other pharmaceutical products
  - Processing of meat, milk, cereals, fruit and vegetables.

In practice, this means that the control will extend to thousands or even tens of thousands of Polish entities. In addition, such broad criteria may make it difficult to assess whether or not a given entity will meet a criterion.

The first decision on this form of investment control was issued in October 2020 in favour of a buyer from the Cayman Islands, concerning Centrum Rozliczeń Elektronicznych Polskie ePłatności SA, a provider of payment processing services. The president of UOKiK did not object and found it unnecessary to apply control in this case.

Ex ante control, indirect and subsequent acquisition

Proceedings before the president of UOKiK will be initiated on the basis of a notification submitted by an investor intending to obtain dominant status or significant participation in a protected entity, as those terms are defined in Art. 3 of the Act on Control of Certain Investments.

Ex ante control will also be exercised in cases of acquisition of dominant status or significant participation indirectly through subsidiaries controlled by the investor, or in cases of acting in agreement, even verbally, or through a trustee.

In such case, the notification will be submitted by the subsidiary or other entity taking actions resulting in the indirect emergence of dominant status or significant participation, or by all members of the agreement as to joint action towards the protected entity or an entity with a dominant relationship towards the protected entity.

Subsidiaries of investors from outside the EU with no registered office in an EEA or OECD member state will also be subject to the same obligations as the investors themselves, even if the subsidiaries are registered in Poland. If indirect acquisition of dominance or significant participation subject to control takes place as a result of an act carried out on the basis of laws of a foreign country, in particular as a result of a merger of companies registered in a foreign country or acquisition or taking up of shares in such companies, then the subsidiary with dominance or significant participation in a protected entity will be obliged to notify the president of UOKiK of the relevant event after the fact. In such case, the president of UOKiK may issue a decision prohibiting the exercise of rights acquired on the basis of acts or events covered by the *ex post* notice.

We know from practice that subsidiaries may have difficulties meeting reporting obligations because, as in the case of obligations concerning beneficial owners, subsidiaries do not always have information on the changes giving rise to the reporting obligations.

Circumvention-of-law clause

The president of UOKiK will be able to commence an examination procedure at the regulator's own initiative if there are indications of abuse or circumvention of law. In particular, this will be the case if an entity acquiring significant participation or dominance does not actually carry out economic activity on its own behalf other than that relating to acquiring significant participation or dominance, or does not have a permanent establishment, an office or staff in the territory of a member state. In these cases, proceedings at the regulator's initiative will not be commenced only if 5 years have passed since significant participation or dominance was established.

Timeframe for control proceedings

As a result of investment control proceedings, the president of UOKiK will issue a decision stating no objection to the intention to obtain dominant status or significant participation in a protected entity. The deadline for issuing this decision is 30 days as part of initial proceedings, i.e. if the case does not require additional control proceedings. If control proceedings are conducted, the president of UOKiK will issue an investment control decision within a total of 150 days from initiation of the proceedings.

Sanctions

Legal acts carried out despite an objection raised by the president of UOKiK or without the required notification will be null and void. Additionally, criminal sanctions are possible, such as fines of up to PLN 50 million, imprisonment for a term of 6 months to 5 years, or both.

STRATEGIC INVESTMENT CONTROL SYSTEM IN POLAND:
ACT ON CONTROL OF CERTAIN INVESTMENTS

Prior to Shield 4.0	Under Shield 4.0
OBJECTIVE control of takeovers of companies vital to the Polish economy	**OBJECTIVE** control of acquisition (directly or indirectly) of dominance or significant participation in Polish companies by investors from outside the EU/EEA/OECD
RELATES TO 13 entities of strategic importance for the state (such as Grupa Azoty SA, KGHM Polska Miedź SA, PKP Energetyka SA, Tauron Polska Energia SA, and PKN Orlen SA)	**APPLIES TO** thousands of Polish entities meeting both of two criteria: • Revenue of EUR 10 million or more in Poland • Public company status or holding critical infrastructure assets (difficult to determine) or carrying out specific activities (very broad scope)

Assessment of regulation

Without applying the procedures for access to classified information, an investor intending to obtain dominance or significant participation in a Polish company will not be able to determine whether the relevant transaction is subject to notification of the president of UOKiK under the provisions on control of certain investments.

Obligations related to the verification of whether it is necessary to make a notification resulting from the amendment to the Act on Control of Certain Investments will be far-reaching, and in many cases may even prove impossible to perform properly. This is due to the broad definition of protected entities, the extension of control to cases of indirect acquisitions of dominance or significant participation, even as a result of an oral agreement by a group of investors, as well as subjecting transactions to control involving entities registered in the EU, EEA or OECD but controlled by entities from outside these areas.

The list of practical problems likely to arise from the imprecise new provisions, raised during the drafting phase, is long and probably not exhaustive. For example, it is unclear what the management of a Polish company must do to protect against liability for failing to report a secondary acquisition, and what initiative Polish management have to take to verify information about changes in the structure of the group (a problem generally similar to reporting changes in beneficial owners).

Another good example is investment control of companies owning critical infrastructure. According to the Crisis Management Act of 26 April 2007, the consolidated list of objects, installations, devices and services constituting critical infrastructure is covered by a classified information clause, and information on the inclusion of a given property or service on this list is provided only to public administration bodies with tasks included in the national critical infrastructure protection programme, and owners and holders of the relevant property. Thus, without applying the procedures for access to classified information, an investor intending to obtain dominance or significant participation in a Polish company will not be able to determine whether the relevant transaction is subject to notification of the president of UOKiK under the provisions on control of certain investments.

The new regulations may greatly impede the process of acquiring control over Polish companies, regardless of who currently controls them and who intends to acquire their shares. This will make access to capital more difficult and increase transaction costs.

It will take time to check whether the amended provisions of the Act on Control of Certain Investments will apply to a given transaction. Collecting the information necessary to make an appropriate notification to the president of UOKiK, and conducting proceedings before the regulator, will take even more time. On top of this, some provisions of the act cannot be interpreted unequivocally.

As a result, the new rules will have to be taken into account when carrying out transactions involving a truly vast set of entities. Transactions will have to be carried out with great care, especially since the potential sanctions are drastic.

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Systemic limitation on liability of public authorities in Poland

The existence of rules for liability of public authorities is a feature distinguishing democracies from other legal systems. But sometimes a broad scope of state liability does not translate into a real possibility of obtaining damages.

Civil liability of public authorities has not always been a feature of the legal system, in Poland or other countries around the world. It was only over time, along with the appearance and growth of democratic political systems, that it was accepted by national legislatures that the state can also act illegally, thus infringing the rights of individuals. It was gradually acknowledged that unlawful action may be manifest in abuses by state officials, inaction, or even defectively drafted laws. Ultimately it was recognised that unlawful activity by public entities may lead to material injury to entities subject to public authority. Thus regulations and legal mechanisms were introduced with the aim of compensating for injuries arising as a result of defective actions by public entities.

The need to redress injuries to the assets of private parties also arises in situations connected not so much with defective action by the authorities, as by the occurrence of unforeseeable natural phenomena (flood, drought, epidemic, and so on). In such situations states also assume the burden and responsibility of compensating for the resulting losses.

The development of regulations governing the liability of public authorities was a natural outgrowth of, among other things, the introduction of the administrative court system, tasked with oversight of the public administration, the establishment of constitutional courts reviewing the constitutionality of legislation, and the creation of international courts protecting human rights. The inclusion in countries' legal orders of rules for the liability of public authorities became a feature distinguishing democracies from other legal systems.

In theory: a broad scope of liability

Polish legislation includes a range of regulations under which damages can be sought from the public authorities. These provisions are mainly found in the Civil Code, but also in other acts. A theoretical legal analysis of these regulations indicates quite broad grounds for the liability of public authorities across a number of areas of the functioning of individuals. As a rule, the state should redress actual loss (*damnum emergens*), but also lost benefits (*lucrum cessans*). Injury is redressed through the courts and in some situations through administrative routes. In theory.

In practice: limited possibility for redressing injuries

The practice shows that injury is not always redressed in situations provided for by Polish law. Indeed, there is a noticeable systemic tendency to narrow this liability. This is not caused solely by changes in law, but rather by how the law is executed.

The difficulty in pursuing claims for damages is tied primarily to the nature of public authority as the entity obliged to redress the injury. This is an entity that due to the power it holds (legislative, executive and judicial) has vast and essentially exclusive influence over shaping the actual scope of its own liability. Moreover, this entity is perceived as requiring special protection and different, preferential treatment. After all, public authority administers national property, functions on the basis of the public budget, invests in the country's infrastructure, and finances education, the health service, the armed forces and so on. The practice shows that the financial capabilities of the state are regarded in court decisions as an additional negative ground limiting or excluding the liability of public authorities.

The financial capabilities of the state are regarded in court decisions as an additional negative ground limiting or excluding the liability of public authorities. This is enough to make the battle for damages through the courts a lopsided affair.

This reason alone is enough to make the battle for damages through the courts a lopsided affair.

It is in the interest of public authority to maintain control and a real influence over the number and level of claims for damages asserted by injured parties. To this end the state exploits certain instruments which for many years have allowed it to interfere in the very possibility of initiating procedures for pursuing claims, in certain situations resulting in outright stripping claimants of this possibility. Examples of such measures are presented below.

Undeclared states of emergency

An advantageous geographical location protects Poland against the biggest natural disasters. Nonetheless, natural phenomena occur every few years in Poland causing significant harm to the property of citizens and enterprises. There were widespread floods in 1997 and 2010. In other years there have been detrimental events in certain areas of the country (such as droughts and windstorms). Despite the objective existence of a state of emergency, no state of emergency was declared in any of these instances as provided for in Art. 228 of the Polish Constitution, i.e. a state of natural disaster regulated in detail in the State of Natural Disaster Act of 18 April 2002 (or in relation to the floods in 1997, the State of Emergency Act of 5 December 1983). In relation to events occurring after entry into force of the current Constitution in October 1997, declaration of such a state would require the public authorities to pay compensation (the rules for which are regulated in the Act on Compensation for Material Losses Resulting from Restrictions During a State of Emergency on Freedoms and Human and Civil Rights of 22 November 2002). Thus as there was no legal obligation on the part of the state to redress these injuries, no claims arose on the part of the injured persons to apply to the province government and then the state court to enforce such claims.

Instead of exercising the laws regulating states of emergency, the public authority adopted special regulations governing state financial assistance for persons injured in successive natural disasters. However, these regulations did not create rights to enforce financial support, but only authorised persons to apply for state assistance, the scope of which was greatly restricted when compared to the extent of losses actually incurred (e.g. supplementary payments, loans, and special-purpose benefits). The payment of compensation thus occurred under conditions and rules imposed ad hoc by the public authority.

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The public authorities adopted a similar practice in 2020 in connection with the COVID-19 pandemic. In this situation as well, no state of emergency provided for in the Constitution was declared. Instead, a series of acts and regulations were adopted or amended, which on the substantive level adapted the existing regulations involving constitutional states of emergency, but within the framework of a state of epidemiological threat or a state of epidemic. In each of these instances, the failure to introduce a constitutional state of emergency resulted in depriving injured parties of a realistic possibility of seeking redress from the state for injuries arising in this crisis.

When there is no legal obligation on the part of the state to redress injuries, no claims arise on the part of the injured persons to enforce such an obligation.

Hyperactivity of the legislative and executive branches

Another manifestation by the authorities of measures aimed at the practical limitation of the possibility of seeking damages from the state is two applications to the Constitutional Tribunal to examine the constitutionality of Civil Code Art. 417[1] §1 filed in 2020, almost simultaneously, by the Speaker of the Sejm and the Prime Minister (cases K 18/20 and K 21/20). The impetus to file these applications was the possibility that Polish businesses would seek damages due to the restrictions on commercial activity introduced under regulations concerning the COVID-19 pandemic. The applicants seek a declaration that Art. 417[1] §1 is unconstitutional insofar as it allows the ordinary courts to issue a ruling on their own, for purposes of proceedings seeking damages, holding unconstitutional a normative act whose adoption gave rise to the injury in question.

If the tribunal adopts that position, it would deprive injured parties of the possibility of obtaining damages on the basis of that provision of the Civil Code. But the mere filing of those applications exerts a paralysing effect on potential plaintiffs in cases against the public authorities. It postpones their obtaining an eventual judgment in their favour, but also increases the risk of a negative result in the litigation, and thus exposes them to the loss of significant funds invested in pursuing that litigation.

Reprivatisation legislation

The liability of the public authorities in the area of reprivatisation has been effectively limited as a result of lawmakers' teaming up with the Constitutional Tribunal. Through the Act of 25 June 2015 Amending the Real Estate Administration Act and the Family and Guardianship Code, many pre-war property owners and their heirs were practically stripped of ownership of buildings originally seized by the communist authorities after the Second World War. Although

REGULATIONS INVOLVING PARTICULAR TYPES OF NATURAL DISASTERS

- Act on Support for Enterprises Affected by the 2010 Floods of 12 August 2010
- Regulation of the Council of Ministers of 26 July 2011 on Specific Conditions for Realisation of the Programme of Aid for Agricultural Families on Whose Farms or Plots for Special Agricultural Production Injury Has Occurred Due to Windstorm, Cloudburst or Spring Frosts in 2011
- Act on Special Solutions Connected with Removal of the Effects of the 2010 Floods of 24 June 2010
- §13 of the Regulation of the Council of Ministers of 27 January 2015 on the Detailed Scope and Methods of Realisation of Certain Tasks of the Agency for Restructuring and Modernisation of Agriculture

REGULATIONS INVOLVING THE COVID-19 PANDEMIC

- Amendment of the Act on Prevention and Combating of Infections and Infectious Diseases of 5 December 2008
- Regulation of the Minister of Health of 20 March 2020 Declaring a State of Epidemic in the Territory of the Republic of Poland
- Act on Specific Solutions for Preventing, Combatting and Counteracting COVID-19, Other Infectious Diseases, and Resulting Crises of 2 March 2020 (with successive amendments)

this amending act was dubbed the "little reprivatisation law," it led to de facto expropriation without any compensation, even though the Constitution permits expropriation only with adequate compensation. Nonetheless, the Constitutional Tribunal upheld the act in its judgment of 27 July 2016 (case no. K 3/15).

These efforts are carried forward by the subsequent "little reprivatisation law," the Act of 17 September 2020 Amending the Act on Specific Rules for Eliminating the Legal Effects of Reprivatisation Decisions Concerning Warsaw Real Estate Issued in Violation of Law, the Act on Commercialisation and Certain Employee Entitlements, and the Real Estate Administration Act. This amending act further stripped former owners of opportunities for recovering rights to real estate unlawfully taken over by the state.

Termination of investment treaties

Another phenomenon limiting the liability of public authorities to private entities is the successive termination by Poland of bilateral investment treaties, on the basis of which foreign investors could pursue redress of injuries caused by the action of public authorities in Poland through international arbitration.

Termination of these treaties was tied to issuance by the Court of Justice of the judgment of 6 March 2018 in C-284/16, *Achmea*, under which inclusion of an arbitration clause in BITs was deemed inconsistent with EU law. A number of these treaties provide that they will continue in force for a certain period following submission of a notice of termination, and thus for several more years some of these treaties will continue to provide a basis for claims for damages against Poland.

A litmus test for democracy

Pursuing claims for damages against the state has never been an obvious or easy matter. It has usually required complex litigation to be conducted over many years, and these cases have rarely been susceptible to resolution through any amicable settlement. It is justified to conclude that the measures pursued by the public authorities, observed for many years, are systemic in nature. This demonstrates a change in the state's attitude toward the responsibility it has acknowledged toward private entities. The COVID-19 pandemic, driving the state into debt and worsening its budgetary position, will undoubtedly only exacerbate this trend.

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Can epidemic claims be pursued in a class action?

During the first and second waves of the coronavirus, various restrictions were placed on personal and professional life. Businesses wonder whether they can seek compensation from the State Treasury for losses caused by restriction or prohibition of business activity without introduction of a state of emergency.

Could such compensation claims also be pursued in class actions?

Damage to businesses during the epidemic

The Polish legal system provides for liability of public authorities for legal damages. This concept is applied in the theory of civil law to pecuniary loss resulting from actions of state or local government bodies in compliance with the law. It is also undisputed that liability for this type of tort is exceptional and special. The businesses' pecuniary losses must be found to have their source in sudden legislative actions of the state, under which the state imposes restrictions on their activities. Restrictions might take the form of additional obligatory expenses (e.g. purchase of disinfectants) or even a partial or total ban on certain business activities (e.g. the hotel or event industry).

It seems that if the state, in the interest of the common good, restricts or prohibits certain business activity, it should at least partially compensate the businesses for their resulting losses. The Polish Constitution envisages such a solution, under which, in the case of specific threats, when ordinary constitutional measures are insufficient, it is possible to introduce a state of emergency, where individual freedoms and rights of citizens may be restricted. In that case, the actual material damage caused by those restrictions (including to the freedom of business activity) must be compensated. This provision of the Constitution is implemented in the Act on Compensation for Material Losses Resulting from Restrictions During a State of Emergency on Freedoms and Human and Civil Rights of 22 November 2002.

No state of emergency has been declared in Poland in connection with the COVID-19 pandemic. However, there is a debate underway on whether, under the notion of dispersed constitutional review, the common courts may on their own determine the unconstitutionality of provisions of particular normative acts, thus making it possible to file an effective claim without first obtaining a predicate ruling in the form of a judgment of the Constitutional Tribunal. (Currently, the Prime Minister has submitted an application to the Constitutional Tribunal to examine the constitutionality of Art. 417[1] §1 of the Civil Code insofar as it does not require a finding of unconstitutionality by the Constitutional Tribunal.)

The possibility to seek compensation from the State Treasury is also provided for in the general provisions of the Civil Code (Art. 417 and following).

Assuming that general provisions of the Civil Code, in conjunction with the possibility of dispersed constitutional control, entitle businesses to file effective claims for losses caused by these restrictions, it is also worth considering whether the Class Actions Act of 17 December 2009 would apply to such claims. One of the undoubted advantages of class actions is the economy of proceeding in this form, due to the greatly reduced court costs.

Unification of claims may lead to a reduction in the amount of claims by some class members.

Nature of class actions

Claims for damages arising out of a wrongful act (tort) may be asserted in a class action if they are brought by at least 10 persons and their claims are based on the same or similar factual grounds. This concerns a situation where there is a common nexus between the members of a group based on the unity of the event giving rise to the loss (e.g. the same restrictions on conducting business activity). The case law recognises that this will be a state where there are facts in common (a premise in the broad sense). At the same time, the relevant circumstances must support a claim common to all claimants. This primarily means basing claims on similar events (which corresponds to the notion of an identical factual basis, which is an element of formal joint participation). Thus it appears that in the reality of pandemic claims, a 10-person claimant group would have to consist of businesses engaged in similar activities (services with the same PKD business classification code) which were subject to the same restrictions. For example, this might be the hotel industry (PKD 55.10.Z or PKD 55.20.Z), organisation of trade fairs (PKD 82.30.Z), or catering (PKD 56.10.A and PKD 56.10.B).

A class action itself will be admissible only if the amount of the claim of each member of the group is unified by equalising the amount of the claim asserted by the members of the class or subclass (the unification of the amount of claims may take place in sub-groups of at least two persons). For this reason, in the field of pandemic torts, it may be difficult to assert claims, as each claimant may have suffered damage of a different amount. Therefore, it is reasonable to conclude that the unification of claims may lead to a reduction of the amount claimed by some class members (also in the case of creation of many relatively small subclasses).

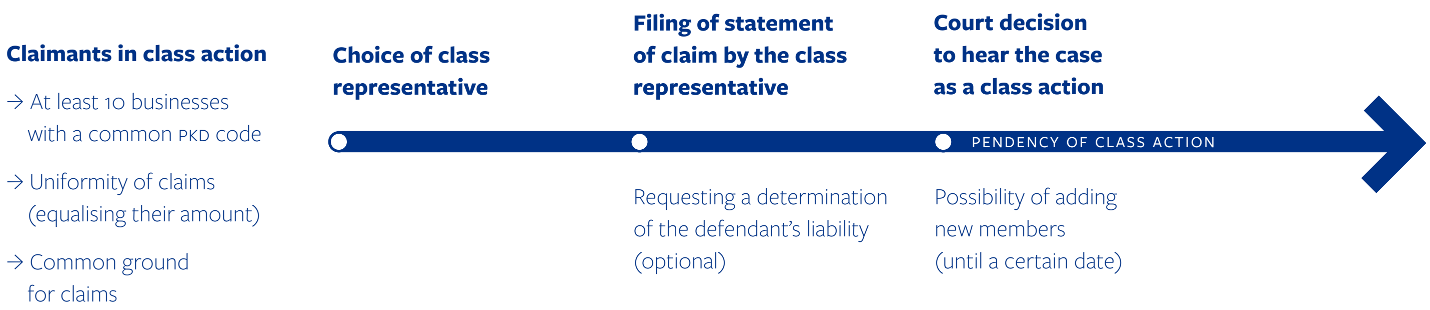
In pursuing a class action, the injured parties are in effect agreeing to some sort of common and identical lump sum of damages exhausting their claims. Legal commentators stress that consent to pursue a claim in a class action means exclusion of the possibility to pursue the claim individually, and waiver of a right to seek further-reaching »

BASIS FOR COMPENSATION CLAIMS

If in the future the Constitutional Tribunal rules that the Act on Counteracting and Combating COVID-19 (or other normative act restricting specific types of business activity) is unconstitutional, as orders and prohibitions were introduced (including closure of many branches of the economy) merely on the basis of executive regulations, even though Art. 31 of the Constitution expressly provides that this may take place only on the basis of a statute, then Civil Code Art. 417[1] §1 will undoubtedly provide grounds for State Treasury liability.

Another basis for claims for damages may be Civil Code Art. 417[1] §4 of the Civil Code, covering the situation where the "silence" of a legislative body (failure to act) is covered by the tort regime—in particular failure to introduce a state of emergency allowing businesses to claim compensation for restriction of their rights and freedoms.

JUDICIAL CLASS ACTION



satisfaction of the claim. Partial enforcement of claims in a class action is deemed inadmissible.

It is possible to limit the claims asserted under the Class Actions Act to seeking a determination of the defendant's liability for a specified event or events. In a class action, claimants do not have to demonstrate a legal interest in seeking a determination of the defendant's liability. At the same time, by allowing the claim to proceed, the court establishes the joint liability of the defendant to the class members for a specific event or events constituting prerequisites for the claims asserted by them.

