Hastings International and Comparative Law Review

Volume 17
Number 4 *Summer 1994*

Article 6

1-1-1994

Privatization of State-Owned Enterprises in Poland

Jerzy Rajski

Follow this and additional works at: https://repository.uchastings.edu/hastings_international_comparative_law_review

Part of the Comparative and Foreign Law Commons, and the International Law Commons

Recommended Citation

Jerzy Rajski, *Privatization of State-Owned Enterprises in Poland*, 17 Hastings Int'l & Comp.L. Rev. 767 (1994).
Available at: https://repository.uchastings.edu/hastings_international_comparative_law_review/vol17/iss4/6

This Article is brought to you for free and open access by the Law Journals at UC Hastings Scholarship Repository. It has been accepted for inclusion in Hastings International and Comparative Law Review by an authorized editor of UC Hastings Scholarship Repository.

Privatization of State-Owned Enterprises in Poland

By JERZY RAJSKI*

I. Introduction

The privatization of post-communist economies based extensively upon state ownership of property requires fundamental changes in the property ownership structure inherited from former regimes. The dilemma facing economic reformers is that to create a self-regulating market economy, they must intervene on an unprecedented scale. The scope, rate, and nature of the privatization process have greatly influenced the emerging post-communist political, economic, and social systems.

Privatization in Poland, as in other post-communist countries, has become a complex and difficult political, social, and economic issue. Deeply rooted political controversies were revealed during parliamentary debates over the drafts of privatization laws and then during the implementation of privatization policies. Powerful left-wing lobbies have been strongly combating various pro-market reform programs. In 1990, these lobbies pressed for privatization laws oriented both toward worker participation in management and capital ownership by workers. In that same year, compromise solutions were reached which provided for a state-controlled privatization concept and took account of the legitimate interests of workers.

II. Legal and Organizational Framework

A legal framework for the privatization of state-owned enterprises (SOEs) has been established through a series of acts passed by the Polish Parliament in 1990. These acts include:

1. the Privatization of State-Owned Enterprises Act of July 13, 1990;[1]

* Professor at the Faculty of Law, Warsaw University.

1. Privatization of State-Owned Enterprise Act, J.L., No. 51, item 298 (1990), *as amended by* J.L., No. 60, item 253 (1990); J.L., No. 111, item 480 (1990) [hereinafter Privatization Act].

2. the Extension of Operation of the Privatization of State-Owned Enterprises Act of November 9, 1990;[2] and

3. the Establishment of the Office of the Minister for Ownership Transformations Act of July 13, 1990.[3]

The above legislation has been supplemented by the Act of March 30, 1993 on National Investment Funds and Their Privatization[4] (NIF Act), which created the legal framework for a mass privatization program. Separate rules concerning privatization of state-owned banks have been included in the Banking Law Act of January 31, 1992, as amended.[5]

Specific rules were introduced by the Act of February 5, 1993 on Ownership Transformations of Some State-Owned Enterprises of Particular Importance for National Economy.[6] The Act determines the principles of privatization of state-owned enterprises engaged in:

1. black-coal mining and wholesale trading;

2. brown-coal mining; and

3. production, transmission and sale of electric and heating energy.

The list of the above enterprises was established by Regulation of the Council of Ministers of April 19, 1993.[7]

Development of the organizational framework for privatization involved a reallocation of duties between the Polish Parliament and the government, represented by the Council of Ministers. The *Sejm*, or lower house of Parliament, establishes annually the fundamental direction of privatization operations and determines the distribution of funds collected therefrom.[8] The *Sejm* makes decisions by passing resolutions at the instigation of the government. The government's responsibility is to prepare appropriate proposals for privatization and to justify their merits to the *Sejm*. The *Sejm* also supervises the government's privatization activities. To fulfill this responsibility, the *Sejm* established a special permanent Commission on Ownership

2. Extension of Operation of the Privatization of State-Owned Enterprises Act, J.L., No. 85, item 498 (1990).

3. Establishment of the Office of the Minister for Ownership Transformations Act, J.L., No. 51, item 299 (1990) [hereinafter Minister of Privatization Act].

4. National Investment Funds and Their Privatization Act, J.L., No. 44, item 207 (1993) [hereinafter NIF Act].

5. Banking Law Act, J.L., No. 72, item 359 (1992).

6. J.L., No. 16, item 69 (1993).

7. J.L., No. 33, item 147 (1993).

8. Privatization Act, *supra* note 1, art. 2, para. 1.

Changes charged with oversight of the government's privatization projects.

