



THE WORLD BANK

Report on the Observance of Standards and Codes (ROSC)

Corporate Governance

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Corporate Governance Country Assessment

Poland

June 2005

Overview of the Corporate Governance ROSC Program

WHAT IS CORPORATE GOVERNANCE?

Corporate governance refers to the structures and processes for the direction and control of companies. Corporate governance concerns the relationships among the management, Board of Directors, controlling shareholders, minority shareholders and other stakeholders. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies and increasing their access to outside capital.

The *OECD Principles of Corporate Governance* provide the framework for the work of the World Bank Group in this area, identifying the key practical issues: the rights and equitable treatment of shareholders and other financial stakeholders, the role of non-financial stakeholders, disclosure and transparency, and the responsibilities of the Board of Directors.

WHY IS CORPORATE GOVERNANCE IMPORTANT?

For emerging market countries, improving corporate governance can serve a number of important public policy objectives. Good corporate governance reduces emerging market vulnerability to financial crises, reinforces property rights, reduces transaction costs and the cost of capital, and leads to capital market development. Weak corporate governance frameworks reduce investor confidence, and can discourage outside investment. Also, as pension funds continue to invest more in equity markets, good corporate governance is crucial for preserving retirement savings. Over the past several years, the importance of corporate governance has been highlighted by an increasing body of academic research.

Studies have shown that good corporate governance practices have led to significant increases in economic value added (EVA) of firms, higher productivity, and lower risk of systemic financial failures for countries.

THE CORPORATE GOVERNANCE ROSC ASSESSMENTS

Corporate governance has been adopted as one of twelve core best-practice standards by the international financial community. The World Bank is the assessor for the application of the OECD Principles of Corporate Governance. Its assessments are part of the World Bank and International Monetary Fund (IMF) program on Reports on the Observance of Standards and Codes (ROSC).

The goal of the ROSC initiative is to identify weaknesses that may contribute to a country's economic and financial vulnerability. Each Corporate Governance ROSC assessment reviews the legal and regulatory framework, as well as practices and compliance of listed firms, and assesses the framework relative to an internationally accepted benchmark.

- Corporate governance frameworks are benchmarked against the OECD Principles of Corporate Governance.
- Country participation in the assessment process, and the publication of the final report, are voluntary.
- The assessments focus on the corporate governance of companies listed on stock exchanges. At the request of policymakers, the ROSCs can also include special policy focuses on specific sectors (for example, banks, other financial institutions, or state-owned enterprises).
- The assessments are standardized and systematic, and include policy recommendations. In response, many countries have initiated legal, regulatory and institutional corporate governance reforms.
- Assessments can be updated to measure progress over time.

By the end of June 2005, 48 assessments had been completed in 40 countries around the world.

REPORT ON THE OBSERVANCE OF STANDARDS AND CODES (ROSC)

Corporate governance country assessment

Poland

June 2005

Executive Summary

This report assesses Poland's corporate governance policy framework, and its enforcement and compliance practices. It highlights recent improvements in corporate governance regulation, makes policy recommendations, and provides investors with a benchmark against which to measure corporate governance in Poland. The report updates the corporate governance ROSC carried out in 2001.

Poland is at an advanced stage of corporate governance debate, discussion, and reform. Since the previous assessment, Poland has adopted new legislation, effectively promulgated a corporate governance code, and continued to develop strong regulatory and enforcement institutions. These improvements have resulted in a corporate governance framework that complies with many of the OECD Principles. The basic minority rights and disclosure framework are in place. Several issues drive the requirements for future reform, including the growing power of pension funds, which are rapidly becoming significant holders of Polish shares.

The report identifies several potential problems and remedies, including:

- insufficient regulation of the corporate governance activities of the pension funds;
- weakness of the supervisory board;
- problems in the delisting / squeeze-out process; and
- insufficient approvals of related party transactions.

Policy recommendations are based on Poland's competition with increasingly sophisticated markets in OECD countries, and the need for corporate governance policy to rise above basic minimum standards.

At the request of the authorities, this report also includes two detailed analyses of special policy topics: Annex 1 is an analysis of the Warsaw Stock Exchange Best Practices Code and options for compliance, and Annex 2 is an assessment of the corporate governance issues of state owned enterprises.

Acknowledgements

This assessment of corporate governance in Poland was drafted by Alexander Berg of the Corporate Governance Department of the World Bank as part of the Reports on Observance of Standards and Codes Program, with support from Susan Rutledge (Regional Corporate Governance Coordinator, Europe and Central Asia Region, World Bank) and Richard Symonds (Legal Vice Presidency, World Bank). The ROSC was based on a corporate governance template-questionnaire completed by the Polish Institute of Directors. Richard Symonds prepared the Note on the Enforcement of the Warsaw Stock Exchange Code (Annex 1) and Agata Waclawik-Wejman (Legal Vice Presidency, World Bank) prepared the Note on Corporate Governance of State-Owned Enterprises in Poland (Annex 2). The due diligence mission was carried out in November 2004. Additional information was supplied by the Polish authorities in October 2005. The report was also presented at a seminar organized by the Polish Institute of Directors, the Warsaw Stock Exchange and the World Bank in December 2005.

Agata Waclawik-Wejman, Frederic Gielen, Roger Grawe, Fernando Montes-Negret, Tatiana Nenova, and David Robinett of the World Bank provided advice and comments.

The assessment reflects technical discussions with the Polish Securities and Exchange Commission, the Warsaw Stock Exchange, the National Depository for Securities, commercial banks, issuers, and numerous market participants. The Polish Chamber of Pension Funds (IGTE) also provided written comments.

The team also recognizes the late Dr. Krzysztof A. Lis for his important contributions to this report and to the improvement of corporate governance practices in Poland.

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Country assessment: POLAND

This ROSC assessment of corporate governance in Poland benchmarks law and practice against the OECD Principles of Corporate Governance, and focuses on listed companies.

*General adoption of
acquis, and
convergence with
continental European
corporate governance
norms*

Poland is at an advanced stage of corporate governance debate, discussion, and reform. Several key features distinguish Poland's corporate governance framework.

- Poland has largely adopted the *acquis communautaire*, and has worked to modernize its company and securities laws to meet EU standards. Implementation remains a concern. Ownership concentration, securities market regulation, levels of foreign investment, and general patterns of corporate organization are moving towards continental European norms.
- Despite the legacy of privatization, the State has continued to play a major role in corporate governance.
- The new and growing forces in Polish corporate governance are the mandatory pension funds, which hold 10 percent of market capitalization.
- A series of corporate governance scandals increased awareness of the importance of minority shareholder rights. Several organizations have developed corporate governance codes, including the Warsaw Stock Exchange, the Gdansk Institute of Market Economics, and the Private Equity Association (forthcoming). Many organizations actively participate in the debate on corporate governance, including the Polish Institute of Directors, the Association of Issuers and the Association of Investment Funds.
- Regulatory oversight is stronger than in many transition and emerging markets. The Polish Securities Commission (PSEC) and the Warsaw Stock Exchange (WSE) have taken leadership roles in promoting minority protection and corporate governance reform.

*Strong legacy of state
ownership*

*Rapidly growing
pension funds will play
major role*

*High awareness of
corporate governance*

Strong institutions

Market profile

*Largest equity market
among recent EU
accession countries,
but more average in
relative terms*

Market capitalization at the end of October 2005 was PLN 271.1 billion. Market capitalization at the end of 2004 was PLN 213.0 billion, or US\$ 71.1 billion, a 53 percent increase since the beginning of 2003. Poland has the largest market of the eight transition countries that acceded to the EU in 2004. However, in relative terms, the equity market is smaller than most EU accession countries (except Slovakia and Latvia); market capitalization amounted to 30.3 percent of GDP at the end of 2004. At the end of end of October 2005 there were 254 companies listed on the WSE, up from 203 at the beginning of 2004, and from 221 companies at the end of 1999. The market saw 67 new listings in 2004-2005.

*Ownership
increasingly
concentrated, free float
decreasing*

Because of the design of its privatization programs, Poland had a relatively dispersed ownership structure in the early years of transition. Over time, the ownership and control structure of Polish companies has become concentrated, in line with other countries in continental Europe. Average free float decreased from about 43 percent to 33 percent. The State remains an active owner. Institutional investors include 16 private mandatory pension funds. The pension funds already have 69 significant (i.e. > 5 percent) stakes, and collectively controlled almost 10 percent of market capitalization at the end of 2004.

*Pillar II pension funds
becoming prominent
shareholders*

Influential corporate

The WSE promulgated a corporate governance code of best practice (*Best*

governance code

Practices in Public Companies) in 2002, and updated it in late 2004. The WSE requires listed companies to disclose compliance with the Code on a “comply or explain” basis. Market participants report that the Code appears to have had a significant impact on company behavior. The main item of controversy has been the concept of independent directors. Considerable concern was expressed by the authorities about the difficulty of penalizing “false compliance” with the Code.

Key institutions include the Securities Commission of Poland, the Warsaw Stock Exchange, and the KDPW

Public companies are under the supervision of the PSEC. The WSE is the country’s leading stock exchange, and the KDPW (National Depository for Securities) is the central depository. Most regulatory functions are centralized at the PSEC. The State Prosecutor maintains a special group of prosecutors who coordinate with the PSEC to prosecute capital market crimes. Registration of companies is conducted with the National Court Register.

Key issues

The following sections highlight of the principle-by-principle assessment of Poland’s compliance with the OECD Principles of Corporate Governance.

Investor protections

Basic minority rights in place

Basic minority shareholder rights are in place in Poland. All shareholders have the right to participate in general meetings. Amendments to the company articles (including capital increases) require 75 percent supermajority approval. Authorized capital increases (in which the board has discretion to issue shares up to the level of authorized capital) are possible, but rare. Existing shareholders have pre-emptive rights in the event of a capital increase.

Past problems related to the conduct of general meetings appear to have been resolved

General meetings must be called at least three weeks before the date of the meeting. There are no quorum requirements in the law. Significant (10 percent) shareholders can place items onto the agenda of the next general meeting, up to 30 days before the date of the meeting. Shareholders have the right to be represented by proxy. Postal and electronic voting are not available. There are some concerns that institutional and other investors may find existing voting processes relatively cumbersome, particularly the requirement to obtain “registration certificates” and the fact that voted shares are blocked for at least 7 days before the GM. Since the prior assessment in 2001, market participants report that on average the conduct of shareholder meetings has improved.

Little regulation of pension fund voting

There are no rules yet in place to require the disclosure of voting or voting policy by institutional investors acting in a fiduciary capacity. Institutional investors are working to prepare a code of ethics for the industry.

Cash flow rights are relatively closely aligned with voting rights

The 2001 Commercial Code strengthened “one-share/one-vote” provisions, and removed the possibility for public companies to issue preferred shares. Private companies can issue different types of preferred shares, but with a maximum of two votes per share. Pyramid structures, share parking in subsidiaries, and cross-shareholding have traditionally been relatively rare in Poland.

Takeover rules are generally clear and well-enforced...

Any person who has “come into the ownership of shares of a public company” of more than 50 percent of voting shares must make a bid for the remaining shares.

Poland has recently moved to implement the EU Market Abuse Directive and elements of the Takeover Directive. Squeeze-out and sell-out rules have been introduced for public companies at the 90% level. Some concerns have been raised about the existing delisting / squeeze out procedures. Over the past few

The lack of rules and recommendations on the approval of related party transactions is a relatively major weakness

years, valuation issues during squeeze-outs (and the conflicts of interest surrounding who appoints the valuation expert) were key concerns of minority shareholders.

Related party transaction approval is not regulated in the law, and receives only limited attention in the WSE Code. The lack of required approvals by the supervisory board (or the general meeting), combined with a general lack of board independence, leaves many companies open to potential expropriation. The case of Stomil Olsztyn indicates that minority shareholders may be at risk in companies controlled by foreign strategic shareholders.

Specific provisions in the company law regulating large transactions are also limited, although in many companies large transactions must have approval of the supervisory board.

Current “acting in concert” regulations appear to restrict legitimate shareholder consultation

The recently enacted Public Offering Act appears to turn many forms of normal shareholder consultations into illegal activities, and poses a legal risk for institutional investors and their employees who attempt to engage in shareholder consultations. Market participants report that questions are raised and investigations launched when institutional investors appear to vote according to a certain pattern, and if they communicate with each other at the AGM.

Disclosure

The disclosure regime is strong in Poland relative to many emerging and transition markets

Public companies are required to file annual, semi-annual, and quarterly reports. International Financial Reporting Standards (IFRS) are mandatory for all listed companies filing consolidated financial statements as of January 1, 2005. Material events must be disclosed immediately. Secondary regulation provides detailed reporting requirements and conditions. Companies are also required to “comply or explain” with the WSE Code. Public companies can disclose through an electronic system to the WSE and the PSEC, which is in the process of being upgraded to a new internet-based network. Measured against other countries that have participated in the corporate governance ROSC program, law and practice are generally in line with (or exceed) the requirements laid out in the OECD Principles.

One potential problem: the lack of preparation at many companies for the transition to IFRS

While listed companies are now required to file financial statements according to IFRS (at least the approximately 140 companies required to file consolidated statements) the Accounting and Auditing ROSC pointed out that many companies do not appear to be ready for the transition in 2005. In addition, past compliance with accounting standards was relatively weak, and the PSEC has not had the capacity or authority to enforce IFRS requirements.

Ownership disclosure

Shareholders of listed companies must disclose their direct and indirect ownership when they cross the 5% threshold (and every 2% thereafter – see detailed assessment). Companies must disclose significant shareholders in quarterly and annual reports. While the ownership structure of Polish public companies is generally well understood, the current shareholder recordkeeping framework does not lend itself to ownership transparency. The KDPW is not aware of the “ultimate owners” of Polish public companies.

Executive and Board Remuneration

As in many countries, there is reluctance to disclose executive and board pay, particularly at the individual level. Until 2005, companies were required to disclose board remuneration in the aggregate (with apparently limited compliance); from June 2005 the PSEC will require individual disclosure.

Audit quality assurance reviews have only recently gotten underway

The Chamber of Auditors is responsible for the oversight of the audit process. From 2005, Poland has adopted International Standards of Audit (ISA) in full. However, quality assurance reviews have only recently started, and there is limited transparency and public oversight of the review process.

Company oversight and the board

Two-tier board, normally supervisory board appoints management board

Joint stock companies are governed by a two-tier board structure, consisting of a supervisory board and a management board. The supervisory board is responsible for supervising the company's activities. The management board is responsible for managing the day-to-day operation of the company. The supervisory board of public companies must have at least five members.

Proportional representation possible available for the election of the supervisory board

The supervisory board is normally elected by majority vote at by the AGM, but at the request of 20% of capital, the board is elected by group voting (a form of proportional representation). By default the management board is appointed by the supervisory board, but the company articles can allow the general meeting to elect the management board, severely weakening the supervisory board.

Little guidance on duties of care and loyalty

Company law has relatively limited descriptions of the duties and liabilities of the boards. Management board members, supervisory board members (and liquidators) must, in performance of their duties, "...exercise due diligence proper for the professional nature of their actions." Management and supervisory board members and shareholders have a duty to act in the best interest of a company, but this obligation is not explicitly provided in Polish law. There are no specific requirements for members of boards to act in the interests of all shareholders, and limited conflict of interest rules for supervisory board members.

New audit committee recommendation

The revised (2005) WSE Best Practices Code (WSE Code) contains a new recommendation for the establishment of audit and remuneration committees of the supervisory board. However, there are no details about the audit committee's role and responsibilities.