As in a class action the claimant does not have to demonstrate a legal interest in a determination of liability, it is permissible to bring such an action also in a case where the claimant may bring an action for performance (including a demand for payment of money). Therefore, an application for determination of the defendant's liability may also be brought when pecuniary claims cannot be standardised in amount, or when determining the amount of pecuniary claims would involve excessive difficulties.

A class action must be brought by a class representative, who may only be a person who is a member of the class. He should conduct the proceedings in his own name but on behalf of all class members. When the decision that the case will be heard in a class action becomes legally final, the court will order announcement of commencement of the class action.

Joining the class after the deadline set by the court is inadmissible. As soon as the declaration on joining the class is presented to the court, a pending case will arise between the class member and the defendant with regard to the claim under the class action. A person who prior to commencement of the class action brought an action against the defendant for a claim that may be covered by the class action may file a declaration joining the class no later than the end of the proceedings at the first instance in the other litigation. Then the court in that case will issues a decision discontinuing those proceedings.

ANNOUNCEMENT OF COMMENCEMENT OF A CLASS ACTION MUST INCLUDE:

- Identification of the court before which the class action is pending
- Identification of the parties to the proceedings and the subject matter of the case
- Information that the class may be joined by further persons whose claims may be the subject of the class action—such persons must submit to the class representative a written declaration on joining the class; the deadline for submitting the declaration must be specified and must not be less than one month or more than three months from the date of the announcement
- Rules on attorney's fees
- Reference to the binding effect of the judgment on the class members.

Summary

For these reasons, it should be recognised that businesses may seek pandemic damages under the Class Actions Act. A group of at least 10 persons would have to be made up of businesses providing services under a common PKD code which suffered similar pecuniary loss from pandemic restrictions.

The rationale for uniformity of claims seems most troublesome, as it would require some businesses in the class to waive part of their claims. Nevertheless, a class action seeking to establish the liability of the State Treasury seems to be an extremely interesting solution. Then the judgment would constitute a predicate ruling for members of the class to rely on in individual lawsuits, where they could later demand damages based on the principle of full compensation, i.e. without limits as to amount.

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"Your people are taking bribes": What to do with this information?

Learning that corruption is occurring at a company is often met with disbelief. But such reports should not be taken lightly.

How should serious corruption charges be handled? How can companies prepare in advance for this eventuality? And what to do if the allegations turn out to be true?

A few years ago political scientist Francis Fukuyama wrote that the battle with corruption will be the biggest challenge in the 21st century. Fukuyama was referring to political corruption (when governments cease to serve their own citizens but become tools of violence serving corrupt leaders), but the point seems to apply equally well to corruption in business, which corrodes healthy competition, undermines social trust, and drives honest firms from the market.

In recent years we have increasingly observed scandals in which companies small and large have had to admit that they have become involved more or less knowingly in corrupt practices. States are no longer content with that, and are introducing harsher penalties and increasing funding for the operation of authorities combatting corruption. More and more, they also require enterprises to take active measures to combat corruption. In some jurisdictions companies have to introduce special anticorruption procedures and enable whistleblowers among staff and contractors to report irregularities anonymously. Here and there, companies are now being held responsible for failing to effectively combat corrupt practices. These trends are reaching Poland and are eagerly being adopted here.

When we hear that corruption may be occurring in our own company, our response is often disbelief. Questions arise: What to do with such a report? How to determine whether the allegations are true? How to prepare the company in case suspicion becomes fact?

Where to begin?

It is best to start with an action plan. It should answer four basic questions:

1. Who (inside and outside the company) should be informed of suspected irregularities?
2. Who should verify the allegations, and in what manner?
3. How great is the risk that if the allegations are upheld, the company will be exposed to legal liability or injury to its reputation—and what can be done to minimise the risk?
4. Is the company prepared to cooperate with state authorities, which may decide for example to conduct an inspection or search at the company?

Who should be notified, who should verify allegations and under what procedure?

Whom to notify

First and foremost, the management board of the company should be notified of suspected irregularities. In some companies, the shareholders are also informed. The company should determine whether there are other reporting obligations, and when they should be carried out. Listed companies may be required to disclose information to shareholders about allegations or procedures being followed. Such reporting may be delayed for the sake of the investigation, but it is essential to maintain control over the process. Group policies may require allegations to be reported to the parent company, particularly when the parent is covered by foreign anticorruption regulations. The company may also be required to report allegations to its insurer, as notification is often a condition for insurance coverage. Contractors may also have to be informed, if compliance with anticorruption policies is included in the parties' contract.

Team and external advisers

First, a team of people should be appointed to handle the matter. Not all companies have internal audit or compliance divisions or large legal departments. Conducting an investigation can be time-consuming and labour-intensive, particularly in the case of suspected corruption, so doing so with the help of staff from various divisions may distract them from handling their everyday duties. And the organisation may not have confidence in all of its personnel, particularly in light of the specific allegations.

For this reason, in practice many companies decide to engage an external adviser. This approach is followed more often when the nature of the allegations indicates that it will be necessary to pursue analytical or forensic measures. But external advisers will also need support from "inside." This means explaining how the company operates on a day-to-day basis, how it is organised, and what procedures (if any) it follows. Moreover, it is usually necessary for staff to collect the relevant documents and provide them to the external advisers.

Confidentiality

When engaging external advisers, the legal protection of information provided to them and the advice they provide must be considered. Proper protection of information concerning potential criminal offences is vital. The knowledge gained by an *adwokat* or attorney-at-law on the basis of information from the client, and the legal advice obtained by the client from the lawyer, are protected by attorney-client privilege. This does not mean that all documents and information concerning the case become confidential and cannot be obtained for example by law enforcement authorities. The authorities may obtain these for example through a search of the company's premises. But an *adwokat* or attorney-at-law cannot be interrogated concerning circumstances surrounding their delivery of legal advice (unless released from the privilege by the court, but that can only be done in special circumstances). Work product created by counsel while providing legal assistance (e.g. legal analysis of whether certain behaviour constitutes a criminal offence) also enjoys protection and as a rule cannot be collected by law enforcement authorities.

But when other types of experts are retained, such as forensic analysts, there may not be any special protection for the analyses they develop based on information obtained from the company. The situation is somewhat different if experts obtain certain information only with the aim of providing expert support to lawyers. The scope of attorney-client privilege is a complex issue and must be examined on a case-by-case basis to develop the safest model of cooperation for the company.

Documents

In most cases, clarification of the matter begins with gathering the relevant documents. It should first be determined what types of documents (including electronic data) the organisation has in its possession, the form in which they are stored, who has access to them, and whether they are at risk of loss. Some companies store all documents in digital form on a central server. But sometimes the organisation possesses certain documents only in paper form, often in a single copy on a shelf in one employee's office. In other instances, employees may possess documents on their desktop computers, company or private mobile devices or laptops, if they are approved to use such devices. If a suspected employee learns that an investigation is afoot, they may seek to get rid of incriminating information. The right strategy must be adopted to deal with this eventuality. In practice, such materials are often obtained under a pretext to avoid »

> **The most common follow-up actions are to discharge the dishonest employee, seek restitution from that person, and in specific situations notify state authorities of a criminal offence.**

arousing suspicions. But when obtaining data from devices provided to staff, regulations on protection of personal data and privacy, as well as internal policies, must be taken into account. If the company consents to employees' use of company devices for private purposes, access to the data on those devices may pose legal difficulties. A legal assessment must be conducted before obtaining emails or other data from electronic devices.

Analysis of the evidence

The collected and selected documents should then be analysed. How this will be conducted, and what the company will look for, depends on the specific case and the amount of preliminary information gleaned from the original notification. The more detailed the report, the greater the possibility of narrowing the search to certain individuals and events. Significantly, when launching an analysis, an investigative hypothesis should be adopted, i.e. an assumption of how an offence might have occurred, and then the evidence should be verified in light of this hypothesis. The preliminary assumptions may change as the analysis progresses and new information is obtained, but the absence of a guiding hypothesis will result in chaotic verification of a vast amount of information leading nowhere. It may be necessary to rely on expert support during the analysis (e.g. from forensic IT specialists, data analysts or auditors).

Investigative measures

Sometimes it will prove essential to engage private investigators, who can lawfully obtain certain information about suspects, particularly about their assets and their personal or financial ties with other suspects or other commercial entities. It must be borne in mind that verification of this information in the case of an employee is permissible only if the employer has formed a well-founded suspicion about the employee.

Interviews and confrontation

Analysis of documents and forensic measures will usually not suffice to verify reported irregularities. Interviews with employees, including suspects, will also have to be conducted. The interviewers must prepare both substantively and tactically. The tactic most often used is to interview the suspected employees at the end, when the company has already gathered information from all other sources. The employer may demand that employees cooperate and provide the requested information out of a duty of loyalty and for the good of the workplace. But employees cannot be forced to participate in such interviews. Refusal to participate may be grounds for further consequences, however, even up to and including termination of employment. If an employee agrees to "testify" voluntarily, he or she should be instructed on the nature and aims of the interview. If the interview is conducted by a lawyer, the employee must be aware that the lawyer represents the interests of the company and is acting on behalf of the company and not the employee. The interview is thus not confidential, but all information given will be shared with the employer, which may decide to pass on the information to others, including state authorities. In practice, employees sometimes participate in such interviews accompanied by their own lawyers.

Final report on the investigation

The investigation should end in drawing up a final report. The report describes the facts established, the irregularities identified, and the possible legal steps. The most common follow-up actions are to discharge the dishonest employee, seek restitution from that person, and in specific situations notify state authorities of a criminal offence. This report is generally submitted to the management board, which will then take the appropriate decisions. But if management board members themselves are implicated in corrupt practices, the report may instead be submitted to the supervisory board, or the owners.

> **A legal assessment must be conducted before obtaining emails or other data from electronic devices.**

Risk of negative consequences for the company

If the allegations of corruption are found to be true, this means there is legal and reputational risk to the company.

The company must determine whether the uncovered irregularities constitute a criminal offence and whether the company has a legal obligation to notify the relevant authorities of the suspected offence. Under current Polish law, in the case of both public and private corruption there is no legal duty to notify law enforcement authorities of information in the company's possession (there is only a "social obligation"). But it should be borne in mind that if public corruption is uncovered, a company employee implicated in giving a bribe may decide on his own to notify the authorities of the offence in expectation of receiving immunity.

Moreover, both public and private corruption is grounds for holding the company criminally liable as a legal person (under the Act on Liability of Collective Entities for Punishable Offences). A corruption offence committed by an employee or associate of the company may constitute a basis for criminal liability of the company itself. This liability will arise if the company obtained or could have obtained a benefit from the offence, even of a non-material nature, and the offence was related to the duties of the dishonest employee or associate and was committed as a result of improper selection or supervision or because the company's operations were not organised in a manner that would avoid commission of the offence.

Criminal liability of the company may result in severe sanctions: fines, certain prohibitions (e.g. against seeking public contracts), and even dissolution of the company. It is true that because of the need to obtain a prior final conviction of an individual, prosecutors in Poland very rarely charge companies with criminal offences. But proposed legislation shows that the state is seeking to change the rules for corporate criminal liability, to make it easier to prosecute and convict companies. The current act does not provide for any form of leniency for reporting offences. Thus if there is a risk of criminal liability for the company as such, the company must assess which method of proceeding will be the safest and most advantageous for it, bearing in mind the rights enjoyed by the company, particularly against self-incrimination.

A corruption offence committed by an employee or associate of the company may constitute a basis for criminal liability of the company itself.

Apart from criminal liability, the company must assess the risk of civil claims. It should determine whether actions of its employees have caused injury to third parties (such as another company) and whether the injured party could assert civil claims against the company.

Injury to the company's reputation if reports about corruption are published constitute an additional, non-legal risk to the company. Thus the company must be prepared for that situation and have a communication plan in place, including a draft press release ready for publication. In this respect, the company may seek support from communications experts as well as external firms or platforms for monitoring the media for publications about irregularities in the company. But it is essential that internal and external communications be consulted with the lawyers advising the company in the matter.

Heading off a crisis

Crisis management is difficult and time-consuming. If we wait until a crisis is actually occurring before drawing up rules and planning steps, we may overlook many significant issues and expose the company to added risk. Hence the Latin adage "If you seek peace, prepare for war."

Anticorruption policy and risk analysis

As part of preventive measures, implementing anticorruption procedures in your organisation should first be considered. Such procedures are not currently mandatory under Polish law. However, they can minimise the risk of occurrence of corrupt practices. It is also worth identifying what sort of corruption risks are likely to arise in your own company's operations, as they will differ depending on the sector, size, organisational culture, and other factors. Then it should be determined whether the company has appropriate controls and supervisory mechanisms in place.

But even the existence of such solutions does not guarantee that irregularities will not occur at the company and thus that the company will not be hit by such a crisis. Therefore the company should be prepared to deal with a crisis.

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Dawn raid procedure

The company should be prepared for a search and seizure by the authorities, particularly law enforcement. A "dawn raid" policy covering unannounced searches will protect the company from chaos and inappropriate behaviour by staff (e.g. destruction of documents or hindering the activity of officers), and will also designate the responsible persons who should be notified of the search. A lawyer should also be available "on call" so that at any hour they can came to the company to attend the search, monitor the officers' compliance with the regulations, and generally secure the company's interests.

Whistleblowing procedure

Whistleblowing policies are not currently mandatory, but this will soon change (when Poland implements the Whistleblower Protection Directive ((EU) 2019/1937)). But it is already worthwhile to implement such a procedure, bearing in mind that the key aim of such policies is to encourage employees and associates to report irregularities first inside the organisation, rather than taking them outside (to the media or law enforcement). Undoubtedly it is better for a company to learn of an instance of corruption first, so that it can take remedial measures, than to learn of it from press reports, or worse, in a notice from the prosecutor's office.

1 PREVENTIVE MEASURES

What to do in advance to be ready to investigate corruption charges?

- Draw up a risk map
- Create and implement an anti-corruption policy
- Create and implement a whistleblowing procedure
- Create and implement a dawn raid procedure

2 INVESTIGATION OF ALLEGATIONS

How to conduct the process after receiving a report?

- Appoint a team to handle the matter and notify the people who need to know of the report and the investigative measures undertaken
- Engage necessary external advisers (legal, data security, etc)
- Secure the evidence (documents, digital files)
- Analyse the collected evidence
- Conduct interviews with staff, including confrontation with suspects
- Draw up a final report on the internal investigation identifying the legal and reputational risks and the possible legal steps
- Prepare for the need to carry out internal and external communications

3 FOLLOW-UP ACTIONS

What to do if the allegations turn out to be true?

- Take a decision on notifying state authorities of the occurrence (law enforcement, regulators)
- Evaluate the risk of civil claims
- Enforce consequences against the perpetrator
- Improve internal organisation and procedures


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Electronic evidence still poses challenges

The existence of information technologies has been taken for granted for many years. Artificial intelligence, machine learning, cloud computing and blockchain are no longer news. But as usual, the law—particularly regulations governing judicial proceedings and the practice of judges themselves—has failed to keep pace with these developments. Use of electronic evidence in judicial proceedings remains problematic. But increasingly, the only available evidence of a fact may be a database that cannot be entirely reduced to a physical medium (or it would be highly impractical to do so).

Anyone today might find themselves in a situation where demonstration of certain facts (execution of transactions, theft of data, infringement of personal interests, or proper delivery of a digital product or online service) can be supported only by data existing exclusively in electronic form.

It is hard for the courts to find their way in this situation. They are not helped by regulations unsuited to contemporary existence, or at times outright archaic. On top of this, there are doubts connected with the protection of personal data.

What is electronic evidence?

Poland's Civil Procedure Code does not currently define the notion of "electronic evidence." Under European legislation, there is also a gap in defining and handling electronic evidence. Under Polish law, the regulation opening the way to a solution in this respect is Civil Procedure Code Art. 227, which provides: "The subject of evidence is facts relevant for resolution of the case."

Facts, in turn, mean any events or phenomena defined in space and time, but also states of the external world and states of an internal nature (e.g. connected with the human psyche), if their existence or occurrence can be objectively determined. The essence of evidence, and the facts arising out of it, is the possibility of independently recreating it at the stage of trial, enabling verification of whether a given fact actually follows from the given evidence. This raises the question of whether an electronic record, a sort of digital trail, meets

ELECTRONIC EVIDENCE
Information recorded or transmitted in digital form

LOCATION OF RECORD

Permanent medium
e.g. disk or memory card

Digital transmission
not permanently connected with a medium (cable or optical fibre transmission — broadband internet), or at least not with a medium accessible to the user or generally identifiable

FORMS

Files
e.g. text, graphics, audio, video, computer documents (emails, SMSs), system files

Digital data
e.g. logs (log-in data), location data

ORIGIN

Unlimited
e.g. computers, mobile phones, GPS trackers, computer networks, internet, integrated circuits, voice recorders

this definition, and thus whether it may be regarded as evidence in civil proceedings.

We should first distinguish the evidence as such from its source. When using electronic evidence, the evidence is the electronic record, e.g. in the form of a recording, not the medium on which it is found. The medium is only a source of evidence. This distinction is crucial, as electronic evidence usually cannot be rendered independently, because it inherently lacks the characteristic of materiality. Electronic evidence can be read only through some medium.

A document, or miscellaneous evidence?

Electronic evidence may be classified variously under civil procedure regulations. Although the classification does not in itself determine whether the evidence will be admissible, it does affect the regulations applicable to the evidence.

Generally, electronic evidence may be classified either as a document or in the miscellaneous category of "other evidentiary means." There is nothing preventing electronic evidence from being the subject of an expert opinion, and it seems that in the case of assessment of operating systems this may be the only available method of admitting the evidence.

It is commonly recognised that an electronic document means data recorded on a material medium, including data stored using electronic or similar means, so long as it can be reconstructed in a form enabling perception of the data. Moreover, under Civil Procedure Code Art. 243^{1}, the subject of evidence from a document can only be a document containing text enabling determination of the issuer of the document. This generates doubts in the context of electronic evidence, primarily when it comes to ascribing authorship.

For example, a database or computer program is often the work of many persons independent of one another, where sometimes there is no way to identify the issuer. This applies in particular to "living" items or systems, which are (or can be) subject to constant changes in response to users' actions or as a result of the operation of algorithms. Under this rule, for example, a blockchain would rather have to be excluded from the category of "documents," as it is generated automatically and is generally made up of smaller units revealing the intentions of various people.

Nonetheless, a particular fragment or element of a database, program or other record that can be ascribed to a specific person or persons as the issuer may constitute a document. On this basis, a transaction recorded in a blockchain system, revealing the intention of a given person, can be a document.

In many instances, electronic evidence will be regarded as other, unclassified evidentiary means within the meaning of Civil Procedure Code Art. 308. This group includes evidence obtained using various technologies. Within this group we can distinguish between:
– Visual evidence, containing information perceived through sight (e.g. film, television, photography)
– Audial evidence, containing information perceived through hearing (e.g. sound disks).

The evidentiary means discussed in this article are not an exhaustive set.

Thus, ultimately, in civil proceedings, any evidence available at a given stage of development of technology and science can be used in a case, even if it does not fall within any specific category of evidence. This follows from Civil Procedure Code Art. 309, which states that any evidentiary means is admissible for purposes of civil procedure, regardless of whether it is enumerated in the code.

But in the case of evidence involving the state of a functioning IT system, and thus subject to change in real time, the broad admissibility of various evidentiary means under Civil Procedure Code Art. 308–309 does not resolve all doubts. The key problem is whether a "living" system can be captured and contained within a medium without altering its nature (even leaving aside the technical feasibility of capturing the system in this way).

In a certain sense this is a very old problem. An operating production line, the flow of a river, the degree of contamination of air, or the average concentration of sound at a given place: for similar reasons, none of these can be reduced to a medium and brought into court. But electronic evidence is usually thought of in terms analogous to documents, i.e. fixed records of words or images, and this is the focus of the regulations.

But when we approach operating IT systems, like other elements of reality that are generally enduring but subject to various ongoing processes, the solutions to evidentiary issues in examining such items should be sought among the methods of introducing evidence already existing in the law.

For example, if the actual, current operation of a system is relevant, it should undergo analysis by an expert witness, which, in a textbook manner, should also include an on-site inspection of the operation of the system, to ensure participation by the parties and oversight of the process by the court and avoid the allegation that the expert was hired to "find evidence" for the party.

Such an examination does not exclude (and in many instances will require) examination of the source code of the software, which may constitute a document for purposes of the regulations or be admitted as evidence based on the regulation on documents. Specific products of the functioning system may also be treated as documents, such as reports, readings, graphs etc generated by the system.

Special issues—and not only evidentiary ones—may also be created by systems or products using AI or machine learning, where the system not only undergoes changes in real time and generates those changes itself (i.e. modifies its own code), but also makes changes in a way that is sometimes opaque even for the authors of the system, as experience has confirmed. The creators of such systems are not in a position to explain the aims served by particular solutions and elements of code generated by AI, and thus cannot link them causally with the "external" manner of operating the system. Determining how to examine such a system when taking evidence, and what may serve as the subject of evidence reliable and useful for the case, will require a separate assessment in each case. It's not hard to imagine that the court might require the assistance of an expert to define or at least clarify the scope of the opinion, which seems permissible as a rule, although the optimal solution would be to appoint a separate expert for this examination and for issuing an opinion on the merits.

Council of Europe guidelines on electronic evidence

The foregoing considerations are supplemented by the "Guidelines of the Committee of Ministers of the Council of Europe on electronic evidence in civil and administrative proceedings," adopted on 30 January 2019. While the guidelines are not legally binding, they provide a useful set of practical rules for handling electronic evidence drawing on the experience of European justice systems.

Under the definition presented by the Council of Europe, "electronic evidence" means "any evidence derived from data contained in or produced by any device, the functioning of which depends on a software program or data stored on or transmitted over a computer system or network."

The guidelines thus cover a broad range of electronic evidence, taking such forms as text files, video, sound recordings, location data, and system files. Such evidence may also be generated by any device, such as computers, mobile phones, GPS trackers, or computer networks.

Another important issue identified by the Council of Europe is metadata, defined as "electronic information about other electronic data, which may reveal the identification, origin or history of the evidence, as well as relevant dates and times." Metadata can demonstrate the completeness of information presented using electronic evidence. But they can also be treated as primary evidence for proving such facts as where »

The creators of AI systems are not in a position to explain the aims served by particular solutions and elements of code generated by AI, and thus cannot link them causally with the "external" manner of operating the system.

and when an electronic message was transmitted, or the date of completion of work or modification of an existing program or database.

Unfortunately, in their present form the guidelines do not directly address blockchain or cloud computing, which may soon become a fundamental source of electronic evidence.