The Minister of Ownership Transformations, who answers to the Parliament, implements privatization policy. According to Article 2, paragraph 2 of the Minister of Privatization Act, the Minister of Privatization:

> 1. drafts guidelines on state policy concerning privatization of state-owned enterprises;
>
> 2. drafts, in collaboration with the Minister for International Cooperation, guidelines on state policy concerning capital cooperation with foreign investors;
>
> 3. analyzes ownership changes;
>
> 4. cooperates with trade unions, associations, chambers of commerce and other civic organizations as well as with regional public administrative bodies and local governments in forming and developing private enterprises;
>
> 5. initiates personnel training in fields related to privatization activity, such as capital markets and the development of private enterprises and disseminates pertinent information; and
>
> 6. carries out other tasks specified in the Privatization Act as well as those arising out of other provisions.

The detailed scope of operation of the Minister of Ownership Transformations has been determined by the Regulation of the Council of Ministers of November 14, 1990.[9] The Minister of Industry and Trade exercises the powers conferred to the Minister of Ownership Transformations with respect to state-owned enterprises of particular importance for national economy as provided for by the Act of February 5, 1993.[10]

III. Privatization Methods

The Privatization Act provides two main methods for the privatization of SOEs. The first method involves two stages. Since the specific legal nature of an SOE excludes any possibility of changing its owner, privatization must begin with the transformation of an SOE into a commercial company in order to give it the proper corporate form. The privatization of such a corporation is then effected by selling its shares.

The second method of privatization involves the liquidation of an SOE in order to dispose of its assets. A draft law amending the Priva-

9. J.L., No. 68, item 328 (1990), *as amended by* J.L., No. 69, item 328 (1993).
10. J.L., No. 16, item 69 (1993).

tization Act provides that SOEs (exercised by their bodies and the directors and employees' councils in consultation with the general assembly of employees) decide which privatization method will be utilized for their enterprise.

IV. Transformation of SOEs Into Corporations

An SOE may be transformed into either a joint-stock company or a limited liability company. Transformations proceed on a case-by-case basis through a decision made by the Minister of Ownership Transformations. According to Article 5, paragraph 1 of the Privatization Act, the proper procedure may be initiated either by the SOE itself, acting through its bodies,[11] or by the founding body (*i.e.*, the government agency which founded the SOE, such as a competent minister or a local government body) acting with the consent of the SOE.[12] A minister, however, may reject the proposed transformation of an SOE into a corporation based on the SOE's financial situation or an important state interest.[13]

The Act also grants the Prime Minister the right to order the transformation of an SOE upon the request of the Minister of Privatization.[14] Before submitting such a request, however, the Minister of Privatization should consult the director, employees' council, and founding body of the SOE.[15]

The corporation established through transformation of an SOE is owned by the State Treasury as the sole shareholder.[16] It is subject to relevant provisions of the 1934 Commercial Code (portions of which remain in force) with some amendments introduced by the Privatization Act.[17] These amendments include specific rules addressing the process of transformation of SOEs and the functioning of State Treasury companies created through this process.

It is worth noting that Article 17, paragraph 1, of the Privatization Act provides for the establishment of a supervisory council in each corporation with one-third of the council's members elected by the employees. Furthermore, provisions of the transformed corporation's articles of incorporation or founding act which provide for the elec-

11. Privatization Act, *supra* note 1, art. 5, para. 1.
12. *Id.*
13. *Id.* art. 5, para. 3.
14. *Id.* art. 6, para. 1.
15. *Id.* art. 8, para. 1.
16. *Id.*
17. *Id.* art. 7.

tion of the supervisory council members by the employees may not be repealed or amended, unless the supervisory council consents, while over half of the corporation's shares remain in the hands of the State Treasury.[18]

V. Privatization of State Treasury-Owned Corporations

Privatization of State Treasury-owned corporations is effected by the sale of their shares to third parties or the increase of their stated capital for sale to third parties. All shares must be transferred within two years from the date the corporation is entered into the commercial register, unless the Council of Ministers provides for a longer period.[19] Before offering shares to third parties, the Minister of Privatization must order an economic and financial study valuing the assets of the enterprise and assessing the need to implement proper organizational, economic and technical changes.[20] The economic and financial study is not required, however, if the asset value of the SOE was determined prior to transformation and the shares are to be distributed immediately after the transformation.

Article 23, paragraph 1, of the Privatization Act provides that the State Treasury shares may be sold through either:

1. an auction-type mechanism;
2. a public offering; or
3. negotiations entered into in connection with a public invitation to negotiate.

Bidding by auction open to selected persons or to the public has been used in some sales of small and medium size corporations. Sale by tender has been used for privatizing a number of medium and large size corporations, when the Minister was looking for a proper investor.