Board independence requirements have been controversial, but will be enforced beginning 2005

Board independence requirements are one of the most controversial aspects of corporate governance reform in Poland. The 2002 WSE Code recommended that supervisory boards have a majority of independent directors. However, listed companies (many with concentrated ownership) did not comply with the recommendation, and its inclusion in the 'comply or explain' requirement was essentially postponed until 2005. The 2005 Code eased the 2002 recommendation, by allowing companies with majority ownership control to have only two independent directors.

Relatively little attention paid to supervisory board in law and in WSE Code

In sum, while the Code of Commercial Companies 2000 and the WSE Code represent advances in a number of areas, the role of the supervisory board remains somewhat undefined relative as compared to international good practice. In particular, the balance of power between the supervisory board and the management board remains tilted toward the latter, and the supervisory board does not yet play a central or active role in many (and perhaps the majority) of public companies.

The Polish Institute of Directors is beginning training programs for board members

The Polish Institute of Directors (PID) has developed a number of training programs for directors of listed companies, and participated heavily in the development of the WSE Code. More recently, the PID has organized the Corporate Governance Academy (in conjunction with a number of partners) to provide high-level training to boards. However, the PID does not appear to have

the consistent support from the private sector that will be required to move its development to the next step.

Enforcement

Shareholders have private redress opportunities

Shareholders have a number of private redress possibilities. Significant (10%) shareholders can call an extraordinary meeting. Shareholders can file derivative suits against directors, but only if the company has not acted within one year, and can file direct suits, if the damage is to them and not to the company. Lawsuits against directors are still relatively rare, but are growing. Shareholders can also sue to overturn meeting decisions. 5% shareholders can request the general meeting (and then the registration court) to hire a special auditor to examine a specific issue. Withdrawal (dissenter's) rights are relatively limited in Poland.

PSEC has limited ability to directly intervene, but does investigate complaints

Every shareholder has the right to file a complaint with the PSEC, but PSEC has no special powers that enable it to serve as a specialized shareholder dispute-resolution body. PSEC does follow up on complaints and investigates as necessary. The overall high level and quality of disclosure (as enforced by PSEC) is a strong source of shareholder protection.

Recommendations¹

Poland's laws already tend to comply with most of the OECD Principles, and its strong institutions give it an advantage over many emerging markets. However, it is now in competition with sophisticated markets in OECD countries, and its corporate governance policy goal should be to rise above minimum standards. Implementing the recommendations will require a combination of legislative and regulatory reform, combined with appropriate enforcement.

Increase the accountability and responsibility of owners

The State should continue to refine its ownership policies

The State should fully implement the OECD Guidelines on Corporate Governance of State-Owned Enterprises (SOEs). The government should work to set a clear and transparent ownership policy covering all SOEs, and should consider centralizing the ownership function within one organization, separate from other regulatory/policy-making functions of the state. The MST and other ownership entities should work towards providing a high level of transparency of all SOEs comparable with the level of transparency of listed companies, and should develop a well-functioning uniform disclosure and reporting system.

The government should balance the exercise of its ownership rights through supervisory boards and through the use of other shareholder rights. SOE boards should be empowered to play an active role in the SOE governance. The government should increase the professionalism and independence of the SOE board members.

Annex 2 presents a summary review of the corporate governance of state owned enterprises in Poland.

The corporate governance role of the pension funds should be comprehensively

Given the current and especially future importance of the pension funds to Polish corporate governance, their role should be examined and regulated, based on international good practice. The experience of Chile (where funds hold major stakes in many listed companies) is a useful starting point. Future revisions to

¹ A number of recommendations on accounting and auditing are developed in the Accounting and Auditing ROSC.

regulated

pension fund law and regulation should include a discussion on their corporate governance roles and responsibilities, including voting, board representation and the appointment of independent directors. The OPEs should be obliged to disclose their voting policy.

The WSE's "Novo Mercado" market differentiation strategy could be encouraged through pension fund portfolio regulation

The development of the WSE "plus tier" could be further supported by pension fund regulation. For example, higher portfolio limits could be set for investments in the plus tier companies than for standard listed companies. Over time, this requirement should work to protect pension beneficiaries, and should voluntarily encourage companies to upgrade to international standards and the plus tier.

Enforcing the WSE Code

Concerns about the enforceability of the WSE Code are misplaced

The WSE Code has been an effective tool to build awareness of corporate governance reform. Although concerns have been raised about the enforceability of the Code's provisions, in most countries it is left to shareholders and not to regulators to rule on the accuracy of "comply or explain" disclosures. A number of options are available to improve the scope, flexibility and practicality of imposing sanctions against listed companies that file false compliance statements, including imposing a legal requirement for the board to certify the compliance statement, requiring audit committees (or auditors) to monitor compliance, providing additional investigation and enforcement powers to the WSE, and incorporating the Code in law or regulation. Annex 1 presents a more detailed analysis of the WSE Code and some options for enforcement.

Essential elements of the Code should be migrated to law

International experience suggests that one of the major benefits of codes of best practice is their utility in "test marketing" corporate governance legal reforms; many provisions introduced in codes are later migrated to the law.

Continue to modernize the supervisory board

Future revisions to the law should include provisions related to related party transactions, board liability, and conflicts of interest

Future revisions to the law should focus on empowering the supervisory board, removing the clause that allows the general meeting to appoint the management board, and strengthening the provisions that define the duties of loyalty to the company. Approval of related party transactions should be the explicit responsibility of the supervisory board, perhaps with a requirement for special approval by the independent members. Revisions to the WSE Code should focus on board issues and better defining board responsibilities. Supervisory board members should also have responsibility and liability for the preparation of financial statements.

More support and resources should be provided by the public and private sector to the Polish Institute of Directors

At the same time, more resources should be invested in training supervisory board members. While the Polish Institute of Directors is an established and valuable contributor to corporate governance reform in Poland, it has not become self-sufficient, or had the resources to develop a critical mass of independent-thinking supervisory board members. Achieving this goal will require a combination of incentives, including recommendations for training in the Code, more support from the corporate and investor communities, and continued work to develop relevant curricula. The Treasury could support the Institute by requiring formal training of board members in companies where the state has participation.

The establishment of independent audit committees is a key component of the international corporate governance consensus. The PID should develop guidelines for audit committees, and training courses based on the guidelines.

Review ownership disclosure laws, enforcement, and institutions

Make enforcement ownership disclosure rules a top priority, and consider new legislative solutions

Given the importance of transparent ownership to overall levels of transparency (and to the enforcement of related party transaction disclosure), the PSEC should continue to carefully enforce ownership disclosure rules, and bring as many cases as possible to the prosecutor. In addition, the authorities could consider the option taken in certain jurisdictions (e.g. France, Portugal) of allowing the PSEC to declare certain shares “anonymous”, and stripping their voting rights, until the presentation of additional information about the owners.

Lack of centralized ownership records may create weaknesses

Evidence from other countries in the region suggests that when ownership records are centralized, concealing ownership positions becomes more difficult. KDPW might consider a long-range strategy to assume shareholder recordkeeping functions directly, and become involved in ownership disclosure.

Reform voting procedures

Voting procedures are inconsistent with Poland’s aspirations to become a major capital market, and should be overhauled in the long term

The process of establishing lists of eligible voters for general meetings is cumbersome, and may discriminate against institutional investors who do not want to block their shares in advance of the meeting. Policymakers should consider extending the announcement period to 30 days (in line with international investor requests), should pay careful attention to the EU-wide discussions on cross border voting, and should consider introducing a “record-date” system for establishing voting eligibility, providing a legal basis for postal and electronic voting, developing a standardized proxy voting form, and clarifying and standardizing voting procedures for ADR/GDR voting.

Review the minority protection aspects of the delisting and squeeze-out regulations

Tag-along rights would increase fairness and shareholder protection

Although the Takeover Directive has not been implemented, Poland’s takeover rules are generally in line with current EU practice. Shareholder rights would be improved if the privatization process was not exempted from the takeover rules, and “tag-along” rights were provided to existing minority shareholders during privatization.

The experience with squeeze-out rules should be carefully considered

The implementation of the Takeover Directive provides an opportunity to reform the current approach to the valuation of squeeze-outs. One possible approach is (i) to allow the minority shareholders to pick the initial expert, but provide the majority with the ability to appeal the first valuation by substituting one of their own, and (ii) raising the standard of experts that can be appointed by the court, when the court appoints the expert. In all cases, the law should refer to International Valuation Standards (or European Valuation Standards).

Maintain PSEC’s Independence and Fully Implement the Market Abuse Directive

Current acting in concert regulations should be revised to allow legitimate shareholder consultation

The PSEC should work with shareholder groups and other key stakeholders to bring the Public Offering Act into compliance with the OECD Principle that “...shareholders, including institutional shareholders, should be allowed to consult with each other on issues concerning their basic shareholder rights as defined in the Principles, subject to exceptions to prevent abuse.”

Return the power to issue secondary regulation to the PSEC

An independent regulator is a key element in market confidence and an important pillar in building an effective corporate governance framework. While PSEC appears to operate free of interference on a day-to-day basis, some market participants have expressed concern that the PSEC’s independence has been

compromised by the loss of its authority to issue secondary regulation. This power should be returned to PSEC.

Develop procedures for administrative enforcement of insider trading rules

While the recent adoption of the Public Offering Act has resulted in the implementation of the Market Abuse Directive, the next key step is for the PSEC to work to impose more administrative penalties for illegal insider trading. Recent World Bank research supports the conclusion that administrative sanctions are more efficient, result in more penalties, and thus have a higher deterrent effect than criminal sanctions.

Continue to improve financial reporting

Financial reporting requirements may have risen to meet the OECD Principles, but additional work is required to reach levels in other EU / OECD countries

While financial reporting and disclosure requirements are generally in line with the OECD Principles, considerable additional work by the public and private sectors will be required to improve financial reporting to the level of OECD and EU countries. These steps (detailed in the Accounting and Auditing ROSC 2005) include the transition to IFRS for listed companies (filing consolidated financial statements), enforcement of the new standards, and improvements in audit oversight. In addition, management board members should be held collectively responsible for the preparation of financial statements, and the audit committee should assume responsibility for the establishment of internal controls.

Summary of Observance of OECD Corporate Governance Principles

Principle	O	LO	PO	MO	NO	Comment
I. ENSURING THE BASIS FOR AN EFFECTIVE CORPORATE GOVERNANCE FRAMEWORK						
IA Overall corporate governance framework	X					➤ Strong overall corporate governance framework
IB Legal framework enforceable /transparent		X				➤ Clear and enforceable laws, important Code
IC Clear division of regulatory responsibilities		X				➤ Strong PSEC, clear division of reg. authority
ID Regulatory authority, integrity, resources		X				➤ Relatively strong powers, high integrity
II. THE RIGHTS OF SHAREHOLDERS AND KEY OWNERSHIP FUNCTIONS						
IIA Basic shareholder rights	X					➤ Basic rights observed
IIB Rights to part in fundamental decisions		X				➤ Fundamental decisions decided w/ 75% majority
IIC Shareholders AGM rights		X				➤ Meeting conduct improved. Notice period 21 days
IID Disproportionate control disclosure		X				➤ 5% shareholders disclosed in annual report
IIE Control arrangements allowed to function			X			➤ Mandatory bid at 50%, delisting w/ 80% majority
IIF Exercise of ownership rights facilitated				X		➤ Cumbersome voting procedure, no vote disclosure
IIG Shareholders allowed to consult each other					X	➤ No legal obstacles to consultation
III. EQUITABLE TREATMENT OF SHAREHOLDERS						
IIIA All shareholders should be treated equally		X				➤ Eq. treatment, redress generally available
IIIB Prohibit insider trading		X				➤ Insider trading illegal, considerable enforcement
IIIC Board/Mgrs. disclose interests			X			➤ Disclosure required, but limited approval procedures
IV. ROLE OF STAKEHOLDERS IN CORPORATE GOVERNANCE						
IVA Legal rights of stakeholders respected	X					➤ Limited direct involvement of workers
IVB Stakeholder redress	X					➤ Stakeholder have access to legal process
IVC Performance-enhancing mechanisms	X					➤ Shares and options available, but rare
IVD Stakeholder disclosure		X				➤ Stakeholders have access to public information
IVE "Whistleblower" protection				X		➤ Limited whistleblower protection
IVF Creditor rights law and enforcement			X			➤ Relatively weak creditor rights in int'l comparisons
V. DISCLOSURE AND TRANSPARENCY						
VA Disclosure standards		X				➤ Extensive disclosure requirements
VB Standards of accounting & audit		X				➤ IFRS required for listed co. consolidated statements
VC Independent audit annually			X			➤ ISA implemented for 2005
VD External auditors should be accountable			X			➤ Limited accountability, lawsuits
VE Fair & timely dissemination	X					➤ Many channels of information
VF Research conflicts of interests			X			➤ No specific provisions
VI. RESPONSIBILITIES OF THE BOARD						
VIA Acts with due diligence, care		X				➤ Two-tier board, limited "fiduciary" duties
VIB Treat all shareholders fairly			X			➤ Limited legislative guidance on equitable treatment
VIC Apply high ethical standards			X			➤ CSR and codes of ethics at early stage
VID The board should fulfill certain key functions			X			➤ Relatively weak supervisory board
VIE Exercise objective judgment			X			➤ New Code recommendations, as of June 2005
VIF Access to information	X					➤ Board has legal access to information

Principle - By - Principle Review of Corporate Governance

This section assesses Poland's compliance with each of the OECD Principles of Corporate Governance. Policy recommendations may be offered if a Principle is less than fully observed. **Observed** means that all essential criteria are met without significant deficiencies. **Largely observed** means only minor shortcomings are observed, which do not raise questions about the authorities' ability and intent to achieve full observance in the short term. **Partially observed** means that while the legal and regulatory framework complies with the Principle, practices and enforcement diverge. **Materially not observed** means that, despite progress, shortcomings are sufficient to raise doubts about the authorities' ability to achieve observance. **Not observed** means no substantive progress toward observance has been achieved.

SECTION I. ENSURING THE BASIS FOR AN EFFECTIVE CORPORATE GOVERNANCE FRAMEWORK

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

Principle IA: The corporate governance framework should be developed with a view to its impact on overall economic performance, market integrity and the incentives it creates for market participants and the promotion of transparent and efficient markets.

Assessment: *Observed*

Capital markets. Market capitalization at the end of October 2005 was PLN 271.1 billion. Market capitalization at the end of 2004 was PLN 213.0 billion, or US\$ 71.1 billion, a 53 percent increase since the beginning of 2003, and was the largest of the eight transition countries that acceded to the EU in 2004.² Market capitalization amounted to 29.4 percent of GDP at the end of 2004. In relative terms, the Polish equity market was comparable to that the five largest markets, but smaller than Estonia. The top 10 companies in the market represented 62.5 percent of total market capitalization in October 2004; the top 10 most traded companies accounted for 72.5 percent of total trading volume. The turnover ratio was 30.6 percent in 2004, about 45 percent of the OECD average.

Country Name	Market Cap % GDP 2004*	Market Cap (\$US bill) 2004	Turnover Ratio (%) 2004	Market Cap (% GDP) % of OECD Avg.	Market Cap (\$US mill) % of OECD Avg.	Turnover ratio % of OECD Avg.
Poland	29.4	71.1	30.6	48.9	10.2	41.1
Czech Republic	28.8	30.9	72.8	47.9	4.4	97.8
Hungary	28.8	28.7	57.3	47.9	4.1	77.0
Slovenia	30.1	9.7	13.9	50.1	1.4	18.7
Lithuania	29.0	6.5	9.3	48.3	0.9	12.5
Estonia	57.4	6.2	16.6	95.5	0.9	22.3
Slovakia	10.7	4.4	18.2	17.8	0.6	24.5
Latvia	12.1	1.7	7.9	20.1	0.2	10.6
<i>Average EU-8 Accession</i>	28.3	19.9	28.3	47.1	2.8	38.1
Mexico	25.4	171.9	29.1	42.3	24.6	39.1
Brazil	54.6	330.3	33.1	90.8	47.2	44.5
Germany	44.0	1,194.5	123.7	73.2	170.8	166.3
France	92.7	1,857.2	81.7	154.2	265.5	109.8
United Kingdom	131.5	2,815.9	140.5	218.8	402.6	188.8
OECD Average (2003)	60.1	699.4	74.4	100.0	100.0	100.0

Source: WDI Indicators online (August 2005).