According to the first fundamental principle stated in the Council of Europe guidelines, "It is for courts to decide on the potential probative value of electronic evidence in accordance with national law." This is consistent with the basic rule in Polish procedure of free evaluation of the evidence by the court. This means that when admitting electronic evidence, if the court must seek aid from an opinion by an expert on IT systems, the opinion itself must not prejudge the probative value of the electronic evidence.

The second fundamental principle states: "Electronic evidence should be evaluated in the same way as other types of evidence, in particular regarding its admissibility, authenticity, accuracy and integrity."

The third rule reflects the principle of equal treatment of the parties in civil proceedings: "The treatment of electronic evidence should not be disadvantageous to the parties or give unfair advantage to one of them." This means, for example, that each party must be afforded the opportunity to challenge the reliability of such evidence.

The guidelines show that the courts' traditional adherence to paper versions of electronic evidence can deprive them of access to information relevant to resolving the disputes before them.

COUNCIL OF EUROPE GUIDELINES ON ELECTRONIC EVIDENCE

ADOPTED ON 30 JANUARY 2019

principle 1 It is for courts to decide on the potential probative value of electronic evidence in accordance with national law. (Thus opinions of court-appointed experts should not prejudge the probative value of electronic evidence.)

principle 2 Electronic evidence should be evaluated in the same way as other types of evidence, in particular regarding its admissibility, authenticity, accuracy and integrity.

principle 3 The treatment of electronic evidence should not be disadvantageous to the parties or give unfair advantage to one of them. (Thus each party must be afforded the opportunity to challenge the reliability of electronic evidence.)

How to offer and introduce electronic evidence?

The party applying for admission of evidence should precisely identify the facts which the evidence is intended to prove. The designation of the evidence should demonstrate what evidence is to be admitted by the court as well as the information or circumstances justifying admission of the evidence.

For miscellaneous means of evidence to be properly introduced, the court must specify the manner of introduction of the evidence, suited to the nature of the evidence and applying the evidentiary regulations as relevant.

Another difficulty in admitting electronic evidence is determining how to enclose it with the case file, as it does not have an inherent material form. The principle of openness of proceedings means that each party must be afforded access to the material gathered in the case. It appears correct to require that if a given piece of electronic evidence constitutes an electronic document, a printout of the document should enclosed with the file. Otherwise, a medium containing electronic evidence, which can be opened using the system or programming at the court's disposal, should be enclosed.

This does not exclude the possibility of applying Civil Procedure Code Art. 245 (a private document in written or electronic form is evidence that the signatory made the statement contained in the document) to establish whether a disputed electronic record is accurate. This should be determined by an IT expert. This examination would consist of verification of whether the recorded transaction or system of files was prepared and confirmed in accordance with the rules of the programming.

What about personal data?

A party pursuing its claims may be forced to present electronic evidence containing records with personal data of third parties: databases, software containing HR information, and so on. This raises the question of whether a party processing such data for the purposes of civil proceedings becomes the controller of the personal data.

Art. 4(7) of the EU's General Data Protection Regulation defines the "controller" of personal data as "the natural or legal person, public authority, agency or other body which, alone or jointly with others, determines the purposes and means of the processing of personal data." In turn, under Art. 4(2) GDPR, "processing" of personal data is defined as "any operation or set of operations which is performed on personal data or on sets of personal data, whether or not by automated means, such as collection, recording, organisation, structuring, storage, adaptation or alteration, retrieval, consultation, use, disclosure by transmission, dissemination or otherwise making available, alignment or combination, restriction, erasure or destruction." Based on a literal reading of these provisions, a party using electronic evidence for the purpose of civil proceedings containing personal data should thus be deemed to be a data controller. Consequently, the informational obligations arising from this status will rest on such a party.

As a controller for purposes of the GDPR, the party must ensure that personal data are processed lawfully, by basing the processing on one of the grounds listed in Art. 6(1) GDPR. In this context, this will mainly be Art. 6(1)(f) GDPR, which basically requires a showing that the processing is necessary for the pursuit of legitimate interests. Pursuing claims through civil proceedings may be regarded as a legitimate interest.

But any reliance on this basis for processing requires a balancing of the interests of the party against the interests or fundamental rights and freedoms of the data subject. Data subjects should thus anticipate that a party to civil proceedings may process their data. As the aim is to pursue claims against a specific party, this may reduce the risk of impacting the interests or fundamental rights and freedoms of the data subject. We could say that for the party, the content of the data is relevant to a limited degree, and what counts more is the ability to prove that certain data existed within a certain system. Moreover, a party to civil proceedings does not intend to obtain a financial benefit from the mere processing of data as such (although the party may obtain such a benefit indirectly if the dispute is resolved in the party's favour).

Systematically, the GDPR seems to recognise "the establishment, exercise or defence of legal claims" as an essential aim, numerous times recognising that it takes precedence over the rights of data subjects, or otherwise protecting this aim (Art. 9(2)(f), 17(3)(e), 18(1)(c), 18(2), 21(1) and 49(1)(e) GDPR). It may thus be assumed that for purposes of balancing interests under Art. 6(1)(f), this aim carries a greater weight than some other aims.

Nonetheless, before deploying extensive electronic evidence (such as a large database), the party should analyse the necessity and correctness of the processing of personal data, and potentially take steps to notify the data subjects of the use of their data in a civil proceeding.

Data recorded in blockchain

In the near future, entries in blockchain may assume great evidentiary significance. This technology, originally used to create cryptocurrencies, now facilitates other activities, including conclusion of contracts. Discussions are underway on using blockchain as a notarial record, for maintaining banking records, as a system for authentication of documents, and as a digital signature in the state administration.

The circulation of information recorded in blockchain raises serious evidentiary problems. This mainly has to do with proving the content of records of blocks, connecting a record with its "creator" and its "addressee," and examining whether a given record constitutes the substance of a contractual relationship. The optimal solution would be to develop a uniform framework within EU law for the use of such sources of evidence.

Summary

The transformation of the economy and daily life which some call the Fourth Industrial Revolution is proceeding very quickly, shifting more and more elements of reality into the virtual world. Thus the issue of electronic evidence can only gain in importance. Indeed, it cannot be ruled out that this very concept will soon become anachronistic, as the use of data in digital records becomes the norm, and the use of analogue records comes to be regarded as unusual, or even a dangerous departure from the norm.

There is no escaping the consequences of these changes in any sphere of life, including the law and the judicial system. We can only hope that decision-makers resist the temptation to attempt such an escape, but instead rise to the legal challenges posed by the rapid progress in technologies for gathering and processing data.

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Remote work: Privilege or challenge?

The COVID-19 pandemic has made remote working a common practice. Most employers and employees have accepted this change positively, but this form of work also has significant drawbacks. The pandemic has revealed the gaps in the existing legal regulations concerning remote working.

Telework, remote work, or home office?

First we should straighten up some of the terminology concerning remote working. As EU law does not separately regulate the situation of employees working remotely with use of information and communications technologies, the remarks below will refer to the definitions adopted in Polish labour law.

Confusingly, the terms "remote work," "telework" and "home office" (or "home-based working") are often used in practice interchangeably. Under Polish labour law, these notions are not the same: not everyone working on a computer at home is a teleworker. Under the definition set forth in the Polish Labour Code, an employee is regarded as a teleworker only when the person (1) regularly works away from the workplace, (2) using electronic means of communications (i.e. performs telework), and (3) delivers the results of the work via the same electronic means of communication.

Telework differs from other instances of remote performance of work due to the regularity of performing work duties away from the workplace. Working at home only incidentally, e.g. when a child is ill or there is a breakdown in the office (which is rather a characteristic feature of using a home office) is not telework.

It may be agreed in this respect that the employee will spend part of his or her working time (e.g. on specific days of the week) performing work from home, and otherwise work from the employer's office. Polish labour law does not set any minimum number of hours or days of working away from the workplace, or a ratio of remote working to working at the workplace, which would clearly decide that an employee is a teleworker. An employee using a home office may therefore be deemed a teleworker if remote working becomes a regular method for him or her to perform work, and vice versa—the employee may lose the status of a teleworker if he or she begins to use remote working only occasionally (e.g. when the employer begins requiring the teleworker to work from the employer's office too often).

Unlike the use of a home office, telework is not limited only to working from the employee's residence. A teleworker can also work from other locations, so long as they are away from the employer's workplace (e.g. in an office or coworking space rented by the employee).

This is where the first (but not only) drawback of the Polish telework regulation arises. The Labour Code does not exclude the obligation to specify the working location (place) of a teleworker in the employment contract, or establish any separate rules in this respect (although some commentators take the view in the legal literature that there is no such obligation in the case of teleworkers). Thus specifying the work location may pose a challenge in the case of "nomadic" or mobile telework, i.e. a situation where the teleworker does not perform work from one fixed location but works from wherever he or she happens to be at the moment (if the technical conditions allow for communication with the employer). It would be legally dubious to agree that the employee's workplace will be the territory of the entire country, the entire EU, or indeed the whole world, or a place chosen on any occasion by the employee.

Here we should only red-flag that agreeing with a teleworker on a work location outside of Poland may give rise to further legal complications, in particular involving the governing law and thus the work and pay conditions applicable to the employee, and how salary and benefits would be settled under tax law and social security law.

> "Remote work" in the proposed form would cover telework, remote work under the anti-crisis regulations, and home office. The new provisions are expected to enter into force in the first quarter of 2021.

Remote working: for the duration of the pandemic, or permanently?

The Anti-Crisis Acts (also known as the Anti-Crisis Shields) introduced a definition of remote work into the Polish legal system: it is work specified in the employee's employment contract which at the employer's instruction and for the purpose of combating COVID-19 is performed for a definite period away from the regular working location.

Thus remote work is currently a temporary and exceptional solution, introduced in connection with the COVID-19 pandemic. Remote work is not telework, and the special regulations on telework (including the limitations on the employer's responsibility for ensuring safe and hygienic working conditions) do not apply to remote work. It differs from the telework specified in the Labour Code among other things in that it need not be performed, and the work results need not be delivered to the employer, exclusively using means of electronic communication. Unlike telework, remote work does not require an agreement with the employee. The employer may unilaterally, purely via an instruction (issued in any form), modify the contractually agreed working location (no formal amendment of the employment contract is required).

The special provisions of the Anti-Crisis Shields served as a forerunner for broader regulation of remote working, which employer organisations had sought for years. At the end of September 2020, a proposed amendment to the Labour Code was circulated for consultation within the Social Dialogue Council, calling for replacement of the existing provisions on telework with detailed regulations governing remote work. Under the proposal, "remote work" would be defined as work performed wholly or partly away from the employer's premises or away from the permanent working location specified in the employment contract or indicated by the employer, in particular using means of electronic communication. This means that "remote work" in the proposed form would cover telework, remote work under the anti-crisis regulations, and home office. The new provisions are expected to enter into force in the first quarter of 2021.

Working time or private time?

The rules governing working time are one of the main defects in telework—from the perspective of both employers and employees. Neither the current provisions on telework nor the proposed amendment to the Labour Code provides specific rules for the working time of teleworkers or how their working time should be settled. This means that all the standards for working time and rest, overtime, and the duties to maintain records of working time, also

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apply to persons working remotely. In practice it is difficult or impossible to monitor the working time of teleworkers and settle their working time accurately (even using additional technological solutions like an electronic attendance list or timekeeping applications).

Persons working away from the workplace are usually subject to a task-based system of working time, where what is relevant is the employee's performance of specific tasks, and not the employee's availability during specified hours. But this is not an ideal solution from the employer's perspective, as it does not entirely relieve the firm of the duty to maintain a record of working time (only from recording working hours), nor does it exclude the need to compensate the worker for overtime (but in the case of teleworkers overtime may be settled in the form of a fixed monthly lump sum). The employer's inability to properly monitor working time, combined with the common practice among workers of "catching up" on work outside of business hours (with the tacit approval of their superiors), generates a risk for companies of having to compensate these teleworkers for overtime, and in extreme cases even a risk of criminal liability for failure to comply with legal standards for working time and rest time. In the case of remote work, the employer is in a better situation, as Shield 4.0 authorised companies to require employees to maintain a record of their activities, including the date and time of performance.

The right to disconnect

From the employees' point of view, defects in remote work include blurring the boundaries between private time and professional time, the unpredictability of working hours, and creation of a culture of staff being on duty around the clock. This problem has only gotten worse during the COVID-19 pandemic.

In response, work has begun in the European Parliament on a directive establishing employees' "right to disconnect" (not to be engaged, directly or indirectly, in activities connected with professional work, or communication via digital devices, outside of working hours). An employer's violation of this right would be justified only in exceptional circumstances and would have to be compensated for by time off or pay. And employees could not suffer any negative consequences from exercising this right. To date only a few EU member states have adopted regulations recognising the right to disconnect (Belgium, France, Italy and Spain).

In Poland an employee's right to disconnect has not been expressly adopted, but such a right may be drawn from an interpretation of the rulings of the labour courts and the Supreme Court of Poland: as a rule, an employee has no obligation to answer the phone or respond to email after working hours or when on holiday. And in extreme cases, contacting an employee on work-related matters after working hours may qualify as mobbing (as for example the Lublin Regional Court held in its judgment of 20 June 2018, case no. VIII Pa 86/18). An exception is the situation where an employee is required to serve duty hours, i.e. to remain on-call and ready to work outside of normal working hours (at a place indicated by the employer, including at home). Such duty hours must not infringe the employee's right to daily and weekly rest time, and should also be made up to the employee with time off or pay (except when duty hours are served at home).

10.2%

As of the end of June 2020, due to the pandemic 10.2% of working Poles were performing work remotely (according to Statistics Poland)

37%

In April 2020 about 37% of respondents from European countries were forced by COVID-19 to work from home (Eurofound)

5.4%

In 2019 only 5.4% of people employed in the EU regularly worked remotely from their home (Eurostat)

The price of remote work

The possibility of working from home is typically viewed as a perk for the employee, greatly enhancing the attractiveness of working for the given company, as well as a source of savings, chiefly on the employer's part. But this does not mean that costs of working at home are borne solely by the employee.

As a rule, the employer bears the obligation of providing the employee with the tools and materials essential for performing the work.

	CURRENT LABOUR CODE	**SHIELD 4.0** FROM 24 JUNE 2020	**AMENDED LABOUR CODE** PLANNED FOR 1Q 2021
REMOTE WORK	Customary term, no legal definition	Work specified in the employment contract which at the employer's instruction and for the purpose of combating COVID-19 is performed for a definite period away from the regular work location. No regulations on occupational health and safety. Tools and materials for work provided by the employer. No regulations on the costs of operating tools and materials necessary for work owned by the employee.	**Uniform definition of remote work** Work performed wholly or partly away from the employer's premises or away from the permanent working location specified in the employment contract or indicated by the employer, in particular using means of electronic communication. Partial modification of the existing rules regarding costs of tools and materials necessary for work and occupational health and safety, including that the employee will be responsible for proper organisation of the remote workplace.
HOME OFFICE	Customary term, no legal definition. Generally understood as work performed **incidentally** (e.g. when a child is sick or there is a breakdown in the office) away from the workplace, exclusively at the employee's residence, and the results of the work are delivered electronically. The employer is not required to supply working tools (although usually the employee uses company equipment). The employer is fully responsible for occupational health and safety.		
TELEWORK	Work performed **regularly** away from the workplace, using electronic communications. The results of the work are delivered electronically. The employer bears the cost of equipment and materials needed for the work and is responsible for occupational health and safety.		

In the case of telework, the employer must:

– Provide the employee the equipment necessary to perform telework
– Provide the employee training on how to use the equipment, and technical support
– Cover the costs associated with insurance, installation, servicing, operation and maintenance of equipment provided to the employee.

Polish law permits modification of this rule through a separate agreement with the teleworker. In particular, the regulations suggest that these costs may be shifted entirely to the employee (although some commentators reject this possibility). The parties may also agree that the employee will use his or her own devices for work purposes. But in that case, the employee has a right to obtain a cash equivalent in an amount reflecting ordinary wear and tear on the equipment, the quantity of materials used for work purposes, and the documented market prices for these items.

The greatest controversy is stirred by compensation to the employee working at home for internet access and increased consumption of electricity and water. In our view, the employer should share in the cost of internet access, but there are no legal grounds for the employee to demand reimbursement of increased household utility costs.

Unlike in the case of telework, the provisions on remote work do not expressly provide for any compensation to the employee for the costs of using private equipment and materials.

The proposed amendment to the Labour Code would modify the current regulation on the costs of telework, but the current proposal does not fully meet the expectations of employer organisations or trade unions.

Safety first

The issue of occupational health and safety at the workplace also discourages companies from making broader use of telework and remote work. It is hard to comply with these requirements when the employer does not have full control over the conditions in » force at the work location, particularly in an employee's home.

In the case of telework, the employer's general responsibility to ensure safe and hygienic working conditions is modified only insofar as with respect to a teleworker working from home the employer is relieved of expressly enumerated obligations (e.g. concerning the working premises). Other occupational health and safety obligations must be fully executed, taking into consideration the type and conditions of the work.

Performance of the employer's duties may prove particularly challenging in the event of a work accident. We can say based on our practice that it may be difficult to determine whether the accident occurred during the performance of work duties, particularly if the employee does not cooperate in establishing the circumstances of the accident (e.g. refuses access to his home by the follow-up team).

Shield 4.0 does not address occupational health and safety issues at all: an employee may be instructed to work remotely as long as the employee confirms that he has suitable premises for the work. The act does not specify the minimum standards that must be met by the remote working location (under Polish living conditions, many employees may take the view that they do not have suitable conditions for remote work), or how the employer is supposed to verify the employee's statement in this regard.

The draft amendment of the Labour Code only partly answers the demands of employer organisations, as in occupational health and safety respects it largely repeats the existing provisions on telework. An advantageous change for firms is shifting to the employee the responsibility for proper organisation of the remote workplace and introduction of a sanction for refusal to cooperate in post-accident procedures (the employer would then be entitled not to recognise the accident as occurring at work).

What is worth changing?

It's encouraging that Polish lawmakers have begun working on changes in remote working, but it is hard to reach a clear assessment of the proposed amendment to the Labour Code. At this stage we can only hope that during the discussions between social partners and the parliamentary deliberations, solutions will be developed facilitating broader use of remote work, while maintaining minimum standards of protection for employees.

The COVID-19 pandemic has shown how much these changes are anticipated. For the new regulations to truly encourage the use of remote work, in our view they should reflect the following issues:

- **Fewer formalities connected with introducing remote work**. It is worth considering limiting the statutory duty of reaching agreement on telework with trade unions to employers with a headcount of over 50 (as in the case of workplace and remuneration policies). It would also be good to reduce the formalities connected with the use of remote work on an incidental or short-term basis (e.g. when a worker stays home with a sick child).

- **Rules for recording and settling remote working time**. The solutions concerning working time should reflect the fact that in practice, proper oversight of remote working time can be pure fiction. There are two possible directions for legislative changes. Employers could be relieved of the duty of recording remote work hours, regardless of the system of working time in force for the remote worker (this approach may be resisted by the trade unions, because it does not protect employees from performing unpaid work or excess work above the agreed number of working hours). Tools could also be introduced enabling proper execution of timekeeping duties (e.g. the option of requiring employees to maintain records of remote working time patterned on the solution introduced by Shield 4.0 or imposed on non-employee contractors).

- **Employer's responsibility for occupational health and safety.** There are calls for further limitation of the occupational health and safety obligations borne by the employer when remote work is performed at a place where the employer has little influence (including at the employee's home), particularly with respect to post-accident procedures. A debate should be held on the demand by employer organisations that in such instances, the burden of proving that the accident occurred in connection with work should be shifted to the employee. We also propose that the scope of occupational health and safety duties be unequivocally stated with respect to employees performing remote work (the current wording of the statutory regulations raises grave doubts on the scope of employers' duties).

- **Fees for internet and other utilities in the case of remote work from home**. Setting a rigid statutory lump sum does not appear to be an optimal solution. It would be better to leave this issue to the discretion of the parties.

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A difficult reporting obligation for temporary employment agencies—especially during a pandemic

Failure to submit timely information on the activity of an employment agency may result in removal of the agency from the register, blocking its further operations.

Can this sanction be avoided? And is the sanction proportionate to the violation?

During the pandemic our clients operating in the form of an employment agency began to have serious and well-founded concerns about a collapse of the labour market and difficulty in delivering their services. The factual situations they brought to our attention in the past year show that it was extremely difficult for employment agencies to comply with all the formalities imposed on them.

This also applied to the requirement to submit annual information on the operations of an employment agency, regarded as a type of reporting requirement. Based on our observations, difficulties complying with this obligation were mainly faced by agencies with decision-making bodies abroad and a limited presence in Polish territory. The danger was real, because the sanction for failure to perform this duty is removal of the agency from the register of entities operating employment agencies. It is hard to imagine a more severe sanction for the agency. In this context, at least two questions should be posed:

– What should a temporary employment agency do if it is threatened with removal from the register because of failure to comply with this obligation?
– Is the sanction of removal from the register fair and proportionate to the infringement, particularly under the realities of the COVID-19 pandemic?

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Filing annual information

A temporary employment agency is one of the types of employment agencies functioning on the Polish market. Providing such services is a regulated activity requiring entry in the register of entities operating employment agencies. The register is maintained by the marshal of the province where the agency has its registered office. This also entails the need to meet certain requirements and for the agency to comply with a range of duties. One duty is to file annual information on the agency's activity by 31 January of the following calendar year.

SCOPE OF ANNUAL INFORMATION FILED BY EMPLOYMENT AGENCY

- Number of individuals taking up work via the employment agency
- Number of employers using HR consulting and career counselling services
- Number of individuals using career counselling
- Number of individuals assigned to temporary work by the employment agency
- Information on the employment agency's membership in industry associations

The employment agency must submit this information to the province marshal maintaining the register in which the agency is entered.

The agency must also notify the province marshal of any change in data such as the agency's name, registered office, business address and telephone number.

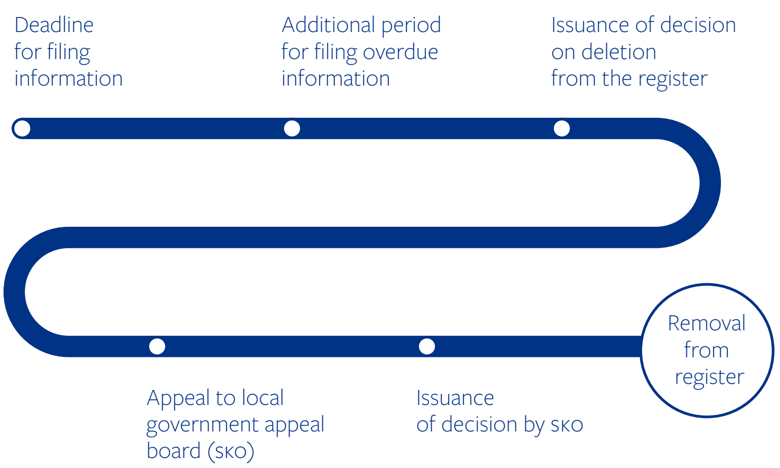
Serious consequences of failure to report

Failure to make a timely filing of information on an employment agency's activity or an update of the agency's data carries far-reaching consequences, as many entities operating on this market have unfortunately already painfully experienced. Filing of this type of information is regarded as an essential condition for operating an employment agency. Failure to meet this condition results in initiation of an administrative proceeding to delete the agency from the register of entities operating employment agencies. In this proceeding, the province marshal will set a deadline for the employment agency to submit the overdue information, and if the deadline is not met, will issue a decision to delete the agency from the register. The agency may appeal this decision to the competent local government appeal board (SKO). The decision on the appeal by the SKO is legally final, but review may still be sought before the administrative court.

Difficult path to set aside a decision on removal from the register…

What should the agency do in this situation? Employment agencies against whom a decision has been issued to delete them from the register often decide to appeal. Weighing on the scale is the possibility to continue doing business, providing employment to a sometimes very large number of temporary workers, and maintaining the agency's reputation in the eyes of its own clients—employers using the agency's services. Unfortunately, as the practice shows, such appeals generally prove ineffective. In justifying the issuance of such decisions, the authorities indicate that under the regulations, the province marshal is required to remove from the register an agency that has failed to submit the required information. They also point out that employment agencies conduct a regulated activity, and as professionals (notwithstanding the extraordinary circumstances of the global COVID-19 pandemic) they should comply with the relevant requirements, which, in the authority's view,

PROCEDURE FOR REMOVAL FROM THE REGISTER OF ENTITIES OPERATING EMPLOYMENT AGENCIES



> In the case of activity involving temporary employment or intermediation in assigning individuals to work abroad, the fine can be as high as PLN 100,000.

are designed to protect individuals working via the agency's intermediation.

These arguments might be understandable in a case where the employment agency fails to file the required information within the designated time. But often the authorities issue such a decision also when for example the annual information is filed but has minor gaps or errors, such as an obvious typo in the agency's address or even an illegible signature in the filing. In similar cases, the administrative courts have found that the authorities have taken too rigid an approach, and ultimately issued rulings in favour of the agency. The courts have correctly found that this practice is impermissible, as obvious oversights do not demonstrate that the employment agency has failed to comply with its obligations. Thus in some circumstances it is possible to effectively challenge decisions on removal from the register of entities operating employment agencies.

Moreover, the authorities often overlook the fact that the additional period for submission of the required information is not specified in the regulations, so this decision rests with the authority. But in practice the authorities set a 7-day period to supplement the information and refuse to grant an extension. Complying with such a tight deadline was particularly hard in recent months, as employment agencies (including those whose real decision-making centres are based abroad) had to deal with difficulties connected with the COVID-19 pandemic, in particular the quarantine of their Polish staff, even before introduction of regulations suspending the running of administrative deadlines.

… but even more difficult consequences of issuance of such a decision

An employment agency that decides not to apply to the administrative court for review of the decision removing it from the register of entities operating employment agencies must bear in mind that conducting such activity without the required entry in the register constitutes a petty offence punishable by a fine. In the case of activity involving temporary employment or intermediation in assigning individuals to work abroad, the fine can be as high as PLN 100,000. Punishment for such an offence also deprives the person of the ability to conduct such activity in the future. Thus it appears that an employment agency that fails to comply with the informational obligation can face draconian consequences.

Ironically, temporary employment agencies that "only" violate the regulations on the maximum periods of assignment of workers to temporary employment are punished much less severely. Such an entity can continue to operate its business, and the potential fine for such an infringement cannot exceed PLN 30,000.

Where is the proportionality in this sanction?

In weighing the appropriateness and proportionality of the sanctions for infringement (particularly under the realities of the COVID-19 pandemic), it should be borne in mind that the annual information on the activity of employment agencies is really only of statistical value. There have also been instances where an employment agency was deleted from the register for failure to notify the authorities of a change in its business address (e.g. when it moved to a smaller office because of the adoption of remote work by its staff). If as a result of such a decision several thousand temporary workers lose their jobs, it is worth pondering whether this sanction is proportionate to the aim of protecting persons using the services of such agencies.

During the course of work on further tightening of these regulations (a proposal that has not yet been pushed through), the employers' organisation Polish Confederation Lewiatan called for amending the regulations to grade the sanctions depending on the seriousness of the violation. This is certainly a concept worth revisiting. Under the current law, the sanctions designed to deter violation of the regulations may instead deter people from operating in the form of an employment agency. This would not be helpful for the labour market during these tough times, requiring more flexibility than ever before.

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Common sense, consistency, and care: Three key standards for transfer pricing in 2021

Turbulence on global and local economies in 2020 has changed market conditions. The altered reality in which enterprises operate also affects transactions between related entities required to set the terms for intragroup transactions patterned on market behaviours. The lack of established standards on the market in the era of COVID-19 means that enterprises must rely on limited information and their own common sense.

Related entities, including multinational enterprises, are required to set prices in intragroup transactions on the terms that would be applied by entities not connected by legally defined links—the arm's-length principle.

Most often, the compliance of intragroup transaction terms with the arm's-length principle is confirmed by comparing the terms to similar uncontrolled transactions, or by comparing the financial result realised from the transaction with the results obtained by enterprises operating on the open market (comparability analysis).

In most instances, the correct data for such a comparison may be found in databases with information about the financial results recorded by enterprises in preceding years and transactions occurring in the more or less distant past.

Transfer prices prefer peace and quiet

The unprecedented turbulence on markets due to COVID-19 has rendered data from before the pandemic incomparable. Locally and globally, in 2020 there were disruptions across numerous sectors in demand and supply chains, forced changes in the operating rules of enterprises, reduced operating margins, a loss of confidence in debtors, and an increased risk in investing and lending.

Under these conditions, new benchmarks must be sought.

SUMMARY OF OECD TRANSFER PRICING GUIDANCE

When analysing transfer prices, taxpayers may encounter barriers that must not be ignored. To protect their own interests, taxpayers should:

- Apply **a high level of diligence** in gathering and documenting information concerning intragroup transactions, the taxpayers' operations, the operations of other entities on the market, and the condition of the market
- Given the inadequate access to information, act on the basis of the principle of **commercial reasonableness** in selecting data for analysis and resist the temptation to change the rules of intragroup accounting to achieve a desirable but improper economic result
- Maintain **intellectual consistency** in justifying the relations between economic events, intragroup settlements, and the operating profile of the related entity.

The contortions affiliated entities must go through to bring the terms of intragroup transactions into line with market conditions begin with a diagnosis of:

– How the pandemic has impacted rules for operation of the enterprise and its financial results
– What measures were taken to manage the challenges posed by the pandemic
– Whether the rules for cooperation with related entities (transfer pricing policy) have been disrupted.

This self-diagnosis should be scrupulously documented, as it may prove decisive in the event of a dispute with the tax authorities.

A fishing rod instead of fish

So far the Polish Ministry of Finance has refrained from drafting or publishing tax clarifications concerning transfer prices during the pandemic and post-pandemic period. One-off changes in regulations have only eased selected administrative burdens imposed on taxpayers during the pandemic. This approach was supposedly caused by a desire to reconcile local guidance first with the expectations set forth in the OECD's much-anticipated Guidance on the transfer pricing implications of the COVID-19 pandemic. The OECD guidance was finally published in mid-December 2020 and covers four areas:

1. Impact of the pandemic on comparability analysis
2. Losses and allocation of costs specific to COVID-19
3. Impact on transfer prices of government assistance programmes
4. Impact on existing advance pricing arrangements and APAs under negotiation.

In the immediate future, the OECD guidance will serve as the most important touchstone for taxpayers, their advisers, and the tax authorities. But in Poland there is a widespread expectation that the Ministry of Finance will take a position on the rules discussed there, to give taxpayers some basic reassurance that a couple of years down the line they will not be drawn into an avoidable dispute with the tax authorities.

By their nature, the OECD guidelines cannot be regarded as a set of binding rules. Nonetheless, they convey many important indicators that can help manage transfer pricing. Boiling down the OECD's 30-page document to a few sentences, the overall advice given by the guidelines would be as follows.

These principles may sound abstract, but their sense will become clear when it is necessary to resolve a thorny issue associated with a specific intragroup transaction.

1. Impact of pandemic on comparability analysis

Taxpayers who carried out high-value transactions between related entities in 2020 may be required in 2021 to prepare transfer-pricing documentation containing a comparability analysis.

While a comparability analysis, once performed, can be used for several years, if there are material changes in the economic environment it is necessary to prepare a new analysis. An analysis prepared for 2020 will have to reflect the circumstances involving the pandemic.

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COMPARABILITY ANALYSIS: WHAT CAN REPLACE OR SUPPLEMENT HISTORICAL DATA?

These additional sources may include for example:

- Publicly available information, including information on GDP figures or industry indicators, published by reliable institutions
- Information on changes in sales volumes and the reasons for these changes, compared to earlier periods
- Specific information on additional costs incurred in connection with the pandemic locally and within the group as a whole
- Information on the value and nature of government assistance received by related entities and other entities operating on the market
- Conclusions from comparison of forecasted data with actual results, and linking the identified differences in results in intragroup transactions, as well as the risks and functions assigned to related entities.

Taxpayers in a position to identify reliable data from 2020 due to the nature of their business (e.g. conducting similar transactions with related and unrelated entities) will be in a privileged situation.

But generally, preparing a comparability analysis will be more difficult because of the unavoidable need to rely on historical data. Because the data may not be fully apposite to the period covered by the analysis, the OECD guidelines indicate the possibility of relying on additional sources of information to make the necessary adjustments aimed at achieving a reasonable level of comparability.

Given the anticipated difficulties in reaching clear and irrefutable conclusions, the OECD guidance also calls on tax authorities to allow taxpayers to rely on reasonable commercial judgment, backed by carefully gathered information.

2. Losses and allocation of pandemic-related expenses

There has been much debate around the issue of the extent to which multinational enterprises can assign losses to entities deemed to be at limited risk. In response, the OECD refers to the general rules governing this issue. The ability to incur losses will be decided by the catalogue of risks assumed by the enterprise in question. To justify incurring a loss, the taxpayer will have to show that the risk it bore came to fruition, and its financial effect is commensurate to the burden imposed on the entity.

The OECD guidance also indicates that various civil-law institutions (e.g. modifying intragroup contracts or evading liability by invoking *force majeure*) should be used only after a careful examination of the rationale for such measures and the available alternatives. While the taxpayer will probably manage with conducting and duly documenting intragroup negotiations or an assessment of the possibility of invoking *force majeure*, it is hard to imagine entering into a dispute with the tax authority over a civil-law institution or an assessment of the position of specific participants in the negotiations.

3. Impact of government assistance programmes on transfer pricing

Assistance to businesses to combat the impact of the economic crisis caused by the pandemic has taken various forms. Even though the general nature of assistance has been similar across numerous countries around in the world, the programmes have differed in essential elements, which can have an impact on the analysis of transfer prices. For this reason, the OECD guidance recommends a careful analysis of this issue.

A self-diagnosis should cover such issues as identification of the assistance received, its value, and the extent to which these benefits were passed on to customers and suppliers.

Enterprises should conduct a comparability analysis bearing in mind that local data will probably be more reliable than foreign data

Potentially comparable entities should be carefully examined in terms of whether they benefited from support instruments and how this impacted the terms of the transactions they carried out.

(given the similarity in available forms of assistance), and potentially comparable entities should be carefully examined in terms of whether they benefited from support instruments and how this impacted the terms of the transactions they carried out.

The key to resolving issues connected with APAs is a dialogue between taxpayers and the tax administration.

4. Impact of pandemic on advance pricing arrangements

Advance pricing arrangements (APAs) are a kind of agreement between the taxpayer and the tax administration, setting conditions for intragroup transactions. Sometimes a change in market conditions or financial results can affect the validity of the APA. The OECD guidance indicates that the key to resolving issues connected with APAs is a dialogue between taxpayers and the tax administration. Undoubtedly cases may arise in which APAs cannot be performed due to the pandemic, but it is recommended to identify and document the problems connected with carrying out the APA and maintain effective communications with the tax administration.

The Polish Ministry of Finance openly declares its willingness to pursue a dialogue with taxpayers if doubts have arisen concerning compliance with existing APAs.

No special treatment

The statistics concerning transfer-pricing controls suggest that this is an area of vital interest to the tax administration, and this trend can be expected to continue. The difficulties faced by taxpayers during the pandemic, even if not treated by tax auditors as a pretext for assessing tax, can be expected to generate numerous controversies.

Transfer pricing is not an exact science. Given the challenges facing taxpayers, it should be remembered that many disputes with the tax authorities can be avoided if taxpayers are guided by the three key standards governing transfer pricing: commercial reasonableness, intellectual consistency, and a high level of diligence.

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When is exit tax not due? Analysis of practice two years after introduction of the tax on income from unrealised gains

Poland's tax on income from unrealised gains, otherwise known as the "exit tax," is a variation on the EU's Anti-Tax Avoidance Directive. Introduced on 1 January 2019, the provisions have caused controversy from the beginning. They are unclear, and their application may lead to double taxation. Two years have passed since their entry into force. We summarise this period by discussing the most interesting tax rulings and case law in relation to personal income tax payers.

The exit tax rules were added to income tax acts in Poland to transpose Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (known as the Anti–Tax Avoidance Directive or ATAD). The exit tax is intended to prevent tax avoidance involving shifting profits to countries with more favourable taxation. The member states decided to synchronise this area and introduce a single, coordinated mechanism to ensure that taxes are paid where profits are generated and value is created.

The ATAD itself applies only to payers of corporate income tax (CIT), and applies when assets, tax residence or a permanent establishment is transferred from a member state to another member state or a third country. In Poland, the regulations differ in some respects from the ATAD—most importantly in imposing exit tax on payers of personal income tax (PIT).

Simply put, the exit tax mechanism consists in adoption of the legal fiction that the taxpayer has disposed of assets for

TAX ON INCOME FROM UNREALISED GAINS

The tax applies when a PIT payer:

- Transfers assets outside Poland, while the transferred asset remains the property of the same person
- Changes tax residence
- Transfers an asset in Poland to another entity without consideration, or
- Contributes an asset to an entity other than a company or cooperative

and, as a result of such action, Poland loses all or part of the right to tax income from the disposal of such assets and assets owned by the taxpayer changing his residence.

ASSETS NOT LINKED TO BUSINESS ACTIVITY THAT MAY BE SUBJECT TO EXIT TAX

In the case of a change of tax residence, the tax on income from unrealised gains is imposed only on assets defined as personal property and constituting:

- Rights and obligations in a partnership (not a legal person)
- Shares, stock and other securities
- Derivatives, or
- Participation units in investment funds

where the taxpayer was residing in Poland for a total of at least five years during the ten-year period prior to the date of change in tax residence.

consideration, where the income subject to taxation is the surplus of the market value of the assets over their tax value (as a rule, the tax value is the historical cost of acquisition or production, less any depreciation write-offs made for tax purposes).

The exit tax provisions are similar for CIT and PIT payers. However, in the case of PIT payers, it is stipulated that the exit tax is applicable if the total market value of the transferred assets exceeds PLN 4 million.

Moreover, the PIT Act contains special regulations applicable to taxpayers who are spouses whose property is subject to the marital property regime. For such taxpayers, the market value of the assets is determined for each spouse as half of the market value of the assets. The PLN 4 million limit applies jointly to the market value of the assets of both spouses.

As a rule, the tax rate is 19%, but with respect to assets for which the tax value is not determined, PIT payers are subject to taxation at the rate of 3%.

The exit tax can increase the cost of cross-border business reorganisation and relocation, even if it is not driven by tax considerations. The tax can also affect wealth management strategies, as for example the use of a foreign foundation for wealth planning may be subject to the tax on income from unrealised gains. Taxpayers have raised doubts related to these processes in applications for individual tax rulings.

Exit tax on gifts

The most common exit tax issue relates to the possibility of taxing a Polish benefactor giving gifts to close relatives residing permanently outside of Poland.

These doubts involve such questions as:

- Simultaneous taxation of a gift with inheritance and gift tax and PIT
- Applying the exit tax to gifts of personal property
- Taxation of gifts of assets located for a long period outside of Poland.

The first doubt is raised by the provisions of the PIT Act expressly stating that the act does not apply to revenues subject to the Inheritance and Gift Tax Act. Thus, because gifts are subject to inheritance and gift tax, they are not subject to PIT.

In turn, the exit tax rules provide that exit tax applies, among other things, to a transfer without consideration (i.e. also a gift) of an asset located in Poland to another entity if, in connection with the transfer, Poland loses all or part of its right to tax income from disposal of the asset.

The Head of National Tax Information (KIS) took a pro-fiscal stance on this issue, holding that the subject of inheritance and gift tax does not overlap with the subject of the tax on income from unrealised gains.[1] In other words, inheritance and gift tax is imposed on the receipt of a gift, while the exit tax is imposed on the giving of a gift. Economically, this can lead to double (or even multiple) taxation of the same gain. This approach by the Head of KIS was shared in a pair of rulings by the Province

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Administrative Court in Bydgoszcz.[2] Neither judgment is final yet.

The second doubt arose in a case where a taxpayer argued that the exit tax does not apply to the gift of a personal asset, in which category the law explicitly includes shares in a company. According to the taxpayer, the tax on income from unrealised gains allows for taxation of personal assets in the event of a change in tax residency by an individual, while in the case of a gift, the tax can only apply to assets related to the taxpayer's business activity. The taxpayer also pointed out that extending the exit tax to gifts unjustifiably differentiates in the situation of two donors, one who makes a gift to a Polish tax resident and the other to a non-resident. The Head of KIS reasoned that a transfer without consideration (gift) of an asset located in Poland by a Polish tax resident to an entity that is not a Polish tax resident will cause Poland to lose its right to tax income from disposal of the asset. Thus, the transfer of shares will give rise to an obligation on the part of the donor to pay the tax on income from unrealised gains.[3]

The Province Administrative Court in Bydgoszcz overruled that individual tax ruling and held that the exit tax does not apply to a gift made from personal property (i.e. not connected with the taxpayer's business activity) by the applicant to her son, who is a tax resident of another country. The court reasoned that "personal property" cannot be equated with an "asset," and thus, as the exit tax applies to transfer abroad without consideration of an "asset," transfer abroad without consideration of "personal property" cannot be subject to exit tax. According to the court, this interpretation is also supported by EU regulations, as the ATAD does not provide for imposition of tax on income from unrealised gains on the gratuitous transfer of personal property. According to the court, the fact that the ATAD sets only a general, minimum level of protection against aggressive tax planning does not give the member states licence to introduce provisions unsupported by the directive.[4] The judgment is not yet final.

ACCORDING TO THE COURTS:

1 Inheritance and gift tax taxes the receipt of a gift, while exit tax taxes the giving of a gift.

2 "Personal property" cannot be equated with an "asset." A transfer without consideration of an asset abroad to another entity is taxable, while a transfer without consideration of personal property is not.

3 If shares in a foreign company are owned by a Polish tax resident, they are deemed to be an asset situated in Poland for purposes of the exit tax regulations.

The source of the third doubt is the language of the act indicating that a transfer without consideration is subject to taxation if it concerns "an asset located in the territory of the Republic of Poland." Based on the literal meaning of that provision, the Polish taxpayer wanted to ascertain that shares in a foreign company are not an asset located in Poland and their gift to a family member will not be subject to exit tax.

The Head of KIS made a different, functional interpretation of the law. She found that shares in a foreign company are an asset located in the territory of Poland, within the meaning of the exit tax rules, as the income from their disposal is subject to Polish tax jurisdiction due to their "allocation" to a person with tax residency in Poland, i.e. subject to unlimited tax liability in Poland.[5] This ruling was upheld by the Province Administrative Court in Bydgoszcz.[6] Those judgments are not yet final.

New opening for limited partnerships in 2021

In November 2020, the Head of KIS issued a tax ruling confirming that there is no obligation to pay exit tax in the case of a change of residence from Poland to Switzerland by a taxpayer who was a limited partner in a Polish limited partnership which did not qualify as a real estate company. The ruling stated that a tax-transparent limited partnership constitutes a permanent establishment in Poland within the meaning of the tax treaty between Poland and Switzerland, leading to taxation in Poland of income from the disposal of assets and of the totality of rights and obligations in such a partnership. The change of tax residency did not cause the event to be subject to exit tax, as Poland retained the right to tax income from any potential disposal of the totality of rights and obligations in the limited partnership.[7]

But starting from 1 January 2021, the underlying situation has changed. Limited partnerships ceased to be tax-transparent entities, and became CIT payers. As a result, limited partnerships no longer constitute a permanent establishment within the meaning of the wealth transfer provisions in tax treaties. Apparently, this means that the reasoning by the Head of KIS in the individual tax ruling referred to above is no longer valid, and partners of limited partnerships who change their tax residency may be obliged to pay exit tax if the other conditions of the regulation are met.

Exit tax and CFCs

Taxpayers also wondered whether an obligation to pay exit tax arises when assets are transferred from Poland abroad to an entity constituting a controlled foreign corporation (CFC) with respect to a taxpayer who is a Polish tax resident. The enquiries concerned the transfer of assets to a family foundation in Liechtenstein. Such a foundation may constitute a CFC for the founder of such an entity or its beneficiaries. The CFC regulations are designed to preserve Poland's right to tax the income of foreign entities controlled by Polish tax residents when those entities are located in jurisdictions with advantageous tax regimes and the entities mainly generate passive income. CFC status means that income earned by such an entity, including income from the disposal of contributed assets, may effectively be taxed in Poland under the CFC rules.

The Head of KIS found that since taxation in Poland under the CFC regime is imposed, among other things, on the disposal of assets by a foreign foundation, the transfer of such assets to the foundation does not mean that Poland loses the right to tax income from their disposal. Consequently, transfer of the assets to the foundation in that scenario is not subject to exit tax in Poland. A different interpretation of the regulations would lead to double taxation of the same income.[8]

Two years of incomplete answers

Individual tax rulings issued in the first two years the exit tax has been in force have outlined the position of the tax administration in key areas for taxpayers. The issue of the relationship between controlled foreign corporations and exit tax has been resolved to the advantage of taxpayers in a manner allowing them to avoid the risk of double taxation. It should be borne in mind that no exit tax will be due if certain conditions are met regarding the transfer of assets abroad. The position concerning taxation of partners' withdrawal from limited partnerships should be assessed positively, but due to the change in CIT regulations it will not apply to withdrawals in the future.