At the end of October 2005 there were 254 companies listed on the Warsaw Stock Exchange (WSE), up from 203 at the beginning of 2004, and from 221 companies at the end of 1999.

Listed Companies 2000-2004

	Start of Year	IPOs	Delistings	End of Year
2000	221	13	9	225
2001	225	9	4	230
2002	230	5	19	216
2003	216	6	19	203
2004	203	36	9	230
2005 ³	230	31	7	254

² Source: S&P Emerging Markets Database.

³ 2005 data are through October only.

The market has seen considerable IPO (and delisting) activity. Since 2000, there have been 100 IPOs and 67 delistings. Strong markets since 2003 have resulted in considerable new IPO activity; 2004-2005 witnessed 67 IPOs, including the successful privatization / listing of PKO BP, the country's largest bank, the first major privatization on the stock exchange in five years.

Ownership framework. Because of the design of its privatization programs, Poland had a relatively dispersed ownership structure in the early years of transition. Over time, the ownership and control structure of Polish companies has become concentrated, in line with other countries in continental Europe.⁴ Data for 2002 suggest that, for 130 non-financial companies listed on the WSE, the largest shareholder controls 40.6 percent of voting rights, up from 33.8 percent in 1997.⁵ The stake of the five biggest shareholders in the 130 companies averaged 64.6 percent. Over time, the share of small shareholders has been decreasing and foreign and that of domestic strategic investors increasing. The average free float (as measured by the WSE) of the 130 companies decreased from about 43 percent to 33 percent from 1997 through 2002. Available data suggests that although concentration has increased, it is not as high as in many neighboring countries (e.g. Austria, Czech Republic, Hungary, Latvia, and Romania).⁶

The State is another. Although Poland implemented a variety of privatization measures throughout transition, the State remains an important owner of Polish companies. As of June 30, 2004, the State Treasury (the ownership vehicle for state owned enterprises) held shares in 1638 companies, including 477 in which it was the sole owner.

Institutional Investors. Poland has active pension and investment funds. The largest are now the 16 private mandatory (pillar II – type) pension funds. The funds are allowed to invest up to 25% of their assets in equity, and are limited to 10% of voting rights in any one company. As of the end of 2004, approximately 12 million members were contributing close to PLN 1.4 billion per month, or about USD 5.5 billion per year. Total assets were PLN 62.6 billion, of which 20.8 billion (about USD 6.6 billion) was invested in shares. The largest three funds had about 64 percent of total assets.⁷ The pension funds are already playing a major role in the corporate governance of portfolio companies. A survey of significant owners of public companies reveals that the pension funds already have 69 significant (i.e. > 5 percent) stakes, and collectively control more than 10 percent of market capitalization. Given the rate of asset accumulation, this role in corporate governance will increase in the future. ING Polska OFE, the largest pension fund, developed a set of corporate governance principles and published them on its web site at the end of May 2004. Two other OPEs have also introduced corporate governance principles.

There is also an active investment funds industry. At the end of October 2004, there were 149 licensed investment funds, including 21 domestic equity funds holding about PLN 4.0 billion in assets, equivalent to 2.4 percent of total market capitalization. This represents an increase of over 300 percent since the end of 2002.

Principle IB. The legal and regulatory requirements that affect corporate governance practices in a jurisdiction should be consistent with the rule of law, transparent and enforceable.

Assessment: Largely Observed

Corporate legal framework. All domestic companies in Poland are incorporated under the *Code of Commercial Partnerships and Companies (CCC) 2001*. The Act governs companies, their relationship to shareholders, periodic disclosure and audit requirements. The Companies Act came into effect on January 1, 2002, replacing a heavily amended pre-war law.

Company types. Corporate forms allowed under Polish law include the joint stock company (*spółka akcyjna*, or S.A.), the limited liability company (*spółka z ograniczoną odpowiedzialnością*, or Sp. z o.o.), and a variety of partnership forms. The limited liability company and the joint-stock company are the two main corporate forms, and are largely based on German models. Only SAs may issue shares publicly. SAs have a minimum share capital of PLN 500,000 (and existing companies must raise capital to that level by the end of 2005). At the end of 2003, there were 8,641 joint stock companies and 177,380 limited liability companies registered in Poland.

Securities law framework. Joint stock companies can be private or public (i.e. have issued shares as a result of a public offer). Public offerings of securities, the conditions for the introduction of financial Instruments to organized trading, and public companies are governed by the Public Trading of Securities Act 2005 and the Public Offering of Securities Act 2005 (POA). Public offerings are subject to the approval of the Poland Securities and Exchange Commission (PSEC), which is established under the new Act of 29th July 2005 on Financial Market Surveillance (FMS). Both laws are implemented by secondary regulation (called decrees) issued by the Council of Ministers.

⁴ See *Ownership and Control of Polish Corporations*, Piotr Tamowicz and Maciej Dzerzanowski, Gdansk Institute of Market Economics, October 2002.

⁵ Maria Aluchna, *Ownership Structure and Corporate Performance: Evidence from Poland*, unpublished thesis, 2004.

⁶ Table 2, *Setting Standards of Corporate Governance: the Polish Experience*, Piotr Tamowicz and Maciej Dzerzanowski, European Business Organization Review, 4:2, 2003.

⁷ Source: <http://www.knuife.gov.pl/>, data for December 2004.

At the end of July 2004, there were 271 public companies. Public companies that are not listed on the WSE (or quoted on CeTO) are considered to be in transition to become listed, or are in the process of converting to a private company.

Listing rules. Basic listing requirements are set by secondary regulation⁸: (i) shares must: be admitted to public trading, (ii) shares must have no transfer restrictions, (iii) the entire share class must be included in the listing application, (iv) expected market capitalization must be at least one million euro, (v) the shares must meet certain free float requirements: either (i) small (<5%) shareholders must hold at least 25% of shares, or small shareholders must hold more than 500,000 shares with expected market cap greater than PLN 17 million.

The WSE's own listing requirements are relatively limited, and were recently revised in line with EU requirements. Companies are listed on either the *main* or the *parallel* market. The main market has the additional requirement of three years of financial statements; in practice, only 15 companies are listed on the parallel market, and 215 companies are listed on the main market. The WSE has also introduced a "plus" market, with additional corporate governance requirements (including mandatory observance of the Corporate Governance Code), which includes 5 companies.

Codes. The Warsaw Stock Exchange Code (*Best Practices in Public Companies*) was first published in 2002 and updated in late 2004, and develops 48 best practice recommendations on the conduct of general meetings, and the activities of the supervisory and management boards. The WSE requires listed companies to disclose compliance with a code on a "comply or explain" basis, and monitors compliance; all listed companies filed compliance statements in 2004. Market participants report that the WSE Code (combined with other awareness-raising activities) appears to have had a significant impact on company behavior. The main item of controversy has been the concept of independent directors (see Principle VIE below). A revised version of the Code was released in November 2004. Beginning June 2005, disclosure of compliance with the revised board independence recommendation will be enforced.

The Polish Institute of Directors (PID) has also worked to develop a corporate governance ranking tool, in cooperation with two associations of institutional investors. In 2005, 65 companies were rated, according to criteria based on the Standard & Poors Methodology and the OECD Principles), and based on a survey of asset managers. The Institute (in conjunction with the WSE) also awards "Trustworthy Company" prizes to listed companies on the basis of the survey.

The Polish Forum on Corporate Governance has also drafted a separate Code (the "Gdansk Code"), and sponsored a number of studies and surveys, including a 2003 survey of the corporate governance practices in 50 listed companies (the "2003 PFCG Survey").⁹

Principle IC. The division of responsibilities among different authorities in a jurisdiction should be clearly articulated and ensure that the public interest is served.

Assessment: Largely Observed

Securities regulator. The PSEC is directly under the supervision and control of the government. The day-to-day operations, which are carried out by the "Office of the Commission" of the PSEC appear to operate largely independent of government interference. The Chairman is appointed by the Prime Minister for a period of 5 years. The two Deputy Chairmen are appointed by the Minister in Charge of Financial Institutions upon the recommendation of the Chairman. The 5 members of the Commission are appointed by specific government agencies and represent the interests of those agencies at the Commission meetings. Due to the personal strength of the past Chairmen, the PSEC has operated largely free of political and industry interference.

The PSEC does not have independent authority to issue regulations ('secondary legislation'), but can draft and recommend such regulations, for submission to the "proper authorities" for approval and promulgation ((FMS, Articles 7.2 and 7.3). The PSEC previously had this authority, but it was taken away from it in 2002 in the Law on Administrative Arrangement. Some market participants expressed concern that recent changes have potentially reduced the independence of the PSEC.

Stock exchange. The Warsaw Stock Exchange (WSE) is the country's principal stock exchange. It is 98.7% owned by the state treasury, although a privatization / demutualization of the exchange is under discussion. The WSE recently entered into a relationship with Euronext. Although the exchange has some enforcement powers towards issuers, in fact most enforcement and regulatory authority rests with the PSEC. The WSE has been very involved in corporate governance reform, and has issued a corporate governance code (see above).

MTS-CeTO is a regulated off-exchange market. CeTO mostly trades bonds, including the primary dealer system organized by the Ministry of Finance, but also trades the shares of 22 public (but non-listed) companies.

Central depository. The National Depository for Securities (KDPW in Polish) is the central depository of securities in Poland. Services provided include the registration of securities admitted to public trading (including government bonds),

⁸ Decree of the Council of Ministers of 17 July 2001 *On determination of conditions that must be satisfied by official stock exchanges and issuers of securities admitted to trading on such exchanges.*

⁹ The Polish Forum on Corporate Governance (which produced the Gdansk Code) carried out a survey of 50 listed companies in 2003.

the management of corporate actions, and the clearing and settlement of transactions executed on the Warsaw Stock Exchange and CeTO. The KDPW had 60 direct participants at the end of 2003, including custodian banks and brokers.

Banking and other regulators. The National Bank of Poland Bank (NBP) is the central. The Commission for Banking Supervision (Chapter 4 of Act on the National Bank of Poland) is responsible for supervising the operations of banks. The executive agency of the Commission is the General Inspectorate of Banking Supervision, which is organizationally autonomous within the structure of the NBP. Under Article 25.2, of the Act on the National Bank of Poland, the responsibilities of the Commission include:

- setting out principles for the conduct of banking activity that ensure the safety of the funds held by customers at banks,
- supervising compliance by the banks with statute, their articles of association and other legal regulations, and also with mandatory financial standards,
- performing periodic assessments of the financial condition of the banks and presenting these to the Monetary Policy Council, and evaluating the impact of monetary, tax and supervisory policies on the development of the banks,
- Giving its opinion on the organizational structure of banking supervision and establishing procedures for the performance of such supervision.

Company Registrar. The National Court Register (NCR) is the company registrar. The organization is based on district courts, supported by a central IT support system (CORS). Data is entered into the system at one of 27 courts. The public can obtain information at one of 50 "information points". Information deposited with the register is stipulated by an ordinance of the Ministry of Justice, and includes company statutes, financial statements, capital structure, indebtedness, and the identity of board members. Ownership information is not maintained for joint stock companies, but is available for limited liability companies. All companies with turnover greater than PLN 800,000 per year must file financial statements, including audit reports. Most documents are kept at the relevant registration court in paper form.¹⁰ A full printout of the information available electronically costs PLN 60.

The Registration Court enforces registration and filing requirements, and can impose fines and other penalties. Any party can inform the court about bad register data. The Court can force compliance. Market participants reported that the system functions reasonably well, without significant compliance problems.

Principle ID. Supervisory, regulatory and enforcement authorities should have the authority, integrity and resources to fulfill their duties in a professional and objective manner. Moreover, their rulings should be timely, transparent and fully explained.

Assessment: Largely Observed

Authority, integrity and resources of regulators. The PSEC reports to the Minister in Charge of Financial Institutions which approves its budget and annual work plan (FMS, Article 6). The PSEC is funded through the fees charged to entities seeking permits from the PSEC. However, these fees are paid directly to the State which then reallocates money to the PSEC as it deems fit. The Minister in Charge of Financial Institutions determines the amount and manner of assessment of the fees and the bonuses to be paid to the Commissioners and staff (FMS, Article 17.7). Budget and resources appear to be adequate, although (based on conversations with market participants) staff turnover appears to be high.

The PSEC has the authority to request that an issuer of public securities - and its officers, directors, employees, and auditors - prepare information and provide written or oral explanations regarding its activity so that the PSEC can evaluate its disclosure activity, insider trading and market manipulation (POA, Article 68.1. and 68.2). However, the PSEC cannot itself conduct an audit of the issuer, which must be conducted by a qualified audit firm (POA, Article 68.3).

Under the revised FMS, PSEC can pursue administrative, civil, and criminal cases to enforce the law. Administrative proceedings are governed by the Administrative Proceedings Code (FMS, Article 12). The PSEC can suspend or revoke licenses for entities that have violated the Law on Public Trading of Securities. It can also level "pecuniary penalties" in administrative cases for violations of the law. Article 17 also vests the Chairman with the powers of a prosecuting attorney as derived from the provisions of the Civil Procedure Code in civil cases related to public trading. The Chairman can then file suit on behalf of investors or intervene in on-going civil cases. The PSEC can seek damages for the investors or injunctions against conduct which violates the laws. The PSEC has initiated (or joined) several civil cases, including for breaches of rules regarding disclosure, resolutions at the AGM and the appointment of a special auditor. The provisions governing both administrative and civil cases are very new, and thus relatively untested.

The Chairman may file a report with the criminal authorities. PSEC staffs are allowed to sit as "second chair" in the criminal prosecutions at the discretion of the criminal prosecutors and question witnesses. PSEC staff can also act as

¹⁰ A recent EU Directive requires all EU member states to keep financial statements electronically by 2007. This transition presents a major technological and financial hurdle for the organization.

expert witnesses. The FMS provides for criminal penalties for many violations which can be brought by the criminal authorities on their own motion or as a result of a referral by the PSEC. In some instances, as in insider trading above a certain amount, the PSEC is required by law to make a criminal referral, rather than bring the case itself.

Poland's general prosecutor has formed a special group of prosecutors to work directly with the PSEC to try capital markets-related cases.

Courts. Court efficiency in Poland (though not specifically reviewed for this assessment) is considered to be relatively weak in international comparisons, particularly relative to other OECD countries. One indirect way to examine court efficiency is to compare the procedures and time required to enforce a standard contract. Poland's procedures take longer than in many other countries (See Doing Business 2005 at rru.worldbank.org).