Over the next two years, we should learn the answer to more questions and find out how the dispute over the exit tax treatment of gifts of personal property to non-residents ends.

1 Individual tax rulings of Head of KIS dated 7 May 2020, no. 0113-KDIPT2-3.4011.182.2020.1.JŚ, and 21 April 2020, no. 0115-KDIT3.4011.228.2020.1.KR

2 Judgments of Province Administrative Court in Bydgoszcz of 5 February 2020, case nos. I SA/Bd 782/19 and 783/19

3 Individual tax ruling of Head of KIS dated 21 April 2020, no. 0115-KDIT3.4011.228.2020.1.KR

4 Judgment of Province Administrative Court in Bydgoszcz of 7 October 2020, case no. I SA/Bd 375/20

5 Individual tax rulings of Head of KIS dated 21 October 2019, no. 0115-KDIT2-1.4011.264.2019.6.MT, and 21 October 2019, no. 0115-KDIT2-1.4011.265.2019.3.MT

6 Judgments of Province Administrative Court in Bydgoszcz of 5 February 2020, case nos. I SA/Bd 782/19 and 783/19

7 Individual tax ruling of Head of KIS dated 26 November 2020, no. 0115-KDIT1.4011.630.2020.3.MT

8 Individual tax rulings of Head of KIS dated 18 July 2019, no. 0114-KDIP3-2.4011.223.2019.5.AK, and 8 November 2019, nos. 0114-KDIP3-2.4011.470.2019.1.LS and 0114-KDIP3-2.4011.471.2019.1.LS

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The need for a holding law in Poland

The corporate law in force in Poland for 20 years has fallen behind the reality in which the companies covered by the law actually operate. The Commercial Companies Code has been amended numerous times since it was adopted, but these changes have not addressed all essential areas. Undoubtedly one overlooked area is the activity of a "holding," i.e. a group of entities (including companies) all controlled by one or more dominant entities, where the group pursues business operations jointly—either contractually or *de facto*.

Polish law does not currently contain a coherent set of regulations governing holdings. True, tax and accounting law include makeshift measures in this regard, such as the "tax capital group" and provisions on preparation of consolidated financial reports, and more recently, also regulations on disclosure of beneficial owners, referring indirectly to links of the holding type. But these are not so much comprehensive provisions governing the issue of holdings, as they are provisions addressing point by point selected consequences of the fact of existence of holding structures.

Rudimentary regulations…

At the key level for companies, the lack of such comprehensive solutions in the Commercial Companies Code is all too evident. While the code does contain provisions requiring disclosure of relations of dominance between companies, and includes certain restrictions on actions between companies, it does not reflect the fact that a significant number of companies (having more to do with the economic weight of these entities than their sheer number) are not in practice independent commercial entities, but *de facto* are components of a larger structure.

Nothing is changed in this respect by Art. 7 of the code, concerning subsidiary management contracts (intended by the drafters to be an instrument regulating, in however limited a scope, the activity of companies that are in practice dependent on other entities). Since entry into force of the Commercial Companies Code in 2001, this provision has for all intents and purposes been a dead letter.

...versus practice

The current regulations still seem to refer more to the notion of a "merchant" (which existed under the old Commercial Code of 1934, replaced by the Commercial Companies Code) than to a business entity in the contemporary understanding. A business entity is not just an individual who sometimes operates commercial activity in the form of a commercial-law company, but first and foremost refers to the company itself which operates such activity (itself being indirectly, or less often directly, owned by a larger number of individuals or other legal entities).

Thus in commercial practice, a company (with one or more owners) may form or acquire another company, to conduct a new business through that company, to take over the activity of another enterprise, its clientele, knowhow, and so on. This gives rise to international holdings made up of dozens of companies in different countries. A company at the bottom of this corporate ladder may be a separate legal person in the eyes of the law, but in practice it is not a standalone entity. To the contrary, it is part of a larger structure, and its role in the structure is that the holding expects it to pursue specific aims set by the holding—not determined by the company itself.

This is where, in the Polish legal system, there is a collision between law and reality. The law not only vests each company with individual personality (regardless of its location on the holding structure ladder), but deems each company to possess its own, separate interest. Under the regulations in force in Poland, the managers of each company should pursue and protect the interest of the individual company.

For simplicity, in the rest of these remarks we will ignore companies (quite common in Poland) with participation of minority shareholders, focusing instead on companies 100% owned by another company, thus making them wholly dependent parts of a holding structure (although most of the remarks will also apply as relevant to companies that have minority shareholders alongside an entity that is dominant in terms of its capital share or number of votes).

The interest of the company and the interest of the group

The problem with the existence and duty of acting in the interest of the specific company is that sometimes something that may seem disadvantageous from the perspective of the specific company (e.g. conclusion of a certain contract, pursuing or not pursuing a certain line of business, or sale of certain assets or business lines to another affiliated entity) may be advantageous from the perspective of the corporate group as a whole (the holding), because it will unleash synergies, cut the costs of management or purchasing, and so on. Ultimately such action is taken in the best interest of the shareholders of the company standing at the top of the holding structure ladder.

Indeed, this is the aim of a corporate group—often operating on a range of markets and allocating its capacity and resources where it is most advantageous.

Today, under Polish law, acting in this manner, in compliance with the policy of the group, may result in civil liability to the company of the company's management board members, as well as liability to stakeholders in the company (including creditors). In an extreme case this could be found to be acting to the detriment of the company, which is subject to criminal liability. Moreover, criminal liability in this scenario may arise regardless of whether the company or its sole shareholder "feels" it has suffered any injury. This is because offences involving acting to the detriment of a company are prosecuted publicly (*ex officio*, and thus in extreme cases even against the wishes of the company or its owners).

> **Here there is a collision between law and reality. The law not only vests each company with individual personality, but deems each company to possess its own, separate interest.**

Liability of managers

A separate issue connected with a subsidiary's acting in the interest of the corporate group is the legal situation of the members of the subsidiary's management board, and more specifically, whether the shareholder can effectively impose on the management board a specific manner of operation, and what the consequences of this could be for the management board members.

Under Art. 375^1 of the Commercial Companies Code, in a joint-stock company neither the general meeting nor the supervisory board may issue binding instructions to the management board on conducting the company's affairs. It is different in the case of a limited-liability company, as Art. 219 §2 contains a comparable prohibition addressed solely to the supervisory board. This is sometimes interpreted (not without reason) as the absence of a ban on issuance of such instructions by the shareholders' meeting (and thus, in the case of a wholly owned company, its sole shareholder). »

Notwithstanding the legal regulations concerning the possibility of issuing binding instructions to management boards of subsidiaries, given the actual existence of holding structures, dominant companies in fact expect their interests to be pursued at the level of subsidiaries. Consequently, managers of subsidiaries either comply with what is expected of them by the group, or they may simply be removed from office. But in practice, while remaining in office and complying with the group's instructions, they also risk personal liability for such decisions (including, it bears repeating, criminal liability). While to some extent directors and officers insurance may provide a remedy in the area of civil liability, there is no way to exclude the possibility of criminal liability.

While the risk facing management boards of small and medium-sized companies may not be great in practice, in larger companies, where certain decisions (motivated by the interest of the group) can exert consequences for example in the form of reduced tax revenue, boards are exposed to much further-reaching consequences as well as a higher probability that these risks will actually materialise.

THE HOLDING LAW SHOULD INCLUDE AT LEAST:

- The definition of a "corporate group"
- Permission for the dominant company and subsidiaries to be guided not only each by its own interest, but also—under certain conditions—by the interests of the group, while ensuring protection of the legitimate interests of the subsidiaries' creditors
- The right for the dominant company to impose certain operating methods on the subsidiary (excluding the liability of the subsidiary's management board for acting to the detriment of the subsidiary and its creditors), while regulating the rules for the dominant company's liability for acting in such manner (including liability to the subsidiary's creditors)

The need for statutory regulation

For the reasons discussed above, among others, there have long been calls in the legal literature for holding law to be regulated in Poland at the statutory level.

The aim of such efforts would obviously be first and foremost to "legalise" the existing practice, while at the same time establishing rules for the operation of holding groups and ensuring protection of stakeholders (including creditors). The existing state of the law, and more precisely the lack of relevant regulations, sometimes leads to pathological situations where formal bans on acting to the detriment of the company are ignored, to the benefit of the corporate group but at some risk to the managers of the subsidiaries and with potential injury to the subsidiaries' external stakeholders.

In mid-2020 a government draft of a holding law was released, containing provisions addressing the issues listed in the box above (alongside many other issues). As of the end of 2020 the draft was the subject of intense debate, and it cannot yet be predicted whether, when, and in what form the law will ultimately be adopted. But the discussion surrounding this proposal is undoubtedly a positive development.

OUR PUBLICATIONS

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Scholarly journal (codozasady.pl/studia-analizy). We address legally and socially important issues. We seek to make a positive contribution to the legal literature. The journal's pages are open to all members of the legal community.

codozasady.pl

Portal on law for businesses, but not only. We write about interesting rulings from the Polish and EU courts, planned and introduced changes in law, and legal nuances that can have a material impact on business.

newtech.law

Blog on new technologies law. We write about blockchain, the data economy, and artificial intelligence. We pose questions about the role of technology in life, and law in technology.

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Blog on Polish and EU employment law. We write about issues relevant to employers, rulings affecting the interpretation of employment regulations, and questions raising doubts in contracts with employees. We report on the latest changes to provisions of labour law and how to interpret them.

komentarzpzp.pl

Online legal commentary on Poland's new Public Procurement Law, updated in real time. We explain what has changed with entry into force of the new act and how to understand its provisions.

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The incentive effect: An increasingly violated condition for obtaining state aid

For state aid to be consistent with the internal market, the aid must be necessary. Support awarded from public funds must be essential for achievement of the project. Aid that does not generate an incentive effect is illegal. But the incentive effect arises not only in a situation where there is a shortage of funds for taking independent efforts. Under the EU's new financial perspective for 2021–2027, this issue will again become the subject of intense analysis on the part of applicants for state aid and institutions considering aid applications.

Under the position of the Court of Justice of the European Union on the incentive effect, originally stated in the ECJ's 1980 ruling in C-730/79, *Philip Morris Holland BV v Commission*, the necessity for aid is a fundamental condition for its consistency with the internal market, and arises directly from Art. 107(3) of the Treaty on the Functioning of the European Union.

In its 2012 communication "EU State Aid Modernisation," the European Commission also noted the need to ensure that efforts by the member states to provide state aid must be consistent with the requirement of the necessity of the aid. In announcing the process of state aid modernisation, the Commission stressed: "State aid which does not target market failures and has no incentive effect is not only a waste of public resources but it acts as a brake to growth by worsening competitive conditions in the internal market." This work led to adoption of new guidelines for analysis of the consistency of state aid with the internal market, including the incentive effect. In specific guidance laying down the conditions for the incentive effect, the Commission has generally accepted that verification of fulfilment of the incentive effect should take a dual character: substantive (economic) and procedural.

Economic and procedural aspects of the incentive effect

- Verification of the **economic existence of the incentive effect** generally consists of an objective determination that the actual conditions for realisation of a project are such that the project cannot be carried out without financing from the state.
- The **procedural analysis of the incentive effect** relies, as a rule, on the evaluation of the chronology of events, i.e. whether the beneficiary of state aid applied to the member state for the aid before commencing work on the project. This verification first requires identification of the scope of the project.

As the Court of First Instance stated in T-162/06, *Kronoply GmbH & Co. KG v Commission*, the task of this test is to check whether the incentive effect exists, but without excessively delaying the project due to time-consuming analysis of all economic aspects of the project decision by the aid beneficiary. Thus it was accepted that filing an application for award of state aid prior to commencement of execution of the project allows for a presumption of the existence of the incentive effect.

At the same time, not every action taken before submission of a project automatically excludes the possibility of obtaining state aid. For example, as the Commission stated in the Guidelines on regional State aid for 2014–2020, "'start of works' means either the start of construction works on the investment or the first firm commitment to order equipment or other commitment that makes the investment irreversible, whichever is the first in time. Buying of land and preparatory works such as obtaining permits and conducting preliminary feasibility studies are not considered as start of works. For take-overs, 'start of works' means the moment of acquiring the assets directly linked to the acquired establishment." (Comparable guidelines have not yet been issued for 2021–2027.) The method for fulfilling the incentive effect may also be specified in the conditions for seeking funding within the specific programme.

Chronology of measures for fulfilling the incentive effect

In the first order, assessment of the existence of the incentive effect depends on the nature of the work to be carried out. For example, commencement of construction work or a firm commitment to order equipment indicates that works have started under the given facts.

Meanwhile, "firm commitment" is understood to mean any form of agreement, but it is the conditions contained in the agreement and not the formal classification of the agreement that are controlling. If the agreement is constructed so that from an economic perspective abandoning the venture is difficult, and in particular would result in the loss of significant amounts (e.g. it would entail major costs to be incurred), then it should generally be recognised that works have started. The mere inclusion in the agreement of a provision enabling unilateral termination will not always suffice to find that works have not started.

Finally, when analysing the condition of the existence of a "commitment that makes the investment irreversible," it should be determined whether the entity, guided by the logic of a private investor, would abandon completion of the venture and thus allow funds to be forfeited. In this respect, a commitment means any engagement by the beneficiary in realisation of the project such that objectively, under normal circumstances, it may be stated that it is the beneficiary's intention to carry out the project, whether or not it obtains state aid, and not just incurring an obligation within the meaning of civil law.

The incentive effect in judicial practice

The necessity for the aid in substantive and procedural terms has been the subject of assessment numerous times both by institutions responsible for implementing aid funds and by the courts called upon to resolve disputes by unsuccessful applicants for state aid or entities ordered to return funds already received. A review of the case law provides many examples of how the incentive effect is interpreted by entities scrupulously pursuing ventures in compliance with the rules and by entities sometimes knowingly violating the rules.

For example, in the judgment of 26 March 2015 (case no. I ACa 47/15), the Kraków Court of Appeal ruled on the case of a beneficiary carrying out a project involving the purchase of machinery which allegedly greatly increased its competitiveness. The beneficiary had previously leased the same equipment which it purchased in

CHRONOLOGY OF MEASURES FOR FULFILLING THE INCENTIVE EFFECT

the project. In the view of the implementing authority, this demonstrated infringement of the incentive effect. But the court did not share this view, finding that the beneficiary had taken an economically justified decision to purchase modified machinery which it had previously leased. This contributed to growth of the enterprise and fit within the aims of the operational programme in which the purchase was made. The purchase of different machinery would lack economic justification. The court reasoned that disputing the purchase of machinery solely because it had the same serial numbers as the previously leased machinery showed that the implementing authority valued an empty formalism over entrepreneurship and economic rationales.

Even non-culpable actions causing violation of the incentive effect result in failure to award the benefit or withdrawal of the benefit.

The procedural aspect of the incentive effect was addressed for example by the Province Administrative Court in Lublin in its judgment of 21 December 2010 (case no. I SA/Lu 877/10), which found that the scope of the venture submitted for funding did not constitute the sole, exclusive criterion for identifying the intended commercial venture. Thus the examination of whether the aid exerts an incentive effect is not limited to studying the scope of the eligible costs. All measures essential to achieve the aims of the project (the priority axis for the project) must be assessed.

As the Province Administrative Court in Gorzów Wielkopolski held in its judgment of 23 July 2015 (case no. II SA/Go 322/15), existence of the incentive effect is examined with respect to the entire project, not just the specific project aims covered by the application (which in the case of lack of the incentive effect for one or more project measures would not exclude funding for the rest of the project). Considering the case of an applicant seeking funding for a project for construction of a transformer station and purchase of equipment, the court held: "In imposing the incentive requirement, the EU regulations do not tie it to specific investments covered by one project, but treat the given venture as a whole, as the project covered by the application. The situation cannot be excluded where realisation of a project requires several investments to be carried out, but the incentive effect applies to the project as a whole." A similar finding was made by the Lublin Regional Court in its judgment of 27 March 2014 (case no. I C 581/11), where the court stressed that all phases of the project covered by the funding, regardless of their technological importance and role in the investment process, belong to one and the same project if they are part of the overall plan.

The Supreme Administrative Court judgment of 14 January 2020 (case no. I GSK 2137/19) involved a company planning to implement a project consisting of the launch of an innovative composite material for manufacturing furniture accessories. The company applied for funding for the purchase of equipment for manufacturing furniture accessories and at the same time was conducting work on construction of a manufacturing and warehouse facility. The court found that contrary to the authority's claim, construction of the new plant was a separate investment from the one submitted for funding, and construction of the plant did not cause the project covered by the funding application to become "irreversible," because the new facility would also be used for other activity of the applicant. Because the funding application did not cover construction of the plant, holding back the start of construction of the facility until the contest was completed would lack economical and organisational justification. Construction of the manufacturing and warehouse facility was complementary to but independent from the intended project, and did not constitute the start of works on the project submitted for funding. Thus it did not exclude the incentive effect.

Nor is the existence or absence of the incentive effect determined by the amount of costs incurred before filing of the application for funding, In T-551/10, *Fri-El Acerra Srl v Commission*, the General Court held that the mere fact that the works commenced before filing of the aid application constituted only 10% of the overall costs of the project was insufficient in itself to find that the works on the project were not begun. On the other hand, in the judgment of 22 June 2017 (case no. III SA/Lu 212/17), the Province Administrative Court in Lublin held that the purchase of land did not exclude the incentive effect, even though it required significant investment outlays to be incurred, because the acquired property could be used in different ways, not only for the specific project for which funding was sought. The court also held that work on the project could not be deemed to have started because the applicant had obtained permits and conducted feasibility studies, as these constituted only preparatory works preceding commencement of realisation of the project.

And in the judgment of 22 March 2017 (case no. II GSK 472/17), the Supreme Administrative Court rejected the authority's argument that for the incentive effect to be fulfilled, only new material resources, arising after filing of the funding application, could be used in the project. There the court found that the company was entitled to submit a project in the recruitment which would not only result in a new drilling service, but also in an improved service, and thus the execution of borings using a drill also in the applicant's possession, but as part of a cheaper and more modern technological line created with EU support, demonstrated the market launch of an improved service, and thus the requirements of the incentive effect were met.

Good faith

For assessing the existence of the incentive effect, it is irrelevant whether the applicant knowingly began work on the project before filing the application (guided by its economic interest), or was unaware of the consequences of its actions. Even non-culpable actions causing violation of the incentive effect result in failure to award the benefit (if determination of the absence of the incentive effect occurs at the stage of evaluation of the funding application) or withdrawal of the benefit (if the aid has already been paid out). Payment of aid as to which it is later determined that the aid did not exert the incentive effect fulfils the condition referred to in Art. 207(1)(3) of the Public Finance Act of 27 August 2009 for return of improperly disbursed EU funds.

Regardless of the sanction for the absence of the incentive effect, some applicants, aware that their actions have excluded the incentive effect, nonetheless attempt to conceal this information from the intermediate body or implementing authority. An example is the matter decided by the Lublin Regional Court in the judgment of 27 March 2014 (case no. C 581/11), where the court found that entries in the construction log identifying the date of commencement of preparatory work on the construction site had simply been falsified.

Some entities seeking protection against the effects of a finding by the relevant institution that the aid would not exert the incentive effect try to unwind the legal effectiveness of transactions connected with launch of the project, e.g. by terminating contracts retroactively. The courts generally deny protection to such actions. For example, in the judgment of 4 September 2014 (case no. I ACa 347/14), the Katowice Court of Appeal held that the beneficiary's action of dissolving its agreement with the contractor, originally concluded before applying for aid, and subsequent conclusion of a new agreement with the same contractor, was ineffective and did not alter the validity of the institution's cancellation of the funding agreement. In the court's view, by incurring a legally binding obligation to order movable fixed assets prior to filing an application for public funds, the enterprise breached its contractual obligations to the institution with which it had concluded a funding agreement.

In light of the harsh and unequivocal consequences of violating the incentive effect, any entity seeking state aid should set clear bounds for the planned project and not commence actions connected with the project before filing an application for support. If the applicant's economic interest dictates that it undertake certain measures, for example aimed at faster or more efficient realisation of the project, it must weigh the risk that the intermediate body or managing authority will refuse to grant the aid. And the civil courts ruling in cases involving the performance of concluded funding contracts very rarely depart from rigorous enforcement of this rule. Rulings in favour of beneficiaries are typically issued only when the intermediate body or managing authority has made an error in its assessment of the facts of the case.

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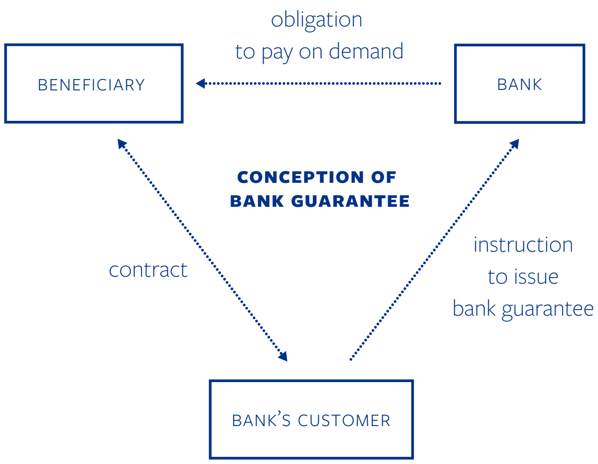
Word is bond: Payment under a bank guarantee (particularly in public procurement)

In any crisis, bank guarantees assume greater importance, as many people regard them as a "sure thing" among security instruments. But before popping the cork on the champagne, we suggest careful review of the guarantee's wording and being aware of the subtle consequences of this trilateral construction.

The bank guarantee is a basic banking product, universal and standardised. There are a number of types of bank guarantees, but one of the most popular is an unconditional and irrevocable guarantee payable "on first demand" securing the performance of an obligation by the bank's customer under a contract concluded between the customer and the beneficiary of the guarantee.

The concept seems simple: instead of for example a cash deposit, the beneficiary of the guarantee receives the bank's commitment that if only it receives a demand from the beneficiary, it will pay the beneficiary the relevant amount. Typically no conditions are stated in this type of guarantee; the beneficiary must only submit a demand for payment along with a statement that the secured obligation was not performed. Thus the beneficiary of a bank guarantee should theoretically be able to rest easy—instead of becoming entangled in a dispute at the level of the specific contract and worrying about the solvency of its counterparty (the bank-guarantee customer), the beneficiary submits a demand for payment to a debtor that is practically rock-solid (i.e. the bank) under an instrument that in theory should be automatic (i.e. a bank guarantee to be paid "on first demand").