Indicator	Poland	Regional Average	OECD Average
Number of procedures	41	29	19
Time (days)	1,000	412	229
Cost (% of debt)	8.7	17.7	10.8

SECTION II: THE RIGHTS OF SHAREHOLDERS AND KEY OWNERSHIP FUNCTIONS

The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

Principle IIA: The corporate governance framework should protect shareholders' rights. Basic shareholder rights include the right to:

Assessment: Observed

(1) Secure methods of ownership registration	To be publicly traded and listed, all securities must be deposited with the National Depository for Securities (KDPW) (POA, Article 12). Shares are dematerialized after deposit in the Depository system, and are replaced by depository accounts managed by KDPW and securities accounts managed by its participants. Final evidence of ownership is the shareholder record of each KDPW participant. Each account holder is treated as the ultimate beneficial owner under law; there is no legal concept of nominee owner. The system functions according to international standards, with no reported problems.
(2) Convey or transfer shares	All shares listed on the WSE must be freely transferable. ¹¹ Similar provisions apply to shares listed on CeTO. Private companies can restrict share transfers (CCC Art. 182). All clearing and settlement is handled by the KDPW. Share settlement is DVP Model 1 (gross share settlement and net cash settlement).
(3) Obtain relevant and material company information on a timely and regular basis	Information on public companies is widely available, including financial and non-financial information.
(4) Participate and vote in general shareholder meetings	All shareholders have the right to participate in GMs, provided they adhere to procedural requirements. Some shares do not carry voting rights.
(5) Elect and remove board members	Process. The supervisory board is elected and removed by AGM resolution, although the company articles can establish a different way to appoint supervisory board members (CCC Art. 385, Section 2). Unless the company charter provides otherwise, management board members are elected by the supervisory board, and can be removed either by the supervisory board or by the GM. Cumulative voting/proportional representation. Shareholders holding 20% of capital can request that board elections be carried out via group voting (a form of proportional

¹¹ Decree of the Council of Ministers of 17 July 2001 *On determination of conditions that must be satisfied by official stock exchanges and issuers of securities admitted to trading on such exchanges.*

¹² CCC Art. 385. For example: assume a company with 5 board seats. Before the AGM, a 20% block of shareholders requests group voting. At the AGM, two 20 % blocks opt for group voting, and appoint one board member each. The remaining 3 board seats are elected by standard majority AGM resolution, by the remaining 60% of capital.

	representation). ¹² The minimum board size in public companies is five.
(6) Share in profits of the corporation	Shareholders are entitled to dividends. Dividends are set by the AGM, based on a recommendation from the Management Board. The company deed can establish an ex-dividend date, which can be no later than two months from the date of the AGM (CCC Art. 193). Preferred shares cannot have dividends more than 50% higher than those of common shares. There were no reports of significant problems with dividend payments.
Principle IIB. Shareholders should have the right to participate in, and to be sufficiently informed on, decisions concerning fundamental corporate changes such as:	
Assessment: Largely observed	
(1) Amendments to statutes, or articles of incorporation or similar governing company documents	Amendments to the Articles require a 75 percent GM supermajority vote. A resolution on "a material change of the object of the company's activity" requires a two-thirds vote. ¹³ Shareholder authorization is also required for the approval of the management board's report and financial statements for the preceding financial year, discharge of the boards of their duties; acquisition of real estate, issuing convertible bonds, and share buy-backs.
(2) Authorization of additional shares	Issuing share capital. Capital increases require an amendment to the company articles (and a 75% supermajority vote). The company Articles may authorize the management board to issue capital, for a maximum of three years. The increase in authorized capital ("target capital") cannot exceed 75% of existing capital. ¹⁴ Resolutions to increase authorized capital require a 75% supermajority adopted with a quorum of 33% (50% of capital for private companies). New issues require supervisory board approval, unless the articles provide otherwise. However, as of 2002, the use of authorized capital in company articles was rare. ¹⁵ Pre-emptive rights. Existing shareholders have pre-emptive rights. The GM can waive pre-emptive rights with an 80% supermajority vote, if the resolution has been placed on the agenda of the GM, and the management board presents a detailed justification.
(3) Extraordinary transactions, including sales of major corporate assets	Sales of major corporate assets. Specific provisions in the company law regulating large transactions are limited. Large transactions are governed by the fraudulent conveyance sections of the Civil Code (Civil Code Art. 527). Contracts for acquisition of assets with a value of greater than 10 percent of capital require a 2/3 supermajority resolution of the GM, but only if the transaction occurs within the first two years of the company's life. In many companies large transactions must have the approval of the supervisory board.
Principle IIC: Shareholders should have the opportunity to participate effectively and vote in general shareholder meetings and should be informed of the rules, including voting procedures, that govern general shareholder meetings:	
Assessment: Largely observed	
(1) Sufficient and timely information on date, location, agenda, and issues to be decided at the general meeting	Meeting deadline. Annual meetings must be held within 6 months of the end of the financial year (CCC Art. 395). Meeting notice and available information. GMs must be called at least three weeks before the date of the meeting (CCC Art. 402). According to the PSEC's detailed disclosure requirements, public companies must announce the GM as a "current report" to the WSE and thus to the public through the exchange's information dissemination systems. ¹⁶ The current report must include the date, time and place of the GM, its

¹³ CCC Art. 416.1. In this vote all shares have one vote.

¹⁴ CCC Art. 444-452. Authorized capital was introduced in 2001.

¹⁵ Only two companies allowed authorized capital increases in 2002. See *Ownership and Control of Polish Corporations*, Piotr Tamowicz and Maciej Dzerzanowski, Gdansk Institute of Market Economics, October 2002, p. 14.

¹⁶ Decree of the Council of Ministers of 16 October 2001 (as amended) (Journal of Law 2001, No. 139, Item 1569) on current and periodical information provided by issuers of securities.

	<p>detailed agenda, the deadline for submission of registration certificates in order to vote, the details of any proposed amendments to the articles, draft resolutions and any appendices. No other resolution can be adopted unless all shareholders are represented.</p> <p>Copies of the management board report, the financial statements, the supervisory board's report, and the audit report must be issued to shareholders at their request, at least 15 days before the AGM. The WSE Code recommends that companies publish financial information on their web sites. AGM resolutions must also be disclosed as current reports.</p> <p>Quorum rules. There are no quorum requirements in the law; though each company's Articles may set especial requirements. Certain resolutions require special quorums (see Principle IIB).</p>
(2) Opportunity to ask the board questions at the general meeting	<p>Forcing items onto the agenda. Significant (10 percent) shareholders can place items on the agenda of the next GM, up to 30 days before the date of the meeting. Items cannot be voted on unless they are on the agenda.</p> <p>Questions. By law the management board must provide information and answer questions to shareholders at the GMs. The management board can refuse to respond to questions if the information is secret or its disclosure would damage the company. A shareholder can appeal this response to the Registration Court, within one week of the meeting, and request the Court to force the publication of the information.</p>
(3) Effective shareholder participation in key governance decisions including board and key executive remuneration policy	<p>Supervisory board remuneration must be determined by either a GM resolution, or in the company articles (changes to which must also be approved by the GM) (CCC Art. 392). Only the GM has the right to grant profit sharing rights to supervisory board members.</p> <p>The WSE Code addresses many issues related to shareholder meetings, implying that the conduct of many GMs was not previously considered to be fair to all shareholders. Since the adoption of the Code and the passage of the new CCC, market participants note that GM conduct has improved.</p> <p>According to a PFCG Survey, the procedures of proposing and announcing candidates for the supervisory board before GMs were rarely well implemented. Candidates were rarely disclosed before the GMs, and were almost never disclosed early enough to be useful to shareholders. Only LPP declared that it will publish information about candidates for supervisory board members on its website 10 days before the GM.</p>
(4) Ability to vote both in person or in absentia	<p>Proxy regulations. Shareholders have the right to be represented by proxy (CCC Art. 412). Proxies must be in writing but do not require notarization. Management board members cannot act as proxies.</p> <p>Postal and electronic voting. Postal and electronic voting are not available.</p>
Principle IID: Capital structures and arrangements that enable certain shareholders to obtain a degree of control disproportionate to their equity ownership should be disclosed.	
Assessment: Largely observed	
<p>Classes of shares. The 2001 Commercial Code strengthened "one-share/one-vote" provisions and removed the possibility for public companies to issue preferred shares. Private companies can issue a variety of preferred shares, but multiple voting shares are capped at two votes per share (down from five) (CCC Art. 351-352). Voting caps are allowed, at levels of 20% or higher, but are relatively rare (CCC Art. 411). The media group Agora introduced a voting cap that prevented any shareholder from voting more than 20%, unless they already own at least 75% as the result of a mandatory bid.¹⁷</p> <p>Pyramid structures, share parking in subsidiaries, and cross-shareholding have traditionally been relatively rare in Poland; one study found six cases of pyramid structures, about 20 cases of shares held by subsidiaries in 2000, and two cases of cross-shareholding. Companies are also allowed to issue "Golden Shares" (i.e. gives special rights in the articles to a specific shareholder). Golden shares were relatively common in some large privatization deals. A new golden share provision is under discussion, to be imposed at 14 state-owned companies.</p>	

¹⁷ Ownership and Control of Polish Listed Corporations, page 14.

Ownership disclosure by companies. Significant (5%) direct and indirect shareholders must be reported in the annual and quarterly reports. Quarterly reports must include changes in share or option holdings by management or supervisory board.

Under Article 70 of the POA, a public issuer is obligated to provide to the PSEC, one day before the AGM, a list of all shareholders entitled to vote. Moreover, 14 days after the AGM the issuer is obligated to provide a list of all shareholders with at least 5% of the shares of the company to the PSEC and an information agency. The PSEC can waive this requirement under Article 148a if disclosure is against the public interest or would cause material harm to the company. Article 167 provides for a fine of 1 million PLN for the failure to timely file this information.

Ownership disclosure by shareholders. The Public Offering Act defines the responsibilities of shareholders to disclose significant ownership. Shareholders should disclose direct and indirect ownership of shares to PSEC, the company, and the Office for Competition and Consumer Protection, within four days of purchase or sale after passing the 5%, 10%, 20%, 25%, 33%, 50% and 75% thresholds. Shareholders owning more than 10% should disclose every 2% change in ownership (companies traded on the WSE) or 5% (companies traded on another regulated market). Shareholders owning above 33% should disclose each 1% change. Acquisition of 25%, 33% or 50% must receive the approval of the PSEC.

The PSEC works to enforce ownership disclosure rules. It receives about 5,000 reports annually, and monitors market transactions, where it can see large block trades. Violations are enforced through the criminal court system; the PSEC cannot impose administrative penalties for shareholder-violators. If convicted in criminal court, shareholders face up to a PLN 1 million fine and frozen votes.

Disclosure of shareholder agreements. The annual report must contain information (in the activity report) about agreements which are significant to the issuer's economic activity, including agreements known to the issuer made by the shareholders, and insurance or cooperation agreements.¹⁸

Principle IIE: Markets for corporate control should be allowed to function in an efficient and transparent manner.

Assessment: Partially observed

(1) Transparent and fair rules and procedures governing acquisition of corporate control

Basic description of market for corporate control. Poland has an active mergers and acquisitions market. However, because of concentrated ownership, there are few hostile takeovers. Privatization has been a major source of M&A activity.

Tender rules/mandatory bid rules. Any person who has "come into the ownership of shares of a public company" of more than 50 percent of voting shares must make a bid for the remaining shares.¹⁹ The management board of a listed target company must present its opinion on the tender within 2 days. Violators can also be fined up to 1,000,000 PLN.

Delisting/going private procedures. Issuers can withdraw their shares from public trading, with the approval of the PSEC, if the following conditions are met. First, an acquirer must make a tender offer for all outstanding shares (POA, Article 91). Second, the acquirer must propose an AGM resolution which must be approved with an 80% supermajority, with a quorum of at least 50% of capital; the resolution must be placed on the agenda at the request of the shareholder making the tender offer.

Large shareholders can squeeze out small shareholders (but in private companies only). Up to five shareholders must accumulate at least 95% of shares. The GM must then pass a "compulsory buyout" resolution (with 95% supermajority).²⁰ The squeeze-out price is the average market price of the prior three months, or (if shares are not quoted), a price determined by an expert chosen by the GM. If GM has not chosen the expert, the management board applies to the registration court to appoint the expert and set his or her compensation.

This squeeze-out procedure suffers from an important conflict of interest related to the valuation of the shares that appears to work against small shareholders. First, the valuation expert can be selected by the acquiring shareholders, providing a downward bias on the acquisition price. Second, when the expert is appointed by the court, the

¹⁸ Decree of the Council of Ministers of 16 October 2001, *On current and periodical information provided by issuers of securities*.

¹⁹ POA, §154. The bid price may not be lower than: 1) the average market price for the last six months before the announcement of the summons or (if the shares were traded on a regulated market for less than six months) the average price over this shorter period, 2) the price, at which the shares were purchased under primary trading or the initial public offering, if the summons relates to shares which are not traded on a regulated market (§155). The price may not be lower than the highest price paid within the previous 12 months by the bidder or other entities in its control. The mandatory bid threshold was originally 33% in 1991, but was raised to 50% in 1998.

²⁰ CCC Art. 418. The company articles may set more rigorous requirements. All voting is one-share, one-vote; the voting must be open.

	<p>lack of any special qualifications and low fees can result in the appointment of relatively unqualified or inexperienced experts. Finally, there is no indication of valuation methodologies that must be followed in the analysis. For example, during the squeeze-out of Stomil Belchatow S.A. the valuator applied a discount of 60% for illiquidity – even though the company had to be private and therefore illiquid to allow the squeeze-out in the first place.</p> <p>In years past market participants believed that it was difficult to get PSEC to approve delisting and “going private” transactions. In at least one case, an application was denied, even though the buyout price was considered to be fair, on the grounds that there was a “national interest” in preventing the decline of market capitalization. Market participants now view the delisting process as relatively straightforward.</p> <p>Abuse of buy-backs/treasury shares. Companies can only buy-back their shares for specific reasons, including offering of shares to employees.</p>
(2) Anti-take-over devices	Anti-takeover devices include the introduction of authorized capital, share buy-backs, and voting caps. The use of these devices appears to be rare.
Principle IIF: The exercise of ownership rights by all shareholders, including institutional investors, should be facilitated.	
Assessment: Materially not observed	
(1) Disclosure of corporate governance and voting policies by institutional investors	<p>General obligations to vote/disclosure of voting policy. There are no rules to require the disclosure of voting or voting policy by institutional investors acting in a fiduciary capacity. The public pension funds are reportedly planning to disclose votes in the future.</p> <p>Special Rules for Institutional Investors / Pension Funds. None</p> <p>Blocked shares/record date. Shareholders who wish to vote must obtain “registration certificates” from their broker or custodian (POA, Article 9). These certificates must then be deposited with the issuer at least 7 days before the GM. Trading in the shares deposited with the issuer are then blocked until the day after the GM (POA, Article 11).</p> <p>The absence of a “record date” for eligibility of attendance at the GM, and certificate-based voting process, will be viewed as relatively cumbersome by international investors, and is inconsistent with the otherwise efficient and modern shareholder recordkeeping process.</p>
(2) Disclosure of management of material conflicts of interest by institutional investors	No rules or regulations are in place, beyond the legal requirements for disclosure of conflicts of interest as noted elsewhere in the report.
Principle IIG: Shareholders, including institutional shareholders, should be allowed to consult with each other on issues concerning their basic shareholder rights as defined in the Principles, subject to exceptions to prevent abuse.	
Assessment: Not Observed	
<p>Rules on shareholder cooperation in board nomination/election. At least 20% of shareholders may vote “in groups” electing the corresponding part of the supervisory board. (CCC Article 385.3)</p> <p>Rules on communication among minority shareholders. The recently enacted POA proscribes “acting in concert”, and appears to turn many forms of normal shareholder consultations into illegal activities, and poses a legal risk for institutional investors and their employees who attempt to engage in shareholder consultations.²¹ Market participants report that questions are raised and investigations launched when institutional investors appear to vote according to a certain pattern, and if they communicate with each other at the AGM. The acting in concert regulation is reportedly used as a defensive measure by the management of public companies to attack the legitimate actions of institutional investors. For example, shareholders find it difficult to call extraordinary meetings or make other similar proposals.</p>	

²¹ Article 87 defines acting in concert: Parties which are bounded by written or oral agreement concerning acquiring shares of the public company or voting in line during shareholders meeting upon significant matters concerning the company, even if only one of the agreeing parties take or intended to take actions resulting in legal obligations (public tender, disclosure of significant stakes etc.).