But practice proves to be more complex than theory. We will examine two nuances complicating the apparent simplicity of this mechanism: the triangular arrangement of this instrument, and the weight of each word included in the guarantee.



A triangular arrangement

Beneficiaries are often aware of only a portion of the mechanism that most often occurs at the bank when a demand for payment is submitted. But the process can be much more complex.

When the beneficiary submits the demand for payment, the bank immediately informs its customer of receipt of the demand. The customer typically has an obligation to pay funds into its bank account maintained at the guarantor bank in an amount equal to the demand within one or two business days before the planned pay-out. This way, on the date of payment the bank can simply withdraw the customer's funds and pay out the same amount to the beneficiary. But it can easily be seen that a side effect of notifying the customer is to draw the customer into the dispute at the level of the guarantee, enabling a counterattack, for example by filing an application with the court seeking relief in the form of an injunction against pay-out by the bank of amounts under the guarantee.

Another aspect which the beneficiary should note is the relationship between the guarantor bank and the customer which has procured the issuance of the bank guarantee. It is after all a client of the bank, and often the bank guarantee is only one of many products purchased from the bank by the client. Thus it may happen that the bank and the customer are in regular contact.

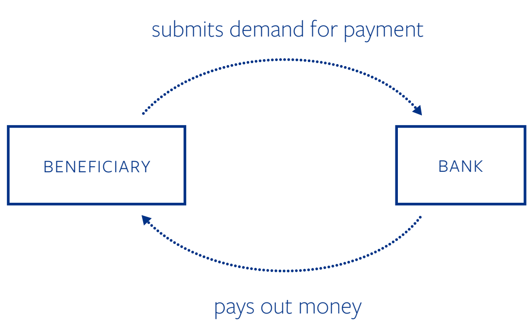
Moreover, as mentioned above, the amount of the pay-out under the guarantee may be funded by the bank in advance or immediately recovered from the customer. In many instances, a problematic situation may arise from the bank's perspective. For example, if the customer that procured issuance of the guarantee is in financial difficulty, the bank, realising the increased risk of an inability to simply withdraw the funds from the customer's account, may review the payment of the guarantee more closely than it otherwise might have—including an examination of the conditions for the payment.

The weight of each word in the guarantee

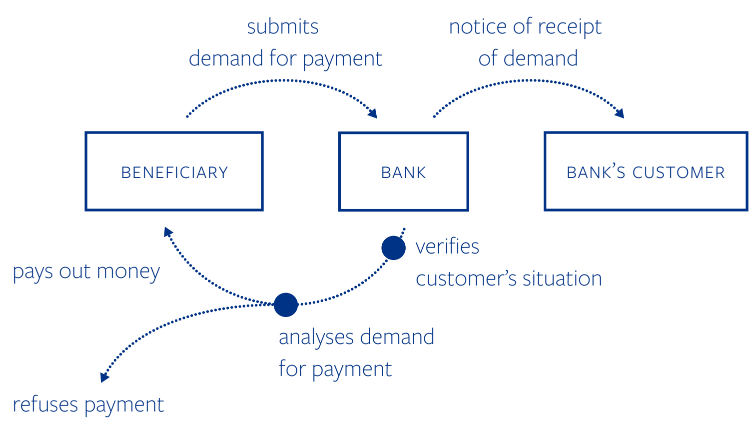
Clearly, the most frequent ground for refusing to pay out on a bank guarantee is failure to comply with the formal requirements for the demand. This is why it is essential both to formulate the conditions unequivocally (particularly in technical respects) and subsequently to analyse the text of the guarantee and to comply literally, in all details, as instructed in the guarantee. This is particularly vital when

PAYMENT OF GUARANTEE

AS IMAGINED BY BENEFICIARY



REAL PROCESS



the validity of the guarantee is nearing an end—when, in short, there will be no second chance. And this applies not only to the issue of the demand.

The importance of the wording of the guarantee was driven home to a consortium competing with a client of ours for a lucrative public contract. The consortium secured its offer in the tender with a bid bond in the form of a bank guarantee issued at the instructions of one of the consortium members. The consortium's offer was rejected, and it lost its chance to win the contract. The bid bond document was issued for one of the members of the consortium, and after a thorough analysis both the contracting authority and the National Appeal Chamber (KIO) found that under the wording of the bank guarantee, the guarantee would pay out **only** in the event of a breach by the specific member of the consortium which was the bank's customer, not a breach by any or all of the consortium members.

Joint and several liability of consortium members does not automatically mean that a bid bond in the form of a bank guarantee secures the offer of the entire consortium. The wording of the guarantee is decisive.

THE CONTRACTING AUTHORITY WILL RETAIN THE BID BOND IF:

1. For reasons attributable to the contractor, the contractor fails to submit statements, documents or powers of attorney demanded by the contracting authority
2. The offer contains errors or oversights rendering it non-compliant with the terms of reference for the procurement, but the contractor refuses to consent to correction of errors or oversights which would not materially modify the offer
3. The contractor refuses to sign the contract under the terms specified in the offer
4. The contractor fails to submit required security for proper execution of the contract, or
5. Conclusion of the contract has become impossible for reasons attributable to the contractor.

It is permissible for a bid bond to be submitted by one consortium member, but the bank guarantee submitted to the contracting authority must expressly provide that it secures the offer of the entire consortium, and the contracting authority will be able to draw on the guarantee regardless of which consortium member breached its obligations connected with participation in the tender. Let's examine this issue more closely.

Use of a bank guarantee for a bid bond

The use of bank guarantees as bid bonds raises a number of issues in public procurement practice, and there is a wealth of case law on irregularities in bid bonds. This arises from the importance of the bid bond: it cannot be supplemented; if it is not properly submitted it is regarded as a nullity; and an offer not properly secured by a bid bond is subject to rejection.

As of the time of opening of the offers, the contracting authority must be certain of pay-out of the bid bond. Because the bid bond document cannot be corrected, the conditions for payment stated in the document must be precise enough that the contracting authority has no doubt that it will be able to obtain satisfaction when it is authorised to enforce the bond.

The instances where the bid bond may be retained do not have to be expressly listed in the wording of a bid-bond bank guarantee, but it must be clear from the wording that any time the contracting authority is entitled to retain the bid bond, it will obtain payment of the guarantee. The situation of the contracting authority which accepts a bid bond in a form other than cash must not be any worse than if it held the amount of the bid bond paid in cash. In other words, the bank guarantee must be worded so correctly and clearly that it becomes an equivalent of cash.

Bank guarantee submitted as the bid bond for a consortium

If a bid-bond bank guarantee is obtained by only one member of a consortium, it is essential that the bank guarantee secure not only acts and omissions by this one member (or acts and omissions for which that member is responsible), but also acts and omissions on the part of other members of the consortium. This is not an "automatic" issue in the context of the consortium members' joint and several liability to the contracting authority, which also exists at the stage of the tender.

Any variation in framing the results of the security which could even potentially narrow the scope of the guarantor's liability will result in a finding that the bid bond was not properly submitted. The contracting authority must have no doubts that the bank will pay out the sum of the guarantee regardless of which consortium member caused the need to retain the bid bond.

If the consortium leader does not present the required document concerning another member of the consortium, because that member failed to obtain the document, this is tantamount to failure to present the document for reasons attributable to that other member, and not attributable to the consortium leader. If only the leader is mentioned in the bank guarantee, then the bid bond will not be effectively received by the contracting authority.

Customarily, a bid-bond guarantee submitted by a consortium will expressly state that the contractor is participating in the tender in the form of a consortium, and go on to list all of the members of the consortium. There are known instances where an offer by a consortium has been rejected where the bid-bond guarantee listed entities other than those making up the consortium filing the offer. This is not such an unusual mistake, as decisions on the offering structure are quite dynamic and can be finalised shortly before the deadline for filing the offer. And joint participation in a tender is possible not only in the form of a consortium. Entities may also rely on essential capacity via subcontracting, which entails lesser liability for the entity lending its capacity. By the time these entities reach agreement, there may not be enough time to obtain a bid bond in the form of a bank guarantee.

But if at the time the bank guarantee is being obtained the offering structure could still change, it is important to state in the guarantee that it secures the offer of the consortium. In this respect, it is not necessary to name all of the members of the consortium. A good method of identifying the consortium is to identify the entity serving as consortium leader (typically the customer applying for issuance of the guarantee) and to expressly state that the guarantee secures obligations and events involving any member of the consortium.

It should be borne in mind that the bid bond must be correct from the very start. The contracting authority will evaluate the documents, including the bank guarantee, upon opening of the offers. Any gaps or imperfections in the wording of the bid-bond bank guarantee cannot be cured through a subsequent clarification by the bank; the bank cannot confirm after the fact that it would pay out the bid bond in this or that situation. That possibility would infringe the rule of equal treatment of contractors: each contractor must submit a proper bid bond by the deadline for opening of the offers, and each contractor must bear the consequences of selection of the bank guarantee as the form for the bid bond. It is up to the contractors to ensure that the bid-bond bank guarantee is free of errors.

This is a universal pointer. Although the wording of a bank guarantee "on first demand" might seem to be standard, it is always better to examine the content in good time, regardless of which side of the contract we are on.

MOST COMMON ERRORS IN BID-BOND GUARANTEES

1. Erroneous identification of the contracting authority or beneficiary (name, address)
2. Erroneous identification of the contractor (individually or as a consortium)
3. Erroneous identification of the contract award procedure
4. Erroneous specification of the sum of the guarantee (amount, currency)
5. Erroneous specification of the validity period
6. Erroneous specification of the grounds for retaining the bid bond
7. Erroneous specification of the grounds for lapse of the bid bond
8. Governing law inconsistent with contracting authority's instructions
9. Inclusion of additional obligations that must be fulfilled to obtain payment of the bond

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Tax instruments supporting innovation

Poland is continually expanding the palette of instruments aimed at fostering innovation. Tax instruments can supplement or replace financing from public funds.

Non-refundable financing

Poland will be the largest beneficiary of European Union funds in 2021–2027. "Smart Europe" is one of the main targets of the new EU financial perspective, and should directly or indirectly contribute to creation and growth of innovative ventures, which can count on significant support. Among the programmes administered at the national level, the most important from the perspective of pursuing innovative activity are to be regional operational programmes for individual provinces as well as a nationwide operational programme, the successor to the Smart Growth Operational Programme which ran from 2014 to 2020.

Innovative projects can also benefit from programmes administered directly at the EU level.

Moreover, innovative activity can be co-financed by non-refundable government grants awarded under the Programme for Support of Investments of Vital Importance for the Polish Economy for 2011–2030, adopted by the Council of Ministers on 5 July 2011 (amended 1 October 2019).

R&D relief

Relief for research and development activity is addressed to businesses conducting R&D work in their operations, within the meaning of income tax regulations (personal income tax or corporate income tax), i.e. research (basic and applied) and experimental development work as defined in Art. 4(3) of the Higher Education and Science Law of 20 July 2018. In practice, a taxpayer may benefit from R&D relief regardless of whether it has a separate R&D division, and regardless of the results of its R&D work.

R&D relief consists of the possibility of taking an additional deduction from income of tax costs in the given year constituting eligible costs incurred for R&D activity, in the amount of 100% for 2018–2020 (150% in the case of an R&D centre), 30–50% for 2017, and 10–30% for 2016. Settlement of the R&D relief can be carried back to tax years that are not yet time-barred. Eligible costs cover primarily salary of employees and associates and expenditures on goods and materials used in R&D activity.

If the taxpayer generates a loss for the year or the amount of the relief exceeds the net taxable income, the relief can be applied in subsequent years—three years in the case of R&D relief for 2016 or six years in the case of R&D relief for 2017 or later.

Taxpayers operating in a special economic zone (SSE) or the Polish Investment Zone (PSI) based on a licence or decision may apply R&D relief with respect to eligible costs that are not included in the calculation of income exempt from tax based on the licence or decision.

R&D—creative and systematic work involving research or experimental development, undertaken in order to increase the stock of knowledge and to devise new applications of available knowledge.

Research

- **Basic research**
  experimental or theoretical work undertaken primarily to acquire new knowledge of the underlying foundations of phenomena and observable facts, without any particular application or use in view.
- **Applied research**
  original investigation undertaken to acquire new knowledge, directed primarily towards development of new products, processes or services or introducing substantial improvements to existing ones.

Experimental development
systematic work drawing on knowledge gained from research and practical experience and producing additional knowledge (including IT tools or software), which is directed to producing new products or processes or to improving existing products or processes, excluding routine changes even if they constitute improvements.

CHANGE IN TAX BURDEN WITH R&D RELIEF

	PLN
Taxable revenue	5,000,000
Amount of ineligible costs	2,000,000
Amount of eligible costs	**1,000,000**

	TAX BASIS	TAX (RATE 19%)
With R&D relief	5,000,000 – (2,000,000 + 2 × 1,000,000) = 1,000,000	190,000
Without R&D relief	5,000,000 – (2,000,000 + 1,000,000) = 2,000,000	380,000

IP Box

The IP Box allows the use of a lower 5% income tax rate (CIT/PIT) in the annual settlement of these taxes by entities earning income from the commercialisation of qualified intellectual property rights created or developed by them through R&D activity. The IP Box applies if all three of the following conditions are met:

- The taxpayer generates revenue from commercialisation of statutorily defined "qualified intellectual property rights" (QIPRs), which include rights to patents, utility models, industrial designs, integrated circuit topographies, supplementary protection rights to patents for medicinal products or plant protection products, rights from registration of a medicinal product or veterinary medicine with marketing authorisation, exclusive rights under the Act on Legal Protection of Plant Varieties of 26 June 2003, and copyright to a computer program—subject to legal protection under separate acts or ratified international agreements to which Poland is a party or other international agreements to which the EU is a party. (Also earning income from other sources does not prevent use of the IP Box.)
- The subject of protection of rights qualifying for the IP Box (e.g. patent or software) was created, developed or improved by the taxpayer as part of R&D activity conducted by the taxpayer.
- The taxpayer maintains the statutorily required records in a manner enabling determination of revenue, tax-deductible costs, and net income (or loss).

The amount of income subject to taxation at the preferential 5% rate is the product of the income from QIPRs achieved in the given tax year and an adjustment known as the "nexus factor." Income (or loss) from QIPRs is income (or loss) from:

- Fees or receivables under a licence agreement involving QIPRs
- Sale of QIPRs
- QIPRs reflected in the sale price of goods or service
- Damages for infringement of QIPRs awarded in a contentious proceeding (judicial or arbitration)
- The costs of earning this revenue, including indirect costs.

$$\text{NEXUS FACTOR} = \frac{(a + b) \times 1.3}{a + b + c + d}$$

a R&D related to QIPRs directly conducted by the taxpayer

b acquisition of R&D results related to QIPRs other than those falling under *d* from an **unrelated** entity (within the meaning of transfer-pricing regulations)

c acquisition of R&D results related to QIPRs other than those falling under *d* from a **related** entity (within the meaning of transfer-pricing regulations)

d acquisition of QIPRs by the taxpayer

Polish Investment Zone

The Polish Investment Zone is a support instrument for investors introduced in 2018, designed to replace the existing special economic zones (which will be phased out by 2026). It enables businesses carrying out new investments, including R&D, throughout Poland to obtain exemption from income tax (CIT/PIT). Exemption from income tax is granted at the request of an undertaking meeting certain quantitative and qualitative criteria, via a support decision issued for a definite period (10, 12 or 15 years) specifying, among other things, the subject of the business and the conditions the undertaking must meet to enjoy the tax exemption.

The value of the benefit from the tax exemption is calculated as the product of the investment outlays (costs of investment or employment) constituting eligible expenditures, and the aid intensity for the region where the investment is carried out—ranging from 10% in the City of Warsaw to 50% in the provinces of Lublin, Podlasie, Podkarpacie, and Warmia–Masuria.

R&D centre

Payers of corporate income tax independently carrying out innovative activity may obtain the status of an R&D centre (CBR). Taxpayers eligible for CBR status include undertakings conducting research or experimental development and generating net revenue from the sale of goods and products and financial operations for the preceding financial year of at least:

- PLN 5,000,000, whose net revenue from sale of R&D services created by them (classified as research and development under the PKWiU codes) or industrial property rights constitutes at least 20% of their net revenue
- PLN 2,500,000 (but less than PLN 5,000,000), whose net revenue from sale of R&D services created by them (classified as research and development under the PKWiU codes) or industrial property rights constitutes at least 70% of their net revenue.

An R&D centre may create an innovation fund to cover R&D costs or costs connected with patenting inventions. Upon fulfilment of the statutory conditions, an R&D centre may recognise write-offs for the innovation fund as revenue-earning costs at the time the write-off is taken (up to 20% of the revenue in the given month), without waiting for expenditure of the money collected in the fund's account, which should be done by the end of the tax year.

R&D centres are entitled to a 150% deduction for eligible costs under R&D relief.

Moreover, under the rules for *de minimis* state aid, R&D centres may enjoy an exemption from real estate tax and the agricultural and forestry tax for taxable properties occupied for the purpose of research and development work conducted by them, in an amount of up to EUR 200,000 in a period of up to three years.

Costs of independently conducted development work

Taxpayers conducting independent experimental development work can time the recognition of deductible revenue-earning costs to match currently declared amounts of net income or tax losses.

The costs of such work, as a specific category of intangibles generated by the taxpayer, and regardless of the anticipated period of use, may be settled through amortisation deductions. In the case of development work completed with a positive result that can be exploited for the purpose of the taxpayer's business operations, and also if:

- The product or production technology is strictly defined and the costs of the work are reliably determined
- The technical usefulness of the product or technology is properly documented and on that basis the taxpayer decided to produce the products or apply the technology, and
- It appears from the documentation that the revenue from sale of the products or application of the technology will at least cover the costs of the development work,

the costs can be amortised, at the taxpayer's election, in their entirety within 12 months, starting from the month following the month in which they are entered in the books, or over any longer period.

If the experimental development work ends in a negative result (or a positive result not meeting all of the conditions outlined above), the expenditures may be applied directly to deductible revenue-earning costs in the month in which they were incurred, pro rata, beginning from the month they were incurred, in equal portions within a period no longer than 12 months, or in a one-time deduction in the tax year in which the work was completed. In light of the principle of equal treatment of taxpayers, these solutions should also be available with respect to experimental development work completed with a positive result and also meeting the conditions set forth above.

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50% revenue-earning costs for creative individuals

Payers of personal income tax who qualify as "creatives" may be entitled to claim 50% of their revenue as deductible revenue-earning costs, up to PLN 85,528 annually (instead of the standard costs of PLN 3,000), for the transfer of copyright or industrial property, grant of a licence (in the first year of the licence) or creation of a work or intellectual property. This privilege applies to revenue earned, among other things, from:

- Creative activity in the fields of architecture, interior design, landscape architecture, civil engineering, urban planning, literature, visual arts, industrial design, music, photography, audio and audiovisual works, computer programs, computer games, theatre, costume design, stage design, directing, choreography, violin-making, folk art, and journalism
- Audio and audiovisual production
- R&D, science, scholarship, research, and university instruction.

In the case of such "creatives" receiving income from remitters (e.g. employers), this allows them to increase their net pay without paying higher social insurance premiums.

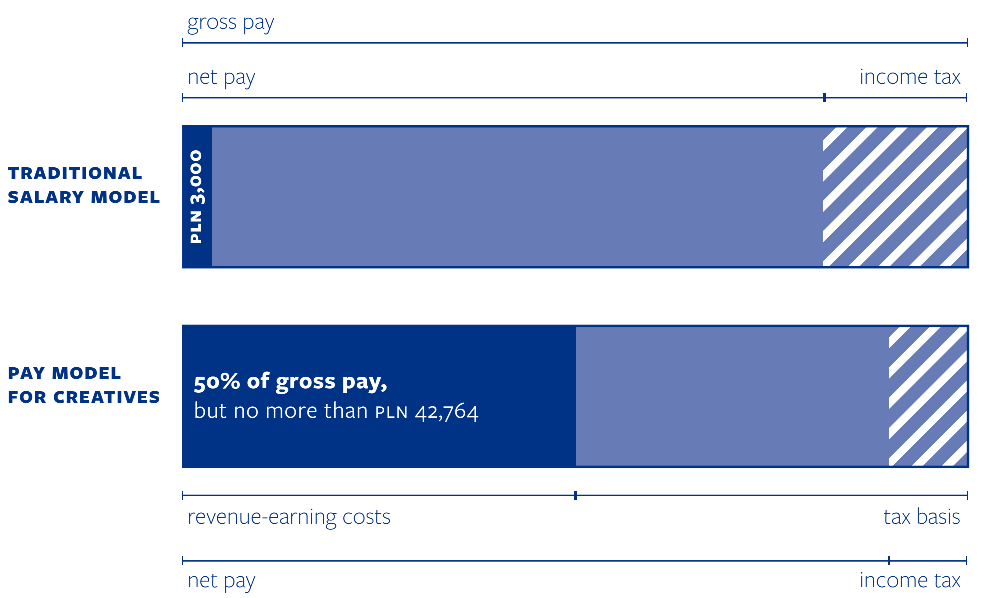
Relief for robotics and automation

From 2021, R&D relief is to be expanded to include relief for automation and robotics. This solution is designed for industrial enterprises interested in developing and implementing new integrated systems for supporting processes, products and business models. Solutions eligible for this relief should enable communication between humans and machinery and ensure the safety of users. ISO standard 8373:2012 is to serve as the basis for the definition of robots.

The additional eligible costs are to cover four categories, including purchase of brand-new robots and additional equipment they need to fulfil their functions, costs of intangibles necessary for proper startup and use of industrial robots (e.g. software), costs of training purchased in connection with industrial robots, and costs of finance leasing for acquisition of industrial robots.

Robotics costs are to be deducted during the tax year, and are to be the basis for taking an additional write-off in the annual tax return.

This new relief is intended to be a temporary solution in force for 2021–2025.



"Estonian CIT"

Apart from R&D activity, from 2021 some payers of corporate income tax will be eligible to defer paying income tax until they distribute profit, and apply a flat rate of taxation, under the so-called "Estonian CIT." Eligible taxpayers will be able to settle Estonian CIT in four-year periods, which can be extended for further four-year periods. At the 19% rate of PIT for dividends, the combined tax rate will be 25% or 20% for small taxpayers (compared to the previous 26.29%) and 30% or 25% for other taxpayers (previously 34.39%). When applying Estonian CIT, it will not be possible to claim tax relief and deductions such as R&D relief.