SECTION III: THE EQUITABLE TREATMENT OF SHAREHOLDERS

The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

Principle IIIA: All shareholders of the same series of a class should be treated equally.

Assessment: Largely Observed

(1) Equality, fairness, and disclosure of rights within and between share classes	<p>Availability of share class information. Share class information is available from the company articles (which are available in paper form at the registration court), and in the prospectus. In addition, the WSE Code recommends that each company post articles and other company statutes on company web sites. According to the WSE, 178 listed companies reported that they complied with this recommendation in 2003.</p> <p>Equal rights within classes. Article 20 of the Public Trading of Securities Act provides that holders of securities of the same kind are treated equally under the same circumstances. However, there are no sanctions in the law for a violation of this provision.</p> <p>Approval by the negatively impacted classes of changes in the voting rights. Where different shares of the company carry different rights, resolutions on amending the company articles, decreasing the initial capital and redeeming shares which may infringe shareholders rights of any class must be adopted by separate voting by each share class, by the majority required each specific type of resolution (CCC Art. 419).</p>
(2) Minority protection from controlling shareholder abuse; minority redress	<p>Shareholders have a number of redress possibilities.</p> <p>Ability to call meeting. Shareholders representing more than 10 percent of capital can demand that a GM be summoned. The Articles may stipulate a lower number. The request must be submitted in writing to the management board at least one month before the proposed date (CCC Art. 400). Once summoned, the GM must pass a resolution on who will bear the costs of the meeting.</p> <p>Withdrawal rights. Withdrawal (dissenter's) rights are relatively limited in Poland. Only a vote on changing the company's activities requires a buy-out offer to those shareholders who objected to the amendment or who were absent at the meeting (CCC Art. 416.4). The price is either the market price (the average of the prior three months) or "a price determined by an expert chosen by the GM." (This method of selecting the expert is biased in favor of the company.) The company Articles can exempt the company from this buyout requirement if there is a quorum of 50 percent at the GM.</p> <p>Ability to sue to overturn meeting decisions. Decisions that are "contrary to the company articles or good practice and prejudicial to interests of the company or intended to wrong a shareholder" may be overturned by the court (CCC Art. 422-427). The management and supervisory boards, shareholders who voted against or who objected to the resolution, and those who were prevented from participating or who were absent when the meeting was improperly convened, may bring the action. If the action is frivolous, the registration court can fine the plaintiff for up to ten times legal fees. The action must be brought no later than three months from the date of the meeting (for public companies).</p> <p>Redress from regulators. Shareholders can complain to the PSEC, and the PSEC investigates complaints. However, the PSEC does not function as a shareholder tribunal for the investigation of shareholder disputes.</p> <p>Ability to sue directors. The company has primary responsibility for suits against directors and others causing damage to the company. If the company fails to bring action within one year, any shareholder may file a derivative suit for making good on the damage done to the company (CCC, Art. 486). The harm must be to the company as a whole; all damages are paid to the company. The court may require the plaintiff to place a security deposit, which will be forfeit if the suit is declared to be frivolous. Shareholders can also file direct suits in their own name, in the event they have been damaged by the company's actions (CCC, Art. 490). Lawsuits against directors are rare, but are growing.</p> <p>Inspection Rights. Shareholders holding 5% of total votes can request the GM of a public company to hire a "duly qualified" auditor to examine a specific issue (POA,</p>

	Article 84). The management and supervisory boards must disclose all required documents. Failing GM approval, the Commercial Companies Code allows requesting shareholders to apply to the registration court to appoint an auditor. The requesting shareholder may be required to place a deposit or bond; if the audit reveals no violations, the deposit may be forfeit.
(3) Custodian voting by instruction from beneficial owners	Because of the basic ownership framework in Poland, custodians as such do not formally exist, because nominee ownership does not exist; the owner of the shares is the holder of record in the accounts of each participant of the KDPW. However, owners of securities do establish contracts with custodians to hold shares.
(4) Obstacles to cross border voting should be eliminated	Other than voting inefficiencies noted above (the "registration certificate" system and the requirement to deposit voting shares) there are no explicit barriers to cross-border voting.
(5) Equitable treatment of all shareholders at GMs	Small shareholders appear to receive adequate treatment at shareholder meetings.

Principle IIIB: Insider trading and abusive self-dealing should be prohibited.

Assessment: Largely Observed

Basic insider trading rules. Polish law defines illegal insider trading very broadly. Insiders and other persons who possess insider information are prohibited from using the information in placing trades in their company's stock.²² The POA also provides for a "closed period" when insiders are not allowed to buy or sell securities of "their" companies. Closed periods include from the time the confidential information concerning the issuer or the financial instruments is gained to the time that information is made public, and the period preceding the publication of quarterly (two weeks), half-yearly (one month) and annual (two months) reports by public companies.

As to the scope of the investigation and the type of information that can be obtained, Article 24 of the FMS permits PSEC to obtain inside information and to share information between the National Bank of Poland, the Banking Supervision Commission and the Commission for Insurance and Pension Funds Supervision. The PSEC may also share information with foreign authorities pursuant to an MOU. The law permits the PSEC to obtain phone records. However, a list of contacts does not include the content of the communication.

Insider trading disclosure. Insiders and their relatives must disclose all transactions in their company's shares within five days (POA, Article 156). The company must disclose all reported insider share trading as a current report, when the transaction value exceeds EUR 5,000 (USD 6,350). Failure to disclose transactions to the PSEC or issuer may result in a fine of up to PLN 100,000 being imposed by the PSEC. The PSEC publishes its decision in its Office Journal or in two national newspapers, at the expense of the violator.

Criminal/civil/administrative penalties. The PSEC can bring an administrative case against a natural person for insider trading and levy a pecuniary penalty of up to PLN 200,000 or five times the obtained benefits (POA, Article 172). The penalty must be imposed based on an administrative trial. If the inside information allowed the person to "derive financial benefit of at least material value" then the PSEC cannot bring an administrative penalty, but must refer the matter to the criminal prosecutors. Successful criminal prosecution can result in fine of up to 5,000,000 PLN (about USD 1,362,000) and imprisonment from 6 months to 5 years. Over the period 1999-2003, the PSEC submitted 37 notices to the Prosecutor (including 9 in 2003) about suspected insider trading violations. The resulting number of convictions is not available.

Principle IIIC: Members of the board and key executives should be required to disclose to the board whether they, directly, indirectly or on behalf of third parties, have a material interest in any transaction or matter directly affecting the corporation.

Assessment: Partially Observed

RPT disclosure rules. Issuers must disclose all "...transactions with its linked entities, where the single or aggregate value of such transactions concluded in the period of the last 12 months exceeds EUR 500,000" in the annual and quarterly reports, and in special current reports. The definition of a linked entity is wide, and includes the parent company, sister companies, the management and supervisory board members and their relatives, and 20 percent shareholders. Large loans and loan guarantees (defined as more than 10% of the issuer's capital) must also be disclosed. Disclosures

²² "Primary insiders" listed in the Act include: (i) members of the management board, (ii) members of the supervisory board, (iii) proxies or attorneys-in-fact of the issuer, (iv) employees of the issuer, (v) certified auditors or (vi) other persons related to the issuer under any mandate contract or any legal relation of a similar nature.

must include the transaction counterparty, the nature of the relationship, and material terms and conditions.

RPT approval rules/rules for approval of board/AGM. There are no legal requirements for the special approval of related party transactions by either board or the GM. The WSE Code does not focus on RPT approval, and only recommends that the management board "...should act with utmost care to ensure that the transactions are at arms' length." The Gdansk Code recommended that management board obtain approval of independent supervisory board members. Based on a survey of 50 companies in 2003, only seven companies had implemented a board approval process involving independent board members; other companies required board approval of certain types of transactions.

Conflict of interest rules and use of business opportunities. In the event of a conflict of interest between the company and a management board member (including spouse, relations to the second degree and "persons with whom the member has a personal relationship"), the member must recuse himself from any decisions on these matters (CCC Art. 387). It does not appear to be mandatory that this conflict be disclosed.

In addition, management board members cannot be involved in a competitive business, as a partner, board member, 10 percent shareholder, or if he or she has the right to appoint someone to its management board, without the consent of whoever appoints him or her (typically the supervisory board) (CCC Art. 380). However, these rules do not apply to family members, supervisory board members, or to significant shareholders who are not board members. The WSE Code recommends that supervisory board members should disclose any conflicts to the board, and should refrain from participating in discussions and from voting on related resolutions (WSE Code, §23).

SECTION IV: THE ROLE OF STAKEHOLDERS IN CORPORATE GOVERNANCE

The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

Principle IVA: The rights of stakeholders that are established by law or through mutual agreements are to be respected.

Assessment: Observed

List of relevant codes for stakeholders. Stakeholder rights are protected by contract or specific laws, such as the labor act, environmental law or the insolvency regime. Labor and other stakeholders have limited direct involvement in the corporate governance process. Despite the German heritage of Poland's company law, there is no codetermination or other direct involvement of workers on boards. The WSE Code recommends that the management board take into account "...the long-term interests of the company's shareholders, creditors and employees ..., as well as those of other entities and persons cooperating with the company, also the interests of the local community."

Principle IVB: Where stakeholder interests are protected by law, stakeholders should have the opportunity to obtain effective redress for violation of their rights.

Assessment: Observed

Redress mechanisms available to stakeholders. Stakeholder rights are protected by contract or specific laws, such as the labor act, environmental law or the insolvency regime.

Principle IVC. Performance-enhancing mechanisms for employee participation should be permitted to develop.

Assessment: Observed

Rules on employee stock option plans. Employees can own shares and share options. Options are, however, rare.

Principle IVD: Where stakeholders participate in the corporate governance process, they should have access to relevant, sufficient and reliable information on a timely and regular basis.

Assessment: Largely Observed

Stakeholders of public companies (employees, creditors, suppliers, and others) can access publicly available information.

Annual report discloses significant facts on employees. There are no specific requirements to disclose significant facts about employees in the annual report, beyond what is required for the reporting of material events. There are no other regulations on communication with employees. An EU Directive on employee information remains to be implemented.

Information is timely and regular. Compliance with periodic disclosure requirements by listed companies is very high.

Principle IVE: Stakeholders, including individual employees and their representative bodies, should be able to freely communicate their concerns about illegal or unethical practices to the board and their rights should not

be compromised for doing this.

Assessment: Materially Not Observed

Whistleblower rules. Employees and other stakeholders enjoy some protection under the Securities Law, in that delivering notice of the commitment of an offence does not violate insider trading and confidentiality rules (POA, Article 172). Legal experts were not aware of any other protections to “whistleblowers” under the law, or of any jurisprudence or case law.

Principle IVF: The corporate governance framework should be complemented by an effective, efficient insolvency framework and by effective enforcement of creditor rights.

Assessment: Partially Observed

Effectiveness of bankruptcy, security/collateral, and debt collection/enforcement codes. Creditor rights (though not specifically reviewed for this assessment) are considered to be relatively weak in international comparisons. A variety of standard measures developed by the World Bank for 130 countries compare Poland to its regional neighbors and the OECD average. In these comparisons legal rights are considerably weaker, but access to credit information and the coverage of credit registries is wider than in neighboring countries. See *Doing Business 2005* at rru.worldbank.org.

Creditor Rights Indicator	Poland	Regional Average	OECD Average
Cost to create collateral (% of income per capita)	1.2	7.7	5.2
Legal Rights Index (out of a possible 10)	2	5.4	6.3
Credit Information Index	4	2.0	5.0
Public credit registry coverage (borrowers per 1000 adults)	0	6.3	76.2
Private bureau coverage (borrowers per 1000 adults)	380	46.7	577.2

SECTION V: DISCLOSURE AND TRANSPARENCY

The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.

Principle VA: Disclosure should include, but not be limited to, material information on:

Assessment: Largely Observed

(1) Financial and operating results of the company	<p>Listed companies must prepare annual, semi-annual, and quarterly reports, plus reports on material events (“current reports”).²³ Financials must be consolidated, and prepared in line with the detail laid out in the prospectus requirements, and with applicable accounting rules (see Principle VB below), and must include comparables for previous periods.</p> <p>Annual report. The annual report must include the audited annual financial statements, the audit report, an “activity report” with detailed information and background to the financial statements, including activities, products, risks, borrowing and loan agreements, securities issued, explanations of the financial results, and future prospects. A separate consolidated annual report (including a “consolidated activity report”) must be prepared when consolidation is required. The annual reports must be submitted within six months of the end of the financial year, and not later than 15 days before the annual meeting.</p> <p>Semi-annual report. The semi-annual report must include the semi-annual audited financial statement, the management board report, and the auditor’s report, and must be submitted within three months of the end of the period (four months for consolidated).</p> <p>Quarterly report. Quarterly reports must include the (unaudited) financial statements, comparisons with previous periods, notes on provisioning, a brief description of significant successes, failures, and events, the opinion of the management board on</p>
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²³ POA, §81, and Disclosure decree, Section 57.1.

	the chances to meet published projections, a list of pending court proceedings, large related party transactions and loans to subsidiaries, and other information of "material importance."
(2) Company objectives	In the annual report, issuers are required to submit a letter describing the most important successes or failures of the issuer, and the prospects for development of the issuer's activity during the next financial year. Quarterly reports must also contain a brief description of significant successes or failures of the issuer during the period covered by the report, a description of exceptional factors and events that had a significant impact on performance, and the opinion of the management on previously published projections for the year.
(3) Major share ownership and voting rights	<p>Share ownership information is publicly available – see Principle IID. In the annual and quarterly reports, issuers must report all shareholders holding, directly or indirectly through subsidiaries, at least 5% of total votes, as well as any changes in the ownership of significant blocks since the prior quarterly report. Quarterly reports must also include a statement of any changes in share or option ownership by the issuer's management or supervisory board (Disclosure decree, Article 61.5, 6).</p> <p>Share class voting rights are disclosed in company articles, which are available from the National Court Register (although a complete set of articles are only available in paper form at the district court where the company is registered). Investors in listed / public companies are able to find out about the voting rights attached to it through the prospectus, which is published before the initial public offering (IPO).</p>
(4) Remuneration policy for board and key executives, and information about directors	Since 2001, issuers have been required to disclose supervisory board and management board compensation, in aggregate, including profit-based compensation (Disclosure decree, Article 64.7.16). The WSE Code echoes these legal requirements (Articles 27, 39). However, compliance has been limited; both the 2003 PFCG Survey and a more recent PID survey indicated that only a few companies disclosed basic information on remuneration. In a highly controversial move, the PSEC will require disclosure of individual compensation packages, beginning with reports filed in 2006.
(5) Related party transactions	See Principle IIIC.
(6) Foreseeable risk factors	In the annual report, issuers must describe "...material risk factors and threats and the degree of the issuer's exposure to them" in the issuer activity report (Disclosure decree, Article 64.6.3). Other periodic reports require a variety of detailed disclosures on risk factors. In the quarterly report, issuers must disclose any litigation, proceedings involving liabilities or debts greater than 10 percent of capital, and any other information that "...is of material importance for assessment of its personnel, assets and financial situations, its financial performance and changes therein."
(7) Issues regarding employees and other stakeholders	Aside from creditors, there are no specific requirements for disclosure of issues regarding employees or other stakeholders (aside from the basic requirement to disclose all events that might affect share price).
(8) Governance structures and policies	<p>Comply-or-explain in force. Companies must "comply or explain their compliance" with the 48 principles of the WSE Code (WSE Code 2005).</p> <p>Regulator enforcement practice. There is a high degree of compliance with the requirement to "comply or explain". In 2004, all 218 quoted companies filed a declaration (for 2003). 86 companies reported compliance with all 48 principles (except the principle related to independent directors). 209 companies declared compliance with all but one principle.</p>
Principle VB: Information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial disclosure.	
Assessment: Largely Observed	
<p>Compliance with IFRS. Beginning January 1, 2005, all listed companies and banks must prepare their consolidated financial statements in line with IFRS, and it is anticipated that most companies will comply. Unconsolidated reports will be prepared according to Polish Accounting Standards, which are close to IFRS but have certain material differences.</p> <p>Review/enforcement of compliance. The Accounting and Auditing ROSC noted that many companies may not be ready for the transition to IFRS. A full discussion of the transition issue is in the Accounting and Auditing ROSC for</p>	

Poland.
Principle VC: An annual audit should be conducted by an independent, competent and qualified, auditor in order to provide an external and objective assurance to the board and shareholders that the financial statements fairly represent the financial position and performance of the company in all material respects.
Assessment: Partially observed
<p>A full discussion on audit enforcement and auditor qualifications is presented in the Accounting and Auditing ROSC.</p> <p>Compliance with ISA. From 2005, Poland has adopted International Standards of Audit (ISA) in full.</p> <p>Who must be audited. All joint stock companies, banks, insurance companies, and funds in Poland must be audited.</p> <p>Auditor independence. The adoption of ISA includes the full adoption of the ISA Code of Ethics. The 2003 PFCG Survey revealed a number of problems in this area, including many cases in which the auditor was also the auditor of the controlling group, (BZ WBK, Citi Handlowy, Kruszwica, Millenium, BRE, Budimex, Kredyt Bank, Świecie, EFL) and some cases where the management board had considerable influence over the auditor appointment (Agora, Żywiec, Impexmetal, Rolimpex).</p> <p>The WSE Code recommends audit rotation after five years. Although 181 firms report compliance in 2004, the 2003 PFCG Survey revealed it to be rare in practice. Only two companies (Jelfa and Okocim) included appropriate statements in their statutes. Insurance companies have mandatory auditor rotation requirements.</p> <p>Audit committee. The revised version of the WSE Code (2005) recommends that listed companies have an audit committee of the supervisory board (WSE Code 2005 §20b). There is no general independence requirement for committee members; the only independence requirement is in Recommendation 20d (below), which refers to the companies with 50% majority control. There is no guidance on specific functions of the audit committee, and no requirements for professional qualifications. Some advanced companies have audit committees (e.g. TPSA) in line with international best practice.</p> <p>Requirements for oversight of audit. Auditors are appointed by the “governing body that approves the financial statements” (usually in the GM), although company articles can provide otherwise. Traditionally, the GM approves the selection of the auditor based on a recommendation from the management board.²⁴</p> <p>Competent and Qualified Audit Enforcement. Until 2004, Poland’s auditing standards were relatively lax. The Chamber of Auditors is responsible for oversight of the audit process, and has recently started to carry out quality assurance reviews. However, there is no public oversight mechanism, and limited transparency surrounding the quality assurance process.</p> <p>Auditor qualifications. In accordance with the Law on Auditors (1994), the Chamber of Auditors is responsible for setting professional standards for auditors, in consultation with the Minister of Finance, PSEC, and (for banks) the National Bank.</p> <p>Discussion of statutory auditors’ role and responsibilities. There are no longer such shareholder oversight institutions for joint stock companies in Poland.</p>
Principle VD: External auditors should be accountable to the shareholders and owe a duty to the company to exercise due professional care in the conduct of the audit.
Assessment: Partially Observed
<p>Auditor accountability. The Accounting Act provides for criminal liability of auditors who issue an audit opinion that “does not agree with the facts”, with penalties of a fine or two years prison or both (Accounting Act, §78). However, there is no evidence that an auditor has ever been prosecuted under these provisions.</p> <p>The Chamber of Auditors is responsible for imposing disciplinary sanctions. In the event of a violation of the Auditing Act, the standards on auditing or the code of professional ethics, it may initiate a disciplinary matter on its own initiative, pursuant to a proposal from a court or to a complaint from a third party. Disciplinary sanctions include an admonishment, a reprimand, a suspension of the statutory auditor’s certificate for one to three years, or a cancellation of an auditor’s certificate. However, the deliberations and findings of the National Disciplinary Court are confidential and not in the public domain. Per KIBR data, 81 cases heard by the National Disciplinary Court in the 18 months to October 2004 resulted in six reprimands and four suspensions but no de-registrations or further actions. The low number of sanctions suggests a</p>

²⁴ The WSE Code recommends that the auditor “...be selected by the supervisory board on the recommendation of the audit committee, or by the GM on the recommendation of the supervisory board containing the audit committee recommendation...” The WSE Code previously recommended that at least one independent member of the supervisory board approves the selection of the auditor, but because compliance any independence requirements has been postponed, this recommendation is not yet being implemented by most companies.

²⁵ See §12 of the Auditing Act, and defined by Decree of Minister of Finance dated December 2, 2003.

high degree of leniency.

The Civil Code provides for a civil liability mechanism for auditors vis-à-vis third parties.

Auditor insurance. The Auditing Act requires statutory auditors to maintain professional indemnity insurance.²⁵ A statutory auditor or an audit firm is liable for the obligation arising from the audit contract. Statutory auditors and audit firms are required to take out a professional indemnity insurance policy of at least EUR 45,000.

Principle VE: Channels for disseminating information should provide for equal, timely and cost-efficient access to relevant information by users.

Assessment: Observed

Information is available through several channels. Once a company goes public, it must submit its periodic disclosures (and current reports) to the PSEC and the WSE (or CeTO if traded there). The WSE maintains an information system (EMITENT) to handle disclosure. EMITENT is currently being upgraded to ESPI, which will be based on the internet rather than a proprietary network. Periodic disclosure (including older reports) is also available at the PSEC, in paper and electronic form.

The NCR maintains information based on company filings, including annual financial statements and the articles of association (both in paper form). Information is also available at the company. For listed companies, information is available

Material facts. Public companies are required to issue current reports on information about any events that may substantially affect the price or the value of the securities. Current reports must be issued immediately after the occurrence of the event (and not later than 24 hours later), to the WSE (or CeTO) and to the PSEC, and (20 minutes later) to the public.

Published information (papers, web). The WSE Code also recommends that companies post their articles and bylaws, reports, GM documents, and other information on its web site, and at company headquarters. In 2004, 178 companies reported that they complied. However, the 2003 PFCG Survey indicated that many companies exaggerate their compliance.

Principle VF: The corporate governance framework should be complemented by an effective approach that addresses and promotes the provision of analysis or advice by analysts, brokers, rating agencies and others, that is relevant to decisions by investors, free from material conflicts of interest that might compromise the integrity of their analysis or advice.

Assessment: Partially Observed

Disclosure of conflicts of interest by analysts, brokers, rating agencies, etc. There are no specific provisions regulating the conflict of interest by analysts. Brokers are regulated by a variety of laws and regulations designed to protect customers and reduce conflicts of interest.

SECTION VI: THE RESPONSIBILITIES OF THE BOARD

The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

Principle VIA: Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders.

Assessment: Largely observed

Basic description of board. Polish joint stock companies are governed by two-tier boards, consisting of a supervisory and a management board. The former is responsible for "supervising" the company's activities. The latter is responsible for managing the day-to-day operations and representing the company in its relations with third parties (CCC Art. 368, 382.1).

Size requirements and typical size. The supervisory board of public companies must have at least five members (three for private companies) (CCC Art. 385.1). The management board has no size requirements. Among the top 10 listed companies, the median size of the supervisory board is 9; the median management board is between 5 and 6.

Nomination and election. The supervisory board is normally elected by majority vote by the AGM, but at the request of 20% of capital, the board is elected by group voting (a form of proportional representation – see Principle IIA.5). By default the management board is appointed by the supervisory board, but the company articles can allow the GM to elect the management board. The members of both boards can serve for up to five years; staggered terms are allowed.

Eligibility requirements. Members of the management board and other senior managers (including managers of subsidiaries) cannot sit on the supervisory board (CCC Art. 387); otherwise, the law imposes no restrictions on

supervisory board members. The WSE Code recommends that supervisory board members should have the “relevant education, professional, and practical experience, be of high morale and be able to devote all time required to properly perform the function on the supervisory board” (§19). 186 listed companies reported compliance in their 2004 reports.

Adequacy of duties of loyalty and care. The CCC has relatively limited descriptions of the duties and liabilities of the boards. Management board members, supervisory board members (and liquidators) must, in performance of their duties, “...exercise due diligence proper for the professional nature of their actions”. Management and supervisory board members and shareholders have a duty to act in the best interest of a company (and not its shareholders as such) and refrain from acts causing prejudice to the Company, but this obligation is not explicitly provided in Polish law, and results from the provisions concerning civil and penal liability for acting to the detriment of a company and for damage caused CC Art. 480, 481, 483, 585). There are no specific requirements for members of boards to act in the interests of all shareholders.

Lawsuits against directors remain rare, but do exist, and are growing in number.

Insurance for directors. Many companies are now providing insurance to directors, although it is not yet common practice.

Principle VIB: Where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly.

Assessment: Partially observed

There are no specific requirements in the law for the board to provide equitable treatment to shareholders.

Principle VIC: The board should apply high ethical standards. It should take into account the interests of stakeholders.

Assessment: Partially Observed

The development of corporate social responsibility and company codes of ethics is at a relatively early stage in Poland.

Principle VID: The board should fulfill certain key functions, including:

Assessment: Partially observed

(1) Board oversight of general corporate strategy and major decisions

Board functionality by law, in practice, as recommended by Code. The supervisory board is specifically responsible by law for the evaluation of the management board's annual report and presenting its evaluation for approval at the annual shareholders' meeting. The articles may extend the powers of the supervisory board, and can identify specific issues where the management board must obtain prior consent (CCC Art 384.1). The management board's responsibilities are more general, and described as any activities which are not specifically allocated to the supervisory board or the GM. Article 32 of the WSE Code states that “...the management board sets forth the strategy and the main objects of the company's operations, and submits them to the supervisory board.”

Director training, IOD. The Polish Institute of Directors (PID) has developed a number of training programs for directors of listed companies, and participated heavily in the development of the WSE Code. More recently, the PID has organized the Corporate Governance Academy (in conjunction with Baker & McKenzie, the Hay Group, Instytut Rozwoju Biznesu, and Price Waterhouse Coopers) to provide high-level training to boards.

However, the PID does not appear to have the consistent support and resources required to move its development to the next step, in order to develop a series of on-going corporate governance training programs for board members, the development of detailed board guidelines, and a growing and active dues-paying membership.

(2) Monitoring effectiveness of company governance practices

The WSE Code recommends that the management board be in charge of the “...transparency and effectiveness of the company management system and the conduct of its business in accordance with the legal regulations and best practice.”

(3) Selecting / compensating / monitoring / replacing key executives

Unless otherwise mentioned in the articles, the supervisory board appoints and recalls members of the management board. A management board member may also be recalled or suspended by the GM (CCC Art. 368.4). The supervisory board always has the power to suspend members of the management board for “important reasons”; supervisory board members can temporarily fill vacant management board seats for up

	to three months.
(4) Aligning executive and board pay with long term company and shareholder interests	<p>Unless otherwise stated in the articles, the remuneration of the management board is determined by the supervisory board. The GM can authorize the supervisory board to grant the management board members rights to profit sharing (CCC Art. 378).</p> <p>The WSE Code provides that the remuneration of board members should be set on the basis of a set of transparent procedures and rules, and should include “incentive schemes” to ensure the effective management of the company. In particular, remuneration should not be “excessive”, and should be proportional to the size of the company, comparable to the level of remuneration granted in similar companies active on the market, and should not represent a substantial cost of the company. The privatization law has restrictions on board compensation at majority state-owned companies.</p>
(5) Transparent board nomination / election process	The WSE Code recommends that information be presented on board candidates in sufficient detail to allow an educated choice.
(6) Oversight of insider conflicts of interest, including misuse of company assets and abuse in RPTs	Boards have no explicit role in approving related party transactions or conflicts of interest between shareholders (see Principle IIIC).
(7) Oversight of accounting and financial reporting systems, including independent audit and control systems	<p>The law (the Commercial Code and the Accounting Act) do not establish collective responsibility of either board for the probity of legal entity and consolidated financial statements, or for internal controls. Accounting and internal control functions are the responsibility of the management board. Under the Accounting Act, the management board is responsible for the preparation of annual financial statements (Article 52). The Accounting Act also requires that financial statements be signed and dated by the person responsible for keeping the books and all the members of the management board. However, Article 4.5 of the Accounting Act allows the designation of a single member of the board as responsible for financial reporting and it would appear that this individual will take full responsibility. Despite a high incidence of qualified audit opinions the Accounting and Auditing ROSC team found little evidence of sanctions against directors of companies where the financial statements included a qualified audit opinion.</p> <p>The WSE Code is silent on board responsibility for the financial statements.</p> <p>Article 162 of the CCC provides that “civil liability for false information lies with the issuer, investment banker, and persons who have participated in the preparation of the information, unless they are without fault.” Article 174 also provides for criminal penalties of 5 million PLN and 6 months to 5 years in prison.</p>
(8) Overseeing disclosure and communications processes	The supervisory board plays no explicit role in the process of disclosure and communications, although they are liable for false statements.
Principle VIE: The board should be able to exercise objective independent judgment on corporate affairs.	
Assessment: Partially observed	
(1) Director independence	<p>Director independence in law and in Code. The main independence criterion in company law is that no employees of the company can serve on the supervisory board. Additional independence requirements have been a central and highly controversial issue in the development of codes of best practice. The 2005 WSE Code recommends that a majority of the supervisory board should be independent. In companies where one shareholder holds majority (50%) control, the requirement is reduced to “at least two” independent members (similar to the Gdansk Code). There was no consensus on previous independence recommendations, and compliance was not required by the WSE (until 2005). The Gdansk Code contained a more modest recommendation (at least two independent members), and gave special powers to the independent board members.²⁶</p>

²⁶ According to the Gdansk Code, the independent members have veto power on auditor appointment, remuneration of management,

	<p>Director independence in practice. By most reports, implementation has been slow. The Polish Forum on Corporate Governance (which produced the Gdansk Code) carried out a survey of 50 listed companies in 2003.²⁷ In the 2003 PFCG survey, only six companies required a majority of independent members (Agora, BZ WBK, BRE, ComputerLand and Netia); the other six require at least one or two independent members. At Amica, the right to nominate independent candidates was held by the minority shareholders; during the election, each share carries one vote and all voting shareholders are capped at 5%.</p>
(2) Clear and transparent rules on board committees	<p>Audit committees. The 2005 WSE Code contains a new requirement for the establishment of an audit committee of the supervisory board. The independence and functionality of the audit committee is not always specified; there is no general independence requirement (except for companies with 50% majority control) and the only mandate of the committee is to appoint the auditor (WSE Code, Article 20d).</p> <p>Since the new Code went into effect in November 2004 (and the relevant AGMs are generally held in the spring) this provision will begin to have an impact in the middle of 2005. However, many leading companies (e.g. TPSA, PZU) have implemented audit committees of the supervisory board, in line with international good practice.</p> <p>Other committees. The 2005 WSE Code also contains a for a remuneration committee of the supervisory board (WSE Code §28). The remuneration committee must consist of at least two independent members and at least one person possessing the relevant qualifications and experience in accounting and finance.</p> <p>Both committees must present reports on their activities to the supervisory board every year. The company should then make these reports available to shareholders.</p>
(3) Board commitment to responsibilities	<p>Restrictions on the number of board seats. There are no regulations or requirements governing the maximum number of board seats that an individual can hold.</p> <p>Board meeting requirements. By law, the supervisory board meets “as required and at least three times each financial year (CCC Art. 389.3).”</p> <p>Public availability of board attendance. Board attendance is recorded in the minutes.</p>
<p>Principle VIF: In order to fulfill their responsibilities, board members should have access to accurate, relevant and timely information.</p>	
<p>Assessment: Observed</p>	
<p>The supervisory board may, for purposes of discharging its duties, inspect all documents of the company, request reports and explanations from the management board and employees, and audit the position of the company assets (CCC Art. 382).</p>	

approval of party-related transactions, and waiver of pre-emptive rights.