Estonian CIT is intended for SMEs that meet additional conditions, including:
– Their annual turnover (including VAT) does not exceed PLN 50 million.
– Their shareholders are solely natural persons (including non-residents).
– They employ at least three people on an annual basis (excluding shareholders).
– They do not hold shares in other companies.
– They invest in fixed assets (investments in intangibles will not be preferred), with required growth of a minimum 15% in a two-year period (no less than PLN 20,000) or 33% in a four-year period (no less than PLN 50,000).
– Less than 50% of their revenue derives from passive income (e.g. dividends, interest, and exercise of rights under financial instruments).
– They do not prepare financial statements in compliance with International Financial Reporting Standards in the instances referred to in Art. 45(1a)–(1b) of the Accounting Act.
– They do not generate income in special economic zones or the Polish Investment Zone.
– They were not created as a result of restructuring measures (such as merger or division).

Investment fund (account)

Also from 2021, taxpayers meeting the conditions for use of "Estonian CIT" will be able to claim write-offs on fixed assets to the investment account as revenue-earning costs (not through amortisation write-offs), which in an economic sense will enable faster settlement of the costs of fixed assets in investments conducted by taxpayers. But unlike Estonian CIT, use of this instrument will not deprive the taxpayer of the right to claim existing preferences, such as R&D relief.

Combining instruments

The tax instruments discussed above can be combined, including with non-tax forms of state aid. But typically it is impermissible for the same expenditures to be covered by two or more forms of support. For example, under R&D relief, eligible costs are not subject to settlement in the portion financed by a grant. Moreover, R&D relief is not taken into consideration in calculating the tax basis subject to the IP Box (thus if the taxpayer decided to apply the 5% income tax rate on income generated from qualified intellectual property rights, the taxpayer will not be able to deduct from that income additional eligible expenditures under R&D relief connected with work on such QIPRs). On the other hand, the IP Box may be applied to QIPRs developed through R&D activity using non-refundable state aid, e.g. under the Smart Growth Operational Programme. Units with the status of an R&D centre entitled to take a write-off to the R&D fund may recognise not 100%, but 150% of eligible expenditures under R&D relief.

With such a broad selection of tax relief and incentives, it is necessary to calculate how they will pay off, and analyse their impact on future growth.

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The digital economy, the EU, and competition

The EU project of regulating digital platforms and the broader digital economy will expand rapidly in 2021, particularly in the area of competition and consumer protection. To track this development, it would be worthwhile to capture a snapshot of the starting point as of the end of 2020.

What is the digital economy, and how is competition law dealing with it?

On 20 May 2019 the European Commission's Directorate-General for Competition published a report entitled "Competition policy for the digital era." The report is principally devoted to an attempt at describing the economy in the digital world, particularly the operation of digital markets. The authors discuss the aims that should be achieved on these markets by the European Union via competition law and policy. These aims serve as a framework for discussing the possibilities of applying principles of competition law to the operation of digital platforms and data-based markets. The report seeks to assess the EU's rules for merger control and identify necessary changes.

The report found the obvious: online platforms—search engines, social media, e-commerce sites—pose huge challenges for protection of the public interest and for public policy.

The experiences of digital markets show how hard it is to compete with large, established players occupying the digital market, not to mention dislodging them. The authors perceive a trend toward anticompetitive practices among the dominant digital firms.

THREE FUNDAMENTAL FEATURES OF THE DIGITAL ECONOMY
ACCORDING TO THE REPORT "COMPETITION POLICY FOR THE DIGITAL ERA"

1. **Extreme returns to scale** due to the much lower cost of production of digital services proportional to the number of customers served.
2. **Network externalities** because the convenience of using a technology or service increases with the number of users adopting it. A new entrant offering better quality and/or a lower price cannot benefit from the effect of scale unless it also convinces users of the incumbent to coordinate their migration to its own services, which can be difficult and time-consuming. Network effects thus prevent a superior platform from displacing an established incumbent.
3. **The role of data, which incumbents have gathered in large quantities along with the evolution of technology**. Data is not only one of the key ingredients of artificial intelligence, but also a crucial input to many online services, production processes, and logistics. Thus the ability to use data to develop new, innovative services and products is a competitive parameter whose relevance will continue to increase.

These characteristics create powerful "economies of scope," giving incumbents a strong competitive advantage.

What can be changed, and how?

All of these characteristics of digital platforms, ecosystems and the data-based economy heavily influence the shape of competition on markets of the digital economy. They require vigorous intervention under competition law, and changes in how competition law is applied. In this respect, the report from DG Competition is radical.

The authors conclude that even where consumer harm cannot be precisely measured, strategies employed by dominant platforms aimed at reducing the competitive pressure they face should be forbidden, in the absence of clearly documented consumer welfare gains.

The authors conclude that on digital markets, regulators should place less emphasis on analysis of market definition, and more emphasis on theories of harm and identification of anticompetitive strategies. Moreover, to disallow potentially anticompetitive conduct, it may be necessary to shift to incumbent firms a burden of proving the pro-competitiveness of their conduct. This applies particularly in the context of highly concentrated markets characterised by strong network effects and high barriers to entry.

THEORIES OF HARM

Constructions explaining why and how a given practice has a negative effect on competition or consumers

DATA AFTERMARKETS

Markets where data are an "input," "commodity" or "component" necessary to operate on those markets

The key conclusions from the report include the following:

– Decisions by the Commission, particularly in the cases of *Microsoft* (2004), *Google Shopping* (2017) and *Google Android* (2018), have raised awareness of the need to adjust analytical tools, methodologies, and **theories of harm** to better fit the new market reality. Such investigations take lots of time, and there is growing awareness of the need to process cases fast enough to keep up with market processes. Theories of harm must be designed with a view to both the costs of related errors and the practicality of applying the theories. The authors propose certain theories of harm that could be applied in practice. For the much-debated issue of acquisitions of startups by dominant platforms or ecosystems, they propose to strengthen and redesign conglomerate theories of harm. As regards data access, they argue that the **aftermarket** (lower-level market) doctrine needs to be re-examined to better reflect the new relevance of data-driven lock-ins.

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– With a view to dominant platforms, data interoperability can be a remedy against anticompetitive leveraging of market power into markets for complementary services. Where integration of platforms and the rise of powerful ecosystems raise concerns, requiring dominant players to ensure **data interoperability** may be an attractive and efficient alternative to breaking up firms—while continuing to allow consumers to benefit from the efficiencies of integration.
– In some areas, the authors propose that a regulatory regime may be needed in the longer run, particularly for implementation and oversight of interoperability mandates. Here, enforcement of competition law may not prove effective enough. At the same time, they recognise that the costs of a public-utility style of regulation, such as the lack of flexibility, may be too high for the digital economy. Instead, competition authorities can contribute to the better functioning of the digital economy by providing guidance, for example on the definition of dominance in the digital environment.

Another vital practical conclusion in the report is the recognition that competition agencies must gain a better understanding of the technologies underpinning the digital sector and the relevance of data for competition policy and enforcement. In particular, the authors believe that in the coming years regulatory agencies must develop internal technological capabilities, to help guide policies moving forward and help in their enforcement.

What follows from the report?

From the legal side, the most important conclusion is obviously the new approach to regulation of digital markets. In this context, work has been taken up in the European Commission to frame appropriate rules for digital platforms, including not only competition aspects but also a review of the e-Commerce Directive (2000/31 EC). Ursula von der Leyen, President of the European Commission, has undertaken to review the regulations governing the internal market for digital services, and the Commission announced this review in its communication entitled "Shaping Europe's digital future" (19 February 2020).

DATA INTEROPERABILITY

The ability for data to be used by various different platforms, systems or environments—recording and storing data in a manner allowing it to be transferred or used on another platform

***EX ANTE* CONTROL**

Preventive review, e.g. before launch of a service, system or platform

This review has resulted in a draft package of new legal frameworks under the working title of "Digital Services Act" (DSA, also currently the name of the draft of one of two regulations included in the package). The main subject of the package is:
– Harmonisation and heightened duties of online platforms and providers of information services, as well as stronger oversight of platform's content policies, through a revision of the e-Commerce Directive from 2000
– Establishing rules for ***ex ante* control** to ensure a level playing field for operating on markets where very large platforms act as information gatekeepers
– Establishing a mechanism for intervention to protect competition on the digital market in the specific instances identified by Margrethe Vestager, Executive Vice-President of the European Commission for A Europe Fit for the Digital Age and European Commissioner for Competition, at a conference at Fordham University on 8 October 2020.

The package currently includes two planned regulations: the Digital Services Act and the separate Digital Markets Act (DMA) developed pursuant to the concept of a "New Competition Tool." This tool would be a method for resolving structural problems involving competition on digital (and other) markets. The Commission published the DSA and DMA drafts on 15 December 2020. According to the proposal, the DSA would govern the duties of digital service providers intermediating in consumers' access to goods, services and content. The DMA, in turn, would supplement the competencies of competition authorities at the EU and national levels. We will track, discuss and report on further work on the package on the firm's "In Principle" portal.

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Online education and personal data

The hazards of COVID-19 have caused not only companies and their staff, but also schools, to shift to remote working. Numerous educational solutions have appeared on the market designed for use by children via internet. They are intended to help children gain knowledge and cheer them up when they are stuck at home. When offering services of this type to children, there are a few issues involving personal data that must be considered.

When delivering an educational programme to children via internet, it should be borne in mind that this will generally involve the processing of children's personal data—primarily data entered in registration forms when creating a user profile, but also data concerning the user's progress in working through the educational programme. Thus a range of duties under the General Data Protection Regulation will apply, in particular the duty to inform participants in an educational programme (such as a game) of the processing of their personal data, by providing them an appropriate information clause. Who bears these obligations will depend on the circumstances (who is the organiser, who has access to the data, and the purposes for which the data are used). For example, the data controller may be an external supplier or it may be the school.

Special protection for children under the GDPR

The GDPR gives children special protection, as they may be less aware of the risks and their rights in relation to the processing of personal data. The preamble recognises a special obligation to ensure the transparency of messages to children.

In practice this means that any communications concerning the processing of personal data, for example in a website's privacy policy, should be worded in a manner tailored to the age of the children for whom the content on that site is intended. It is also recommended to use diagrams, drawings or film clips to help children better understand the message. Practical guidelines in this area, broken down by age group, are found in *Age appropriate design: a code of practice for online services*, published by the Information Commissioner's Office in the UK. While

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Any information and communication where processing is addressed to a child should be in clear and plain language that the child can easily understand.

some of the provisions concern the British regulations, the guide also includes many universal recommendations that could be applied for example when drafting content for children in Poland.

When planning to offer an educational programme online in which children's data will be processed, a proper legal basis for processing the data must be identified. It will not always be necessary to obtain consent to processing of data. In some instances, another basis may be relevant, for example the processing is necessary for performance of a contract (Art. 6(1)(b) GDPR). When considering whether the processing is necessary for purposes of legitimate interests pursued by the data controller, under the requirements of Art. 6(1)(f) GDPR, the interests of the controller and of the data subject must be weighed carefully—in particular where the data subject is a child.

Information society services

Particular attention must be drawn to Art. 8 GDPR, which applies to the offer of information society services directly to children.

It follows from the definition of information society services that such a service must normally be provided for remuneration. But it is recognised that a service is provided for remuneration even when a fee is not paid directly by the user of the service, but for example for displaying advertising.

Whether a given service may be deemed to be offered directly to children will depend on the target group. In the case of educational solutions, it seems from their nature that for the most part they will be classified as offered directly to children.

INFORMATION SOCIETY SERVICE

Any service normally provided for remuneration, at a distance, by electronic means and at the individual request of a recipient of services (Art. 1(1)(b) of Directive (EU) 2015/1535)

Information society services include, for example, most services delivered online, e.g. social media platforms, web-based telephone services, online games, and educational sites

If an information society service is offered directly to children, Art. 8 GDPR firstly introduces a requirement that consent be given or authorised by the holder of parental responsibility over a child who is below age 16, and to verify such consent. It should be borne in mind, particularly if the services are also directed to children in other countries, that the GDPR allows member states to set a lower age for this purpose (but not below 13).

Significantly, the requirement under Art. 8 GDPR to obtain consent in the case of children below age 16 **applies only when personal data are processed on the basis of consent** (e.g. for marketing purposes). It thus does not apply when processing of the data is necessary for performance of a contract.

In practice this means that if the processing is necessary for performance of a contract (e.g. delivery of services in the form of access to an online educational programme), and thus the basis of the processing is Art. 6(1)(b) GDPR, Art. 8 will not apply insofar as the purpose of the processing is to perform that service. Art. 8 will step in when the provider of the educational programme seeks to use children's data for purposes other than using the service, for example also for the purpose of delivering marketing content to the children.

Establishing the user's age

The GDPR does not expressly impose a duty on the data controller to verify the user's age. However, if the controller does not do so, it exposes itself to the charge of processing personal data in violation of law. Thus verification of age seems essential.

As the EU's Article 29 Working Party stated in its guidelines (WP 259), if the users state that they are of the age authorising them to express digital consent, then the controller can carry out appropriate checks to verify that this statement is true. Such checks can be limited to reasonable efforts, proportionate to the nature and risks of the processing activities.

Processing of children's data in the education sector should meet appropriate standards of quality and the rule of law, and data protection by design and by default.

However, "If the user states that he/she is below the age of digital consent then the controller can accept this statement without further checks, but will need to go on to obtain parental authorisation and verify that the person providing that consent is a holder of parental responsibility." This means it will also be necessary to obtain personal data of the parent or guardian. The GDPR requires the data controller to "make reasonable efforts to verify in such cases that consent is given or authorised by the holder of parental responsibility over the child."

The issue of the age of users of an educational programme is also relevant when the basis for processing of the user's personal data is a contract. In that case, the rules for conclusion of contracts with a person lacking full legal capacity must also be borne in mind.

Verification of the user's age, and the related potential need to process personal data of the user's parent or guardian, is thus essential. But age verification itself should not lead to excessive data processing.

What else to bear in mind?

Guidance on processing of children's personal data in the education sector (including guidance aimed at the sector itself) may be found in *Children's Data Protection in an Education Setting: Guidelines*, adopted by the Consultative Committee of the Convention for the Protection of Individuals with Regard to Automatic Processing of Personal Data, under the auspices of the Council of Europe. As stated in the guidelines, "Since children merit special protection, the expected standards for the processing of children's data in the education sector should set a high bar by design, to meet appropriate standards of quality and the rule of law, and data protection by design and by default."

In the case of offering educational programmes via internet, in addition to data protection regulations the Electronic Services Act of 18 July 2002 will also apply. That act imposes on providers of educational programmes a duty to publish on their websites terms and conditions for delivery of services by electronic means.

If the educational programme is also intended for children below age 13, lacking legal capacity, the terms and conditions must also contain provisions on the possibility to use the game or programmes under the supervision of a parent or guardian.

THE TERMS AND CONDITIONS MUST SPECIFY, IN PARTICULAR:

- Types and scope of services delivered by electronic means
- Conditions for performance of the services, including the technical specifications essential for interoperability with the IT system used by the service provider
- Prohibition on uploading of unlawful content by the service recipient
- Conditions for conclusion and termination of contracts for delivery of services by electronic means
- Complaint procedure.

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Operating a virtual art gallery: How to prepare?

The crisis has not scared off investors, and interest in acquiring artworks is growing. But due to the pandemic, auctions have moved online, continuing a trend that began a decade ago.

Can intermediaries in art trading operate exclusively on the internet?

During the pandemic many cultural institutions made their resources accessible online and invited visitors to take virtual tours. An initiative by Google Arts & Culture brought together over 2,000 cultural institutions (including museums and art galleries) from all over the world, facilitating virtual familiarity with works from their collections. Nothing will ever take the place of direct contact with art, but we will increasingly use new technologies to admire collections located in far-flung corners of the globe.

The situation is similar with trading in artworks. Collectors usually wish to see a painting or sculpture before buying it, and often wish to obtain additional confirmation of the work's authenticity. Nonetheless, the internet is making bold inroads on this market. Auction houses have been particularly keen to take advantage of this avenue to increase their turnover. This raises the question of whether it is possible for art dealers to function exclusively online.

The answer appears to be "yes," as the law secures the fundamental requirement in transactions of this type, that is, the guarantee that the buyer will acquire the painting or other work in a state corresponding to the description and photos of the work. But when planning to launch a virtual gallery, there are several other equally important issues to bear in mind.

The issues we have selected to discuss do not exhaust the topic, but should help introduce this model for trading in artworks, which has yet to be clearly recognised from the legal perspective.

A DECADE OF ONLINE ART AUCTIONS (2011–2020)

December 2011: CHRISTIE'S

- First exclusively online auction (Elizabeth Taylor's jewellery collection)

April 2020: SOTHEBY'S

- Record sales for an online auction (over USD 6.4 million)
- Highest price obtained for a single painting in an online auction (USD 1.3 million for *Antipodal Reunion* by the American artist George Condo, sold to an anonymous buyer)

Reports issued in late 2020 by the three largest auction houses—Sotheby's, Christie's and Phillips—show that virtual auctions have generated not only an increase in the number of transactions, but an increase in prices compared to the period prior to the pandemic.

Acquiring artworks "on approval"

When operating an online art gallery, it is possible to offer via the internet only works which the gallery owner has previously acquired in the traditional manner. Under that model, the dealer first carefully examines the original, to estimate the artistic merit and market value of the work, and then decides to acquire the work or accept it on commission. The business decision to enter into the transaction is then made after personally seeing the object, typically still in the artist's possession.

But can galleries safely acquire works at a distance? That would greatly facilitate the acquisition of works regardless where the artists live and work. In this respect, it is worth considering the notion of sale on approval. The transaction with the artist offering the work can be concluded under a suspensory condition that the buyer (the art gallery) finds the work to meet its expectations. The next stage of the transaction is to send the physical work to the gallery for its verification. If after seeing the work the gallery ultimately decides it does not like the work, or for example has doubts as to its authenticity, the gallery can withdraw from the transaction and not go through with the purchase.

The terms and conditions of the virtual gallery should present upfront the fundamental provisions of the contract to be concluded between the artist and the gallery, specifying the form of conclusion of the contract, the party covering the shipment costs and insurance, and the date by which the gallery must confirm whether it accepts the delivered work. To encourage artists to cooperate with the gallery and send in their work, payment of the price may be divided into two or more instalments, or an advance could be provided for the artist so that the work is delivered after the artist receives part of the price.

Acquisition of copyright to works vs "statutory licence"

The purchase of an artwork does not automatically cause the economic copyright to pass to the gallery. Nonetheless, "exhaustion" of the right occurs with respect to an item sold to a gallery. This means that along with transfer of ownership, for example of a painting to a gallery, the author of the work is deprived of the possibility of controlling the further trade in that specific item. However, the gallery does not obtain the right to unfettered exploitation of the acquired work. The rightholder (typically the artist, if the artist has not transferred the copyright to the gallery or other entity) retains, among other things, rights to allow public screening or exhibition and making the work publicly accessible in such a manner that anyone can access the work at a time and place of their choosing (Art. 50(3) of the Polish Copyright Act). Exploitation of a work in any of these ways without the permission of the holder of the economic copyright will constitute an infringement of those rights. But we can hardly imagine the functioning of a virtual gallery without being able to publicise the works via internet. The solution is to address copyright issues in the contract or to base the gallery's operations on one of the instances of permitted use provided for in the Copyright Act.

Permitted use

The Copyright Act introduces two exceptions for art dealers which should be borne in mind. On this basis, galleries can exploit works without the need to request the consent of the holder of the economic copyright, but only in a limited scope, which boils down to:

– Exhibition of an example of a visual artwork or a copy (Copyright Act Art. 32), or
– Use of a work for the purpose of advertising a public exhibition or public sale (Art. 33^3).

The second of these exceptions may be particularly relevant for virtual art galleries, as it does not refer to the notion of a physical example of the work and does not require that the activity be undertaken for non-profit purposes. Under this provision, it is permissible to exploit works for the purpose of their public sale, to the extent justified for promotion of the sale, excluding other commercial exploitation. According to the stated justification for the amendment that introduced that exception, it applies to instances of sale of works

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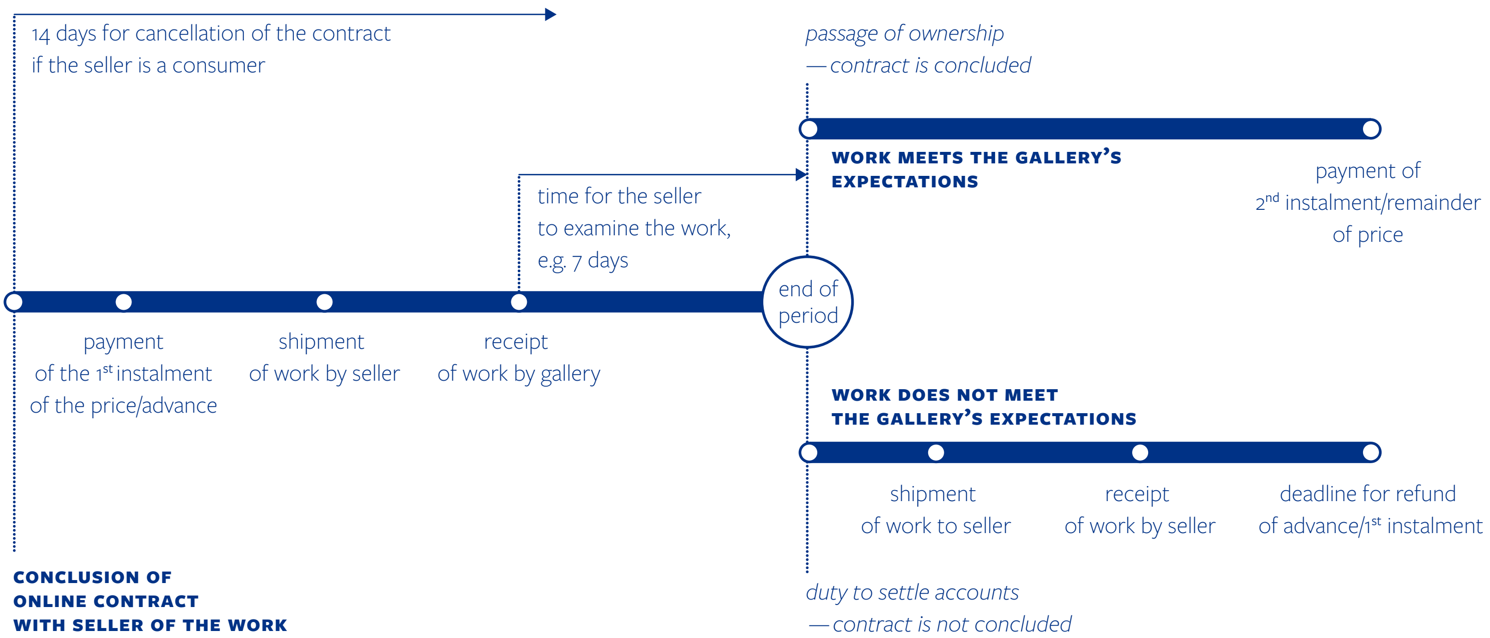

protected by copyright via the internet. The point is also to allow promotion of public exhibitions and online promotion of an exhibition featuring items that have not previously been made available to the public in any way with the permission of the author.