²⁷ A small step forward ... Corporate Governance Rating 2003 for Polish Listed Companies, published in Rzeczpospolita on 26.01.2004.

Annex 1: Note on the Enforcement of the Warsaw Stock Exchange Code²⁸

Introduction

In recent years, corporate governance codes have come into their own as valuable mechanisms of improving corporate governance. The Cadbury Report, prepared for the London Stock Exchange in 1992, prepared and recommended the first of the well-known corporate governance codes. The European Commission has stated that all of its members should adopt such a Code.²⁹ By 2004, virtually every major industrial market—and many emerging markets—had developed a corporate governance code of best practices for their markets. The Polish market is no exception.

One of the key recommendations of the Cadbury Report, known as the “comply or explain” rule, has been incorporated into the Polish Best Practices in Public Companies 2005 issued by the Warsaw Stock Exchange (WSE) and is obligatory for all companies listed on the WSE. Under this rule, listed companies must file a compliance certificate each year which sets forth their compliance with each Best Practice Principle. If a company is not in compliance with a principle, then it must explain the extent and reasons for non-compliance.

Over time, it has been noted that one of the difficulties in the rule is determining whether the statements made in the compliance certificate are accurate.³⁰ This Note will examine the means for monitoring and enforcing the rule.

Evaluation of the Legal Provisions for the Enforcement of the “Comply or Explain” Provision

In 2005 the Warsaw Stock Exchange issued a revised version of its corporate governance code, “Best Practices in Public Companies 2005,” which is applicable to all public companies. The “comply or explain” rule is set forth in Principle 48.³¹ In order to implement the rule, the Warsaw Stock Exchange set forth obligation of a listed company to file a statement of compliance with the Best Practices its 2005 listing rules.³²

The compliance with the Best Practices is set forth in Table 1.

²⁸ This Note as well as the Corporate Governance ROSC and the Note on Corporate Governance of State-Owned Enterprises in Poland were prepared by a team led by Marie-Renee Bakker (then Lead Financial Specialist of the Europe and Central Asia Region) and Sue Rutledge, (Senior Private Sector Development Specialist/Regional Corporate Governance Coordinator) during a mission to Warsaw from November 15 to 24, 2004. All the reports were presented at a seminar in December 2005. The team included Alex Berg, (Senior Specialist in the Corporate Governance Department) who prepared the Corporate Governance ROSC, Richard Symonds (Senior Counsel in the Legal Department), who drafted this Note and Frederic Gielen (Senior Financial Management Specialist and Regional Coordinator), who led the team that prepared the Accounting and Auditing ROSC. Agata Wacławik-Wejman (Legal Department) prepared the Note on Corporate Governance of State-Owned Enterprises in Poland (see Annex II). Research assistance was provided by Olga Puntus of the Legal Department and Pasquale Di Benedetta of the Europe and Central Asia Region. All are with the World Bank.

²⁹ Communication from the Commission to the Council and the European Parliament, COM (2003) 284 Final, 21.5.2003, Sections 3.1.1 and 3.1.4.

³⁰ Speech by Mario Draghi, Vice Chairman and Managing Director, Goldman Sachs International on July 12, 2004 before Transatlantic Corporate Governance Dialogue, European Corporate Governance Institute

³¹ “[Principle] 48. In its annual report, a company should include a statement to the effect that corporate governance standards are applied. Any departure from these standards should also be publicly explained.”

³² Z “[Section 27]

1. The Exchange Supervisory Board and the Exchange Management Board may resolve the rules of corporate governance for joint-stock companies that are issuers of shares, convertible bonds or bonds with priority right admitted to exchange trading.

2. Should the resolutions referred to in sub-paragraph 1 be passed, the issuers shall provide the Exchange with a statement on observing the rules of corporate governance in the company and publish that statement. Unless the issuer declares in the statement that all the rules are observed in the company, the issuer must clarify which of the corporate governance rules adopted by the Exchange Supervisory Board and the Exchange Management Board are not observed and why.”

Table 1: Compliance with Polish Corporate Governance Code

Number of traded companies on Warsaw Stock Exchange	254	%
Companies that failed to submit declarations of compliance	0	0
Companies that complied with all principles	35	14
Companies that complied with none of the principles	8	3
Companies that complied with all principles but one, i.e. principle (number 20) concerning independent members of the supervisory board	172	68
Companies that failed to comply with principle (number 6) concerning conduct of shareholders' meetings and adoption of resolutions	32	13

Source: Warsaw Stock Exchange Data as of October 2005

All publicly-traded companies fulfilled their duties to submit compliance statements to the Warsaw Stock Exchange in 2005. Sixty-eight percent (68%) of the companies were unable to meet the principles concerning independent members of the supervisory board. Even though this is a high percentage, it is a significant improvement in relation to declarations from year 2004. In contrast, only thirteen percent (13%) of traded companies were unable to meet the Code's recommendations on conduct of shareholders' meetings and adoption of resolutions—a key issue since it is at shareholder meetings that increases in capital are approved.

Given the state of reported compliance with the Best Practices, the question is raised as to what mechanisms exist in Poland to monitor the compliance statements for accuracy and to sanction companies or individuals for filing inaccurate statements certificates.

Entities that Can Monitor the Accuracy of Compliance Statements

The monitoring of compliance statements can be done by a number of different entities. The provisions of Polish law and practice give each of them a different set of responsibilities and powers to evaluate the accuracy of the compliance statements.

Shareholders. Article 395.2 states that one of the issues to be resolved at the general meeting is the acknowledgement of the fulfillment of duties by members of a company's authorities. Consequently, since the listing rules set out the duty of the company to file a compliance statement, the compliance with the Best Practice Principles should be discussed at the general meeting.

In addition, the Code for Commercial Companies has several provisions relating to the ability of shareholders to obtain information about their companies. These provisions could be used to obtain information regarding the accuracy of the compliance statements. Under Article 395.4, copies of reports to be presented at an annual meeting will be sent to shareholders on request 15 days prior to the meeting. In addition, Article 428 allows a shareholder to request information during the course of a general meeting if it is related to an item on the agenda. A shareholder who fails to get such information can file a complaint under Article 429 with the Registry Court.

The new Act on Public Offerings³³ in Articles 84-86 also provides that a general shareholders meeting of a public company “may resolve to mandate an auditor to review, at the company's expense, a specific issue related to the company's incorporation or the conduct of its business (special-purpose auditor).” If the meeting does not approve a request by shareholders to appoint a special-purpose auditor, Article 85 of

³³ Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organized Trading and Public Companies, July 29, 2005.

the Act on Public Offerings allows the requesting shareholders to appeal to the Registry Court for an order appointing such an auditor. If the Registry Court approves the appointment, Article 86 requires the management board and supervisory board to provide to the special-purpose auditor all documents required by the Court's order.

Consequently, it appears that shareholders in Polish public companies have a number of different avenues for obtaining documents to monitor the compliance statements submitted by companies to the WSE. Since these provisions are relatively new, further research would be useful to determine the level of success of shareholders in obtaining monitoring information through the statutory procedures.

Independent Directors or Audit Committee. The Best Practices of the Warsaw Stock Exchange in Principle 20 states that over half of the supervisory board should consist of independent directors. This has been the most controversial provision in the Best Practices and as shown in Figure 1 above, many listed companies are not in compliance with it. Principle 28 of the Best Practices says that the by-laws should be changed to require the creation of audit committees of the supervisory board for listed companies. The Code of Commercial Companies does not require these provisions nor do the securities laws and regulations.³⁴

Nonetheless, the obligations of directors in Poland require them to exercise their duties for the benefit of the shareholders. The quality of governance of the supervising (oversight) board is based on the concept of fiduciary duty, which is well-developed in common-law countries such as the United Kingdom, Canada, Australia and South Africa. Polish law provides some guidance for the fiduciary duties of directors. The Polish Commercial Partnerships and Companies Code require a management board member and supervisory board member "in discharge of his duties, to exercise a degree of diligence proper for the professional nature of his actions." Article 283, Section 2. The corporate governance code in Poland thus provides a basis for determining such professional standards. While to date, no Polish courts have reviewed director behavior from such a perspective, it is expected that over time, as they become more familiar with corporate governance issues, Polish judges will look to the corporate governance code as a standard for the professional conduct of directors.

Additional research would be useful to see if the independent directors in those companies that have them have disagreed with or given a minority report regarding compliance certificates or, indeed, if they have conducted any review of the accuracy of the certifications at all.

Independent Auditors. Independent auditors are not required to monitor the compliance by a client company with the Best Practices either by the Code of Commercial Companies or the Best Practices Principles themselves; although their review of the financial statements may involve a review of some aspects of the Best Practice Principles. The Cadbury Report recommended that the independent auditors monitor compliance with the Code. Auditors have the advantage of having access to corporate information on a regular basis which would enable them to conduct such monitoring without significant additional procedural steps. Nonetheless, this is a controversial provision. The auditors regulatory body, the Financial Reporting Council, has undertaken the responsibility of monitoring the Combined Best Practice Code and its implementation, but that does not appear to include evaluations of accuracy of individual compliance statements.

Warsaw Stock Exchange. Under its current listing rules, the Warsaw Stock Exchange has not given itself the explicit authority to investigate listed companies to determine if their compliance statement is

³⁴ As of the date of this Note, two of the new securities laws had not been translated into English. When reviewed, the new laws may require a change in this statement.

accurate. However, they have a general authority to delist if the company fails to file the obligatory statement of compliance. Nonetheless, the WSE could give itself this authority and if a company which had received a request for information failed to comply and provide the requested information, the WSE could take the appropriate disciplinary actions. Even so, it does not appear that the WSE has the current capacity to conduct such investigations in terms of budget and staff.

Polish Securities Commission. To the extent that the compliance certificate contains material misrepresentations, the PSEC can investigate the company for securities fraud. However, the PSEC has no independent responsibility to monitor and enforce the Best Practices.

Sanctions Currently Available for Filing Inaccurate Compliance Statements

The sanctions that can be levied against an issuer for the filing of inaccurate compliance statements are limited in their scope and flexibility. The following are the main sanctions that can be applied and the entities that can bring them.

Shareholders. The shareholders have the authority to remove directors at the annual meeting or extraordinary meetings for not submitting accurate compliance reports.

Warsaw Stock Exchange. The main sanction currently available at the WSE for failing to file compliance certificates or filing false certificates is the delisting of the corporation. This is such an extreme sanction that it has not been applied and is even questionable as to its usefulness. Allegations of false statements in a Company's compliance statement can be adjudicated by the Exchange Court, which has the power to impose a fine on an issuer listed on the WSE up to 100,000 PLN. However, there are no sanctions against individuals either in the form of fines or removal of individuals in responsible positions.

Polish Securities Commission. The PSEC can bring an action for fraud and charge the corporation and responsible individuals. However, it does not have the authority to bring a lesser action which would be easier to bring with less drastic sanctions.

Recommendations for Enhancement of Enforcement Procedures

Based on the above analysis, the following actions could be taken to improve the scope, flexibility and practicality of imposing sanctions against listed companies that file false compliance statements. No one action is comprehensive and an effective enforcement strategy would in all likelihood require the use of a number of these approaches at the same time.

- Amend the Code of Commercial Companies to assist the shareholders in evaluating the accuracy of the compliance statement by making the certification of compliance an automatic item on the general meeting agenda, including the presentation of a report by the Supervisory Board regarding the factual basis for the answers to the compliance or non-compliance responses.
- Amend the securities regulations to require the creation of audit committees for public companies and provide that one of the responsibilities of the audit committee is to monitor the accuracy of the compliance certificates.
- The PSEC and Government of Poland may want to consider the recommendation of the Cadbury Report and give the independent auditors of public companies the responsibility to monitor the parts of the compliance certificate that are objectively verifiable.
- The WSE could amend its by-laws to specifically give itself authority to investigate compliance certificates and develop an internal unit to conduct investigations and provide for a wider range of

sanctions including sanctions against individuals. WSE should consider following the New York Stock Exchange (NYSE) model and make one person or a group of persons responsible for the compliance certificate and then go further than the NYSE and subject such individuals to penalties for false certifications through fines or removal from office. This would be less severe for the company and shareholders than the general sanction of delisting.

- PSEC should consider issuing a disclosure regulation regarding statements in compliance certificates. This would allow it to sanction a company for misstatements in a compliance certificate that fall short of serious fraud without a full blown fraud allegation and proceeding and it would also allow the PSEC to levy sanctions less severe than complete delisting.
- Finally, on a general basis, incorporate the Best Practices Principles that are subject to objective verification into the Code of Commercial Companies and securities laws thus giving them the force of law.

Annex 2:
Note on Corporate Governance of State-Owned Enterprises in Poland³⁵
October 2005
SUMMARY OF FINDINGS

In the past few years Poland has been taking important steps to improve the corporate governance of state-owned enterprises (hereinafter – SOEs). High-quality corporate governance of SOEs is important for Poland in the time of intensive transformation of the Polish economy and privatization, even though the state's ownership of SOEs is being significantly reduced. In order to successfully conclude the process of economic transformation, the state's ownership and privatization policies as well as the corresponding measures to implement those policies must be carefully and precisely designed.

The authorities are to be congratulated for the emphasis that has been placed on improving corporate governance, and on the important steps that have been taken (particularly the development of the MST Principles). However, more can be done to bring SOE governance in line with international good / best practice. Whereas the Ministry of State Treasury has been actively shaping and enhancing transparency of its corporate supervision framework over a large group of SOEs, such framework still remains to be developed by other state ownership entities. A review of the corporate governance of SOEs in Poland reveals a number of key issues, addressing of which could contribute to future improvements in corporate governance of SOEs in Poland.

The following findings are based on a preliminary assessment of corporate governance of state-owned enterprises in Poland, basing on the Guidelines of Corporate Governance of State-Owned Enterprises, as recently developed by the Organisation for Economic Co-operation and Development (OECD). The focus is on large non-financial SOEs. Particular attention is paid to the ownership supervision of the Ministry of State Treasury (hereinafter – MST) and the MST Principles of Corporate Supervision Over Companies with State Treasury Shareholdings and Other State Legal Persons of April 19, 2004, as revised on October 19, 2005 (hereinafter – MST Principles).

Key Issues

Defining the State Ownership Policy

International best practice (as reflected in the Guidelines on Corporate governance of SOEs, as recently adopted by the Organisation for Economic Co-Operation and Development) suggests that "...the Government should develop and issue an ownership policy that defines the overall objectives of state ownership, the state's role in the corporate governance of SOEs, and how it will implement its ownership policy." However, as in many countries, ownership policy in Poland does not appear to be clearly defined:

- Current ownership policy is fragmentary, in terms of its scope of application as well as in terms of the scope of the matters regulated.