But returning to virtual galleries, some doubts are raised by the parliament's use of the phrase "sale of a work," when it is obvious that it is examples of the work that will be sold, not the "work" itself, which has no material form. Nonetheless, it seems that the new provision of the act should be interpreted functionally. The point is that galleries should be able to prepare offers and include in them photos of artworks displayed for sale online.

After completion of the sale transaction, such photos should be taken down from the gallery's website. It should also be remembered that the scope of statutory permission is limited exclusively to exploitation of a work to the extent justified by promotion of the sale, which should be distinguished from the operations of the gallery itself. It is thus not permitted to use images of artworks for the purpose of promoting the gallery. If the gallery wishes to show artworks in whose sale it has intermediated, for example in ad clips or other marketing materials, it must request consent from the artist (if the artist still retains the copyright) for this form of exploitation of the work.

Or perhaps a contract?

Regulating issues related to the copyright to an artwork in a contract with the rightholder appears to be a solution providing the gallery much greater leeway in its actions and certainty as to the consent granted for exploitation of the work. The contract may take the form of a licence (exclusive or non-exclusive) or provide for transfer to the gallery of the economic copyright to the work. In that case, the issue arises of complying with the written form required by law for transfer of copyright or grant of an exclusive licence. Here modern tech solutions enabling the use of electronic signatures may come in handy, if both parties to the transaction (particularly the rightholder) are prepared for this option. It should also be borne in mind that not all electronic signature services offered on the market meet the standards established by Polish law, and use of an inadequate device may result in invalidity of the contract.

Droit de suite—additional royalties for the artist

When operating an art gallery, it should be borne in mind that artists and their heirs, regardless of whether they still hold the economic copyright to their works, are entitled to an additional royalty on resale of an original example of a work of art, known by the French term *droit de suite*. This right is regulated in Copyright Act Art. 19–19[5] and applies to all works of art subject to copyright protection, as to which the economic copyright has not yet expired.

The author of a work is entitled to an appropriate percentage royalty in the case of each subsequent resale of a work following the initial disposal of the work by the artist, if the seller is an entity professionally involved in trading on the art market. Polish law imposes an obligation to pay this royalty on all professional transactions for the equivalent of EUR 100 or more. This threshold has been set quite low, also in comparison with the rules applicable in other EU member states. For example, in France the minimum value for transactions subject to *droit de suite* is EUR 750, and in Italy EUR 3,000. In the case of trading in works by foreign artists, as a rule the Polish regulations will apply. But this does not apply to a situation where the artist is from a country whose law does not provide for payment of *droit de suite* royalties, unless at the time of resale the artist is residing in Poland.

A virtual art gallery must be prepared to administer the duties imposed on the gallery by *droit de suite*, also in light of the general six-year limitations period on claims for payment of these additional royalties. The author also has an informational claim to require the seller to provide the details of completed transactions. The gallery must therefore maintain all essential data regarding transactions for at least the past three years.

Consumer law

The purchase and sale of artworks by a virtual gallery is also subject to the consumer law regime. One of the fundamental rights of a consumer is to withdraw from a contract made at a distance. And most likely such a right can also be exercised from 1 January 2021 by customers who are individual business operators, if their purchase of an artwork is not directly connected with the subject of their business (the effective date of the amending act of 31 July 2019 to this effect was already postponed once due to the pandemic).

It also cannot be ruled out that an artist supplying a work to a gallery will be treated like a consumer. But in the overwhelming number of instances, the artist concludes a contract transferring ownership to an artwork in connection with professional activity pursued by the artist (but the same cannot be said of collectors who sell part of their collection to a gallery). Consumer law can also sometimes protect an artist in the event of conclusion of a contract governing issues of the transfer of copyright, when the transaction is conducted at a distance.

No doubt the traditional art market, for which handling the physical specimen of the work and personal contact with the dealer and the artist are an essential feature, will continue to work its undeniable charm for a long time to come. Nonetheless, the new virtual reality has already made its presence known and is perceived by some as an improvement on the traditional market, and as the future of the art market as a whole.

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Simpler procedure for changes in corporate form

From 1 March 2020, when the 19 July 2019 amendment to the Commercial Companies Code entered into force, the procedure for transformation of the corporate form of companies and partnerships has been simplified.

The new regulations introduced a number of simplifications for businesses. But some changes, connected with introduction of a "corporate right of exit," may raise concern among minority shareholders.

Simplification of minimal content of transformation plan

The contents of a corporate transformation plan were greatly simplified from 1 March 2020. First and foremost, Art. 558 §1(2) of the Commercial Companies Code was amended. The duty provided there to specify in the transformation plan the value of the shareholders' shares according to the financial report prepared for purposes of the transformation was replaced by a requirement to specify the fair market value of the shares.

The new obligation will apply only in the case of transformation of a company into a partnership. Under the law in force through 29 February 2020, the requirement to specify the value of the shareholders' shares in accordance with the financial report prepared for purposes of the transformation applied to all types of transformations.

These changes mean that in practice, in the case of transformation of partnerships into companies, one type of company into another type of company, or one type of partnership into another type of partnership, it will not be necessary at all to specify the value of the shareholders' shares.

The list of mandatory enclosures to the transformation plan also changed. Under the law in force through 29 February 2020, one of the enclosures that had to be annexed to the plan was a valuation of the assets and liabilities of the company or partnership undergoing transformation. From 1 March 2020, such a valuation must be prepared only in the case of transformation into a joint-stock company. Thus, in practice, in the case of transformation into any other corporate form, no valuation of the assets of the company or partnership undergoing transformation must be enclosed with the transformation plan.

KEY CHANGES INTRODUCED BY LAST YEAR'S AMENDMENT CONCERN:

- content of transformation plan
- audit of transformation plan
- adoption of transformation resolution
- corporate right of exit

Elimination of the duty to audit the transformation plan

Under prior law, the plan for transformation of any company or partnership was examined by an auditor for correctness and reliability. The application to appoint an auditor was filed with the registry court. Thus the need for the registry court to act arose at the very beginning of the transformation process, during the management phase.

Now the transformation plan must be audited only in the case of transformation into a joint-stock company. This means that except in the case of transformation into a joint-stock company, the registry court will become involved only at the stage of consideration of the application to register the transformation.

This change expedites the process and reduces the related costs. In the case of transformations other than into a joint-stock company, it is no longer necessary to incur the costs of hiring an auditor.

Change in certain provisions on adoption of transformation resolution

In connection with doubts arising in practice on the manner of calculation of the periods for the two mandatory notices to shareholders of the intention to adopt a transformation resolution, the parliament amended Art. 560 §1 of the code. From 1 March 2020, this provision clearly states that the first notice must be made no later than one month prior to the planned date of adoption of the transformation resolution, and the second notice no earlier than two weeks after the first notice.

Lawmakers also eliminated the doubt, often raised among practitioners, whether a transformation requires, as a separate action, conclusion of articles of association or signing of the statute of the transformed company or partnership. By rewording Art. 563 §2 and repealing Art. 556 §4, it was clarified that adoption of a transformation resolution takes the place of conclusion of the articles of association of the transformed company or partnership, or founding of the transformed joint-stock company, as well as appointment of the bodies of the transformed company or partnership.

Introduction of the "corporate right of exit"

Through 29 February 2020, as part of the transformation procedure, all the owners had to file a written statement on their participation in the transformed company or partnership. A shareholder or partner who failed to submit such a statement did not participate in the transformed company or partnership. Instead, that person was entitled to a claim for payment of an amount corresponding to the balance-sheet value of his shares in the company or partnership undergoing transformation, in accordance with the financial report prepared for purposes of the transformation.

The provisions that were the basis for this procedure (Art. 564–566 of the Commercial Companies Code) were repealed as of 1 March 2020. However, on that date Art. 576^1 entered into force, introducing a new legal institution designed to protect the interests of owners who do not agree to participate in the reorganised entity. The justification for the amending act (Sejm print no. 3236, p. 80) described this as a "corporate right of exit."

Under the new regulations, the existing owners are not entitled or required to file a statement on participation in the transformed entity. Participation in the transformed company by the shareholders of the company undergoing transformation is the rule.

Meanwhile, the corporate right of exit is applicable only in the case of transformation of a company into a partnership. In all other transformations, the existing owners cannot fail to participate in the entity in its changed legal form, if a transformation resolution has been passed.

A shareholder of a company intending to exercise the procedure for the corporate right of exit must object to the resolution, demand that the objection be recorded in the minutes, and then submit to the entity a written demand for repurchase. This demand must be submitted to the company within one week after adoption of the resolution on transformation. When a joint-stock company is to be transformed, the share document must be enclosed with the repurchase demand, or information from the share ledger, or

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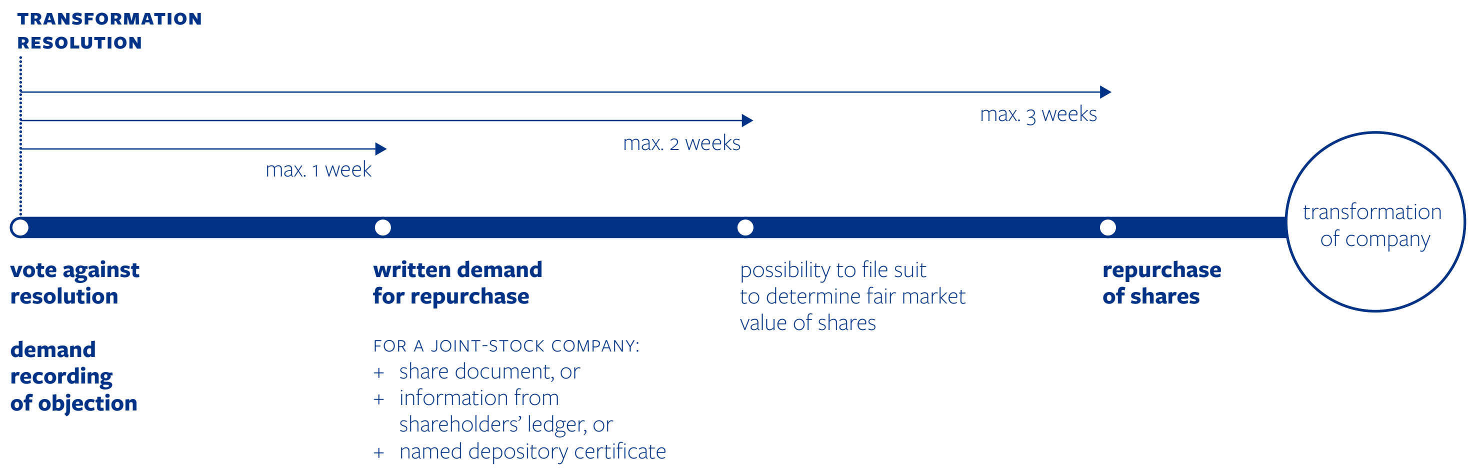
MECHANISM OF THE CORPORATE RIGHT OF EXIT
applies to transformation from a company into a partnership



in the case of dematerialisation of shares subject to organised trading, a named depository certificate issued in accordance with the regulations on trading in financial instruments.

Within three weeks from adoption of the transformation resolution, the company undergoing transformation shall repurchase the shares for the company's own account or the account of the shareholders remaining in the company. The repurchase price should correspond to the fair market value of the shares in the transformed company.

The effectiveness of the repurchase depends on payment of the repurchase price to the shareholders demanding repurchase, or submission of an amount equal to this price into a judicial deposit. Under Art. 576^1 §8 of the code, the repurchase must be carried out for the transformation to be effective.

Art. 576^1 §7 of the Commercial Companies Code provides for an institution protecting the interests of a shareholder who has carried out the actions specified above (i.e. voted against the transformation resolution, demanded recording of the objection in the minutes, and made a written demand for repurchase) and does not agree with the repurchase price. Such a shareholder may file a claim for determination of the fair market value of his shares. The deadline for filing the claim is tight, at only two weeks from adoption of the transformation resolution.

However, filing of this claim does not block the repurchase or registration of the transformation. The transformation may be carried out if the company has repurchased all of the shares of shareholders demanding repurchase within the time specified in the Commercial Companies Code. If the shareholder's claim is later upheld by the court, the partnership will be required to make up to the former shareholder any difference in the repurchase price (J. Bieniak, M. Bieniak & G. Nita-Jagielski, *Commercial Companies Code: Commentary* (7^{th} ed., Warsaw: Legalis, 2020), Art. 576(1)).

This procedure has already been criticised in the legal literature. It is charged that the new regulations lack solutions effectively protecting minority shareholders against arbitrary establishment of the fair market value of their shares, repurchase at an understated price, and possibly many years of litigation. Doubts have also been raised as to the constitutionality of the new solution (e.g. in the commentary to the Commercial Companies Code cited above).

Summary

From March 2020, it may indeed be cheaper and faster to carry out the transformation of the legal form of a Polish company or partnership. The transformation plan has been simplified and does not necessarily have to be audited, which translates into real savings. Doubts have been eliminated as to the periods involved and the need to separately conclude articles of association within the transformation procedure. A corporate right of exit has also been introduced. Under this mechanism, shareholders who do not agree to participate in the transformed entity may now demand repurchase of their shares in certain instances (transformation of a company into a partnership). This mechanism may generate controversy, particularly when it comes to setting the fair market value of the shares of the company undergoing transformation.

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The end of paper shares

From 1 March 2021 no shares of stock can take the form of a document. Joint-stock companies and joint-stock limited partnerships that issued shares of stock before that date in documentary form have been required to summon the shareholders to surrender the share documents to the company (also including public companies, if such shares were issued in the past) for the purpose of dematerialisation, i.e. entry into the ledger of shareholders. Mandatory dematerialisation also applies to subscription warrants, redemption certificates, promoter certificates, and other titles for participation in a company's profit or distribution of a company's assets.

Summons to shareholders to submit share documents

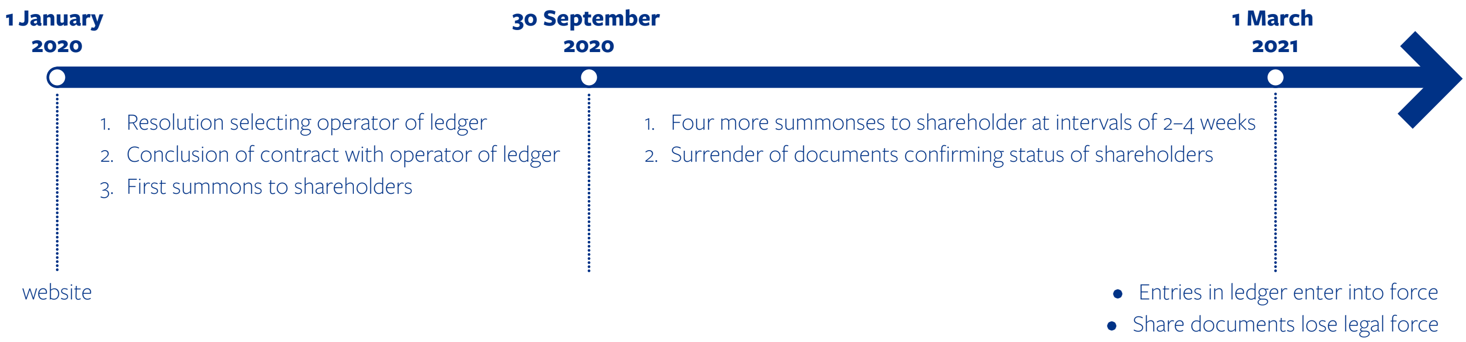
To fulfil this obligation, companies were required on or before 30 September 2020:

- By resolution of the general meeting, to select the entity with which to conclude a contract for operation of the share ledger
- To conclude the share ledger operation contract with the selected entity, and
- To issue the first summons to shareholders to surrender their share documents.

The subsequent summonses (five in total) were to be issued in intervals no shorter than two weeks and no longer than one month. The summonses were to be sent to shareholders, and information on the summonses must be posted on the company's website for at least three years from the date of the first summons. It should be added that from 1 January 2020, every joint-stock company and joint-stock limited partnership in Poland has been required to have a website. Information concerning the website should be filed by the company with the National Court Register (KRS).

On 1 March 2021 share documents will lose force and entries in the ledger will gain force. Shares in document form will retain only evidentiary value, to demonstrate the right to vote or receive dividends. If a shareholder does not surrender share documents by that time to the company, then by 1 January 2026 the shareholder may present the share document and thus demonstrate the right to be entered in the ledger as a shareholder.

KEY DATES



We advise companies that if not all share documents are surrendered by shareholders despite the company's compliance with the duty to summon the shareholders to do so, the company should then post information on its website concerning the final deadline for surrendering the documents and the consequences of the shareholders' failure to do so. And there is no legal barrier to sending an additional summons to any noncomplying shareholders known to the company.

What to do with share documents

The company should store the share documents received from shareholders for evidentiary purposes. The company should confirm receipt of the share documents from the shareholders with a written protocol (one copy for the shareholder and one copy for the company).

Ledger

The ledger is open to the shareholders and the company. They have the right to demand issuance of information from the ledger in electronic or paper form. Depending on the terms of the contract between the company and the entity operating the ledger, fees may be charged for some actions for shareholders.

A ledger certificate in the shareholder's name, issued by the operator of the ledger, is an important document, confirming the right to vote the shares. The shares indicated in the ledger certificate cannot be disposed of from the date of issuance of the certificate until the stated end of the certificate's validity or surrender of the certificate to the ledger operator before that date. During the period indicated in the certificate, the shares are blocked in the ledger.

The entity operating the ledger will make all entries at the request of the company or a person with a legal interest, i.e. shareholders, heirs, acquirers of the shares, pledgees, usufructuaries entitled to exercise voting rights, and enforcement authorities. The operator of the ledger will examine the content of the documents justifying making an entry in the register. It has no legal duty to examine the accuracy or lawfulness of such documents, but it may do so at its own initiative. The applicants are responsible for the correctness of the documents.

Effect of acquisition of shares

An important change is conditioning the effectiveness of transfer or encumbrance of shares on entry of the acquirer in the ledger. Acquisition of the shares or establishment of liens on shares occurs as of the time an entry is made in the ledger indicating the acquirer (or pledgee or usufructuary, as the case may be) as well as the quantity, type, series, and serial number of the shares in question.

Because the operator of the ledger has one week from receipt of an application to make the entry, there is a separation in time between the parties' signing of

We advise companies that if not all share documents are surrendered by shareholders, the company should then post information on its website concerning the final deadline for surrendering the documents and the consequences of the shareholders' failure to do so.

the sale contract and actual acquisition of ownership of the shares. Transfer of ownership of shares must be documented so that it can serve as a valid basis for entry in the ledger. The shareholder will not be the party who acquired the shares in accordance with the contract, but the person who is entered in the ledger. There are exceptions for:

– Acquisition of shares in an issue of shares, when the entry in the ledger of shareholders occurs upon entry of the issue in the National Court Register
– Passage of ownership of the shares by operation of law.

Pledge on shares

The procedure and conditions for entry of shares in the ledger, and the statutory conditioning of the effectiveness of encumbrance of shares on entry in the ledger, as described above, will also cause a significant practical consequence in the case of registered pledges. Under the Act on Registered Pledges and the Pledge Register, establishment of a registered pledge requires entry in the pledge register, which means that to date, the time of establishment of a pledge has been decided by the entry in the court's pledge register. But under the amended provisions of the Commercial Companies Code, encumbrance of shares, and thus also establishment of a registered pledge, will be effective upon entry in the share ledger. There is no provision addressing this inconsistency, and thus from 1 March 2021 there will be two legal regimes differently setting the moment when a registered pledge on shares of stock arises.

In practice it may be anticipated that entities operating share ledgers will not wish to disclose a registered pledge of shares before the pledge is entered in the pledge register, and will require proof of entry of the pledge in the pledge register. But this will still generate doubts whether shares were encumbered by the pledge from the time the pledge was entered in the pledge register or from the time the pledge was disclosed in the ledger of shareholders. Even if the entity operating the shareholder ledger quickly processes applications for disclosure of a registered pledge on shares following entry in the judicial pledge register, the parties to the transaction and the company will be left in a temporary state of uncertainty as to the status of the shares in question. Doubts concerning the effectiveness of establishment of a pledge following entry in the pledge register will also create room for attacking the effectiveness of encumbrance of shares during this interim period.

The inconsistency in these regulations could also lead to an attempt to rebut the presumption of the existence of a registered pledge due to entry in the pledge register, if the pledge has not yet been disclosed in the ledger of shareholders. This raises the question whether, in this situation, the presumption provided for in the Act on Registered Pledges and the Pledge Register will protect persons relying on entries in the judicial pledge register. Therefore, it is recommended to notify the operator of the share ledger of the planned establishment of the pledge and submission of the entry to the pledge register, and to agree on the procedure to be followed so that the entry in the ledger of shareholders is made immediately after entry in the pledge register.

Opinions are also being expressed on the market asserting the primacy of the Act on Registered Pledges and the Pledge Register over the new provisions of the Commercial Companies Code, thus upholding the constitutive nature of the entry of the pledge in the pledge register. Under this interpretation, a registered pledge will still arise upon entry in the pledge register, and entry in the ledger of shareholders will have no impact on the validity of the registered pledge.

About Wardyński & Partners

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We advise private clients, startups, clients from the construction industry, energy and energy-intensive industry, retail and distribution, maritime economy, rail and aviation, media and advertising, healthcare, manufacturing, agriculture, sport, transport and logistics, defence, food, pharma and FMCG.

We share our knowledge and experience through our portal for lawyers and businesspeople (www.inprinciple.pl), the firm *Yearbook*, the new tech law blog (www.newtech.law), the labour and employment law blog (HRlaw.pl), commentary to the new Public Procurement Law (komentarzpzp.pl — only in Polish) and numerous other publications and reports.

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