³⁵ This Annex is based on a Pilot Assessment of Governance of the State-owned Enterprise Sector in Poland. The Assessment was prepared by Agata Wacławik-Wejman, the World Bank (Private Sector Development, Finance, Infrastructure/Europe and Central Asia Division of the Legal Department). The Assessment analyzes the corporate governance of state enterprises in Poland compared to the OECD's 2005 Guidelines on Corporate Governance of State-Owned Enterprises.

- The planned and desired level of future state involvement in the economy is not clear. The MST does set privatization targets for each year, including lists of companies to be privatized, but the Government does not appear to have defined an overall strategy for privatization decisions.
- There does not appear to be a policy defining the state's current involvement in competitive sectors, as opposed to the state's involvement in other sectors.

Organization of the of the State's Ownership Function

Although Polish law confers the general competence for the exercise of the state's ownership function on the Ministry of State Treasury, Poland does not have a completely centralized system of corporate supervision of SOEs. There are significant statutory exceptions. As a result, a number of key state-owned entities are supervised by sectoral ministries. In addition, certain other state entities have the right to designate board members of certain SOEs, which generally are under ownership supervision of the MST (e.g. the National Board for Radio and TV Broadcasting).

The fact that the MST is not the sole state ownership entity and the lack of coordination between the MST and the other ownership entities results in a divergence of applied corporate governance standards, including disclosure requirements.

Transparency of SOEs

Transparency is of key importance for the high quality of corporate governance of SOEs, and is recognized as such by the OECD Guidelines. Also pursuant to the MST Guidelines, achieving transparency of SOEs is one of the key goals of ownership supervision. However, the MST Principles do not establish general SOE disclosure requirements comparable with the requirements for listed companies. The recent revision of the MST Principles removed the previously declared aspiration of the MST to achieve the level of transparency equal to the level of transparency of public companies.

Although the Polish law provides for broad public disclosure, implementation is very much a work in progress. Except for listed SOEs, which must comply with the disclosure requirements of the securities regulations, there are difficulties in accessing current information about the SOEs and their economic performance, such as the current number of particular types of SOEs, size of state ownership, and value of the SOE.

The Public Information Bulletin, which is available on internet, does not yet contain the information on SOEs. Basic information about individual SOEs is available through the National Court Register and in the Official Journal (Monitor Polski). The MST also makes certain information about corporate governance of SOEs available on its website, including information on supervisory board composition, aggregate reporting on the situation of state assets (including state ownership in SOEs), and the text of the MST Principles.

The annual reports which contain aggregate information about SOEs, i.e. the Report on State Assets and the Report on the Economic Situation in MST-Supervised Wholly or Majority State-Owned SOEs, are made available to the public approximately one year after the end of the year to which they pertain. In addition, certain SOEs, such as bankrupt entities or entities in which the state holds minority shares, even if the state would be a significant or controlling minority shareholder, have not been covered by the annual MST reports on the Economic Condition of State Enterprises.

Exercise of Ownership Functions by the State

As regards the standards and procedures determining the exercise of state ownership supervision, MST

Principles regulate the state ownership supervision by the MST. There is no regulation of instruments and procedures of ownership supervision by ownership entities of the state. However, in September 2005, the Polish Council of Ministers obliged all state ownership entities to adopt principles of ownership supervision, modeled after the MST Principles, by the end of 2005.³⁶

The MST Principles are not a complete description of all principles governing the exercise of ownership function by the state. The MST Principles regulate the exercise of the state's ownership supervision through the SOE supervisory and executive boards. They focus on the duties of SOE board members, particularly the responsibilities of MST-designated supervisory board members vis a vis the MST. Other key corporate governance mechanisms, such as voting and requesting information as a shareholder, are not discussed in the MST Principles; however, as the MST informs, all those instruments are applied by the MST.

Functioning of the Supervisory Boards

The competences of supervisory boards under the Polish law, especially the SOE supervisory boards, are broad. They are assigned the key role in the strategy setting for the SOEs, CEO nomination, oversight of company disclosure etc. The existing concern is that the level of professionalism and of independence of the SOE supervisory board members, which are necessary for effective exercise their authority and rights, may be insufficient.

The MST Principles are not clear as regards the main directives of the exercise for the ownership supervision over the SOEs. This creates a certain obstacle to effective exercise of the duties by the SOE supervisory board members. For example, it is not clear how conflicts between the key goals of ownership supervision should be resolved, such as SOE value maximization directive and the duty to manage the state assets to the benefit of the national economy. This uncertainty is strengthened by the fact that the general company law does not clearly determine to whom the supervisory board members owe their fiduciary duties.

Although the number of MST-designated independent supervisory board members from the private sector has increased in the past two years, it is still very small. The Chimney Law,³⁷ which caps the executives and supervisory board members compensation, remains an obstacle to attracting independent board members with significant practice from the private sector to SOE boards. A significant number of the MST-designated SOE supervisory board members are MST employees.

Key Recommendations

Establish State Ownership Policy for SOEs ➤ *The Government should set a clear and transparent policy on state ownership of enterprises.*

The Polish Government should consider developing its SOE ownership policy. The development of the MST Principles is a significant and welcome step forward; the MST Principles clarify many details related to the exercise of state ownership, but do not set an overall state ownership policy. In particular, in view of the planned finalization of the privatization processes, the scope and strategy

³⁶ Cf. the Minutes of the Meeting of the Council of Ministers No. 38/2005 of September 27, 2005.

³⁷ The Law of March 3, 2000 Pertinent to the Compensation of Managers of Certain Legal Entities, Dz.U. 2000.26.306

of the state's involvement as investor in competitive sectors should be clarified. The corporate form should be applied to all non-financial SOEs operating on a for-profit basis.

➤ ***The state's ownership policy should cover all SOEs.***

The State should ensure effective supervision of all SOEs, including companies (subsidiaries) that are part of holding structures established by SOEs. In order to effectively supervise all SOEs, the State could consider narrowing its company portfolio to larger SOEs of strategic significance for the state interests.

➤ ***Performance goals should be clearly defined for each SOE.***

The maximization of SOE economic value should be the main guideline for the exercise of the state ownership rights. The state should also consider identifying any commercial and non-commercial (public interest) goals for each SOE, e.g. in the SOE charter. These goals should determine the operation strategy employed in particular SOEs and would determine the factors of evaluation of their performance.

➤ ***The degree of control of the state over a company's capital should determine the scope and intensity of the exercise of state ownership supervision.***

Like companies in the private sector, the intervention of the state in the functioning of a company should be dependent primarily on the level of state ownership. The breakdown of corporate governance requirements into wholly, majority, and minority state-owned SOEs, as set forth by the MST Principles, may not reflect the actual control of the state over the particular SOE in companies where the State is the controlling or significant minority shareholder. For those companies, the application of standards of state ownership supervision created for majority state-owned SOEs should be considered.

Reorganize State Ownership Function

➤ ***The ownership entities should separate the ownership function from other regulatory/policy-making functions of the state.***

The exercise of state ownership should be further professionalized and focus primarily on enhancing economic performance of the supervised entities. The Government should separate the ownership function from the market-regulation/policy-making functions of the state. It is especially important in light of the recent changes introducing special intervention rights of the state in companies in certain strategic sectors (the "Golden Veto").³⁸

To minimize the potential for conflicts of interest that could occur between the exercise of the ownership function and the exercise of other functions of the state, the Government should ensure that internal governance systems are established within each of the ownership entities which address the potential for conflicts of interest. This can be done through introduction of a set of internal procedures for the ownership supervision units regarding their operation and their contacts with other Governmental bodies whose functions may be

³⁸ The Law of June 3 2005 Determining the Special Rights of the State Treasury and the Exercise Thereof in Commercial Companies Significant for the Public Order or Public Security, Dz.U.05.132.1108.

conflicting with the functions of the ownership entities. For example, there should be an institutional separation between the exercise of the state aid functions and the exercise of the ownership functions of the state.

➤ ***Full centralization of state ownership supervision within one professional and commercially-oriented ownership entity is recommended. As a second alternative, the Government should create a coordination mechanism that harmonizes the exercise of ownership supervision by different ownership entities.***

The Government should eliminate the divergence of corporate governance standards applied by different ownership entities, and to apply a uniform disclosure framework to all SOEs. The Government should consider the possibility of establishing a single state ownership entity. At a minimum, the Government should harmonize the rules and policies of the different ownership entities. The recent resolution of the Council of Ministers of Poland,³⁹ which requires the harmonization of standards of ownership supervision among various ownership entities, should be welcomed.

***Increase
Transparency***

➤ ***The ownership entities should develop a well-functioning uniform disclosure and reporting system. The level of transparency of large SOEs should be comparable with the level of transparency of listed companies.***

The Government should continue to develop the system of public disclosure for unlisted SOEs. In addition to disclosure through the court registry and the official journal (Monitor Polski), the Government should consider facilitating the access to SOE information through increasing further the use of internet as a channel of disclosure. In particular, the scope of the key information available on internet should be increased, as required by the Law on Access to Public Information. To improve the timely updates of the information about the SOEs, the Government could consider publishing at least the key parts of the periodic reporting submitted by the SOEs by means of the Integrated Information System pursuant to the MST Principles directly to a database available on internet, such as the Public Information Bulletin.

The Government and the ownership entities should consider further improvements of the system of aggregate annual reporting on SOE performance through:

- inclusion of all types of SOEs in the annual reports on economic performance (in particular SOEs with significant minority ownership of the state, bankrupt SOEs or SOE subsidiaries),
- modifications of the methods of data aggregation and the reporting formats to increase the comprehensiveness of the data or deepening the analysis of SOEs supervised by ownership entities other than the MST.

The Government could consider requiring large non-listed SOEs to prepare their consolidated financial statements in conformity with International Financial Reporting Standards.

The internal audit of the SOEs should be further developed based on the model

³⁹ Cf. footnote 1.

of large public companies with the application of international best practices. Especially in large SOEs, strengthening of risk management, financial controls, and governance procedures, is recommended.

Exercise Ownership Rights

➤ ***The ownership entities should exercise the state ownership rights through supervisory boards and through other key mechanisms of exercise of shareholder rights.***

The use of particular mechanisms of corporate governance of SOEs should be determined in accordance with the general principles of corporate governance. The appropriate use of available corporate governance mechanisms prevents distortion of balance between the state and other SOE shareholders, as well as stakeholders. To provide for a complete picture of the mechanisms through which the state exercises its shareholder rights, the MST and other ownership entities could consider including the standards of the use of the key corporate governance mechanisms other than the supervisory and executive boards, such as active participation at the General Meetings, voting and requesting information as a shareholder, in the MST Principles and in other possible codifications of SOE governance standards.

Professionalize the Supervisory Boards

➤ ***The Government should increase the professionalism and independence of the SOE supervisory board members to ensure that the SOE supervisory boards are empowered to play an active role in SOE governance.***

The MST and other ownership entities should closely monitor the nomination of supervisory board members to ensure that it leads to the choice of candidates who meet the highest standards of professionalism. The participation of experienced and well-trained persons, in particular private sector specialists on SOE supervisory boards should be sought. To achieve this, the Government should consider revisiting its compensation policies for supervisory board members and linking compensation to performance.

Executive and supervisory board members of SOEs should be required to act solely in the best interest of the SOE. The legal and regulatory framework for the boards and board members should not inhibit their independence and loyalty of the board members to the interests of the SOE. When exercising the state's ownership rights, the ownership entities should put stress on setting up efficient communication between the state-designated board members and other members of the board, enabling the board to act as a whole in the best interest of the SOE.

The SOEs should comply with standards of the Best Practices in Public Companies 2005 of the Warsaw Stock Exchange with respect to the appointment of independent supervisory board members. The MST and other ownership entities should consider reducing the number of civil servants serving as members of supervisory boards, and work to increase the number of independent supervisory board members from the private sector who bring special knowledge, contacts, and other benefits to the company.

Poland Terms/Acronyms

Acquis Communautaire The body of legislation of the European Communities and Union. Applicant countries must accept the acquis before they can join the EU.

GM: General Shareholders Meeting

WSE: Warsaw Stock Exchange

PTSA: Public Trading of Securities Act (Act of 29th July 2005 on the public offer, on conditions for introduction of financial Instruments in the organized trading system and on public companies)

FMS: Act of 29th July 2005 on Financial Market Surveillance

CCC: Commercial Companies Code (basic company law)

PSEC: Polish Securities and Exchange Commission (abbreviated in Polish as KPWiG)

PID: Polish Institute of Directors

Co-determination: Term used to describe labor representation (employees and union representatives) on supervisory boards (particularly of German companies).

Cross Shareholding: Cross shareholding refers to reciprocal shareholdings between two companies.

Cumulative voting: Cumulative voting allows minority shareholders to cast all their votes for one candidate. Suppose that a publicly traded company has two shareholders, one holding 80 percent of the votes and another with 20 percent. Five directors need to be elected. Without a cumulative voting rule, each shareholder must vote separately for each director. The majority shareholder will get all five seats, as s/he will always outvote the minority shareholder by 80:20. Cumulative voting would allow the minority shareholder to cast all his/her votes (five times 20 percent) for one board member, thereby allowing his/her chosen candidate to win that seat.

GDP: Gross Domestic Product.

ISA: International Standards on Auditing

IFRS: International Financial Reporting Standards

KDPW: National Depository for Securities

Pre-emptive rights: Pre-emptive rights give existing shareholders a chance to purchase shares of a new issue before it is offered to others. These rights protect shareholders from dilution of value and control when new shares are issued.

Proportional representation: Proportional representation gives shareholders with a certain fixed percentage of shares the right to appoint a board member. Referred to in Poland as Group or Block Voting.

Pyramid Structures: Pyramid structures are structures of holdings and sub holdings by which ownership and control are built up in layers. They enable certain shareholders to maintain control through multiple layers of ownership, while at the same time sharing the investment and the risk with other shareholders at each intermediate ownership tier.

RPT: Related party transactions. The OECD Principles of Corporate Governance hold that it is important for the market to know whether a company is being operated with due regard to the interests of all its investors. It is therefore vital for the company to fully disclose material related party transactions to the market, including whether they have occurred at arms-length and on normal market terms. Related parties can include entities that control or are under common control with the company, and significant shareholders, such as relatives and key managers.

Shareholder agreement: An agreement between shareholders on the administration of the company. Shareholder agreements typically cover rights of first refusal and other restrictions on share transfers, approval of related-party transactions, and director nominations.

Share Parking: The practice of temporarily holding shares under a variety of names to disguise a large ownership position.

Squeeze-out right: The squeeze-out right (sometimes called a "freeze-out") is the right of a majority shareholder in a company to compel the minority shareholders to sell their shares to him. The sell-out right is the mirror image of the squeeze-out right: a minority shareholder may compel the majority shareholder to purchase his shares.

Withdrawal rights: Withdrawal rights (referred to in some jurisdictions as the "dissenters", "oppressed minority," "appraisal" or "buy-out" remedy) give shareholders the right to have the company buy their shares upon the occurrence of certain fundamental changes in the company.

This report is one in a series of corporate governance country assessments carried out under the Reports on the Observance of Standards and Codes (ROSC) program. The corporate governance ROSC assessments examine the legal and regulatory framework, enforcement activities, and private sector business practices and compliance, and benchmark the practices and compliance of listed firms against the OECD Principles of Corporate Governance.

The assessments:

- use a consistent methodology for assessing national corporate governance practices
- provide a benchmark by which countries can evaluate themselves and gauge progress in corporate governance reforms
- strengthen the ownership of reform in the assessed countries by promoting productive interaction among issuers, investors, regulators and public decision makers
- provide the basis for a policy dialogue which will result in the implementation of policy recommendations

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