The public offering mechanism was used for the first five privatizations of State Treasury corporations at the end of 1990. Public subscription for the purchase of stock of these corporations was very successful, with more than 100,000 persons purchasing shares. However, the last public offering—of one of Poland's largest banks, Bank Slaski—has been severely criticized because of mismanagement. It appears that the public offer price seriously undervalued the shares. Each subscriber could finally acquire only three shares due to the

18. *Id.* art. 17, para. 2.
19. *Id.* art. 19, para. 1.
20. *Id.* art. 20, para. 1.

huge number (about 800,000) of subscribers at the undervalued price. The stockbrokers of the Bank as well as other stockbrokers were unable to register the shares of the majority of shareholders before the first quotation of the shares on the Warsaw Stock Exchange on January 25, 1994, when they rose to almost fourteen times their public offer price! The Deputy Minister of Finance responsible for the valuation of the shares was dismissed, and the Minister of Finance resigned. The Securities Commission revoked the banking license of Bank Slaski and asked the State Prosecution Office to initiate penal proceedings against the Bank's Board.

A sale following negotiations entered into pursuant to a public invitation to negotiate, which may be either open or selective, has also been used to find interested investors, especially foreign investors. The Council of Ministers, on a motion of the Minister of Ownership Transformation, may in specific cases permit State Treasury shares to be sold in a different manner from those mentioned in Article 23, paragraph 1, of the Privatization Act (*e.g.*, to a pre-identified single buyer or to a group of purchasers).[21] Several State Treasury corporations have been sold by permission of the Council of Ministers to pre-identified foreign and Polish investors.

VI. Employee Participation in the Capital Ownership of Privatized Corporations

Employee participation in the capital ownership and management of privatized SOEs has been a highly sensitive political and social issue in Poland. Consequently, it has been the subject of heated discussion in parliament, as well as among political parties, trade unions and in the mass media.

A draft privatization law, endorsed by several members of the Parliament in 1990, focused on employee participation and envisaged a transformation of the majority of SOEs into employee-managed or even employee-owned corporations. Despite the early focus of the draft, the Privatization Act grants the employees of a privatized company a right to purchase on preferential terms only up to twenty percent of the total shares held by the State Treasury.[22] The preference granted to employees expires after one year[23] and consists of the right to purchase shares at fifty percent of the price of non-preferential

21. *Id.* art. 23, para. 2.
22. *Id.* art. 24, para. 1.
23. *Id.* art. 24, para. 4.

transfers offered to other natural persons who are Polish citizens.[24] The Privatization Act also, however, assures employees the right to acquire additional shares according to general (*i.e.*, non-preferential) terms.[25]

Experience in Poland has demonstrated that a great number of employees are interested in preferential purchases of shares of privatized SOEs. There is also a growing tendency towards more complete acquisition of privatized SOEs by the employees and management. The establishment of special financial institutions for this purpose as well as state financial support for employee shareholding are envisaged.

VII. Privatization of State Property by Way of Liquidating State-Owned Enterprises

The decision to liquidate an SOE may be made for various reasons. Some SOEs have to be liquidated in order to demonopolize or otherwise restructure their economic activities. Others should be liquidated because of their unhealthy financial condition or because the SOE's assets may be better utilized by private owners or users. A decision regarding liquidation is made by the founding body of an SOE after having obtained the consent of the Minister of Ownership Transformations.[26] The decision of the founding body may be made at its own initiative or upon a request of the employees' council.[27] The founding body of the SOE and the Minister of Ownership Transformations should obtain the relevant information concerning the SOE's financial condition before making any decision regarding liquidation. If the decision to liquidate is made, a general schedule for utilizing assets after the proposed liquidation of the SOE should be prepared.

An SOE may be liquidated for any of the following purposes:

1. to sell, in whole or in integrated parts, the enterprise's assets;

2. to contribute the enterprise's assets, in whole or in integrated parts, to a corporation; or

3. to transfer the enterprise's assets, in whole or in integrated parts, for a specific period of time for use under contract by third parties.[28]

24. *Id.* art. 24, para. 3.
25. *Id.* art. 24, para. 1.
26. *Id.* art. 37, para. 1.
27. *Id.* art. 37, para. 2.
28. *Id.* art. 37, para. 1.

A number of liquidated SOEs have been sold either in whole or, more often, in parts to third parties. Sale by competitive bids has been frequently used. Two types of bidding procedures have been used: open and selective. Under open or public bidding, tenders are solicited through public announcements. Under selective bidding, usually employees or other persons co-operating with the liquidated SOE (such as agents) are invited to submit a tender. Pursuant to this selective procedure, hundreds of stores belonging to liquidated commercial SOEs have been sold to employees and agents, enabling them to create their own enterprises. Parts of approximately a dozen liquidated SOEs have been sold to foreign investors.

The State Treasury has used the assets of dozens of liquidated SOEs as in-kind contribution to the capital of other corporations. In a number of cases, the purpose of the liquidation was to demonopolize or otherwise restructure the liquidated SOE's activities (*e.g.*, after liquidating an SOE which enjoyed a monopolistic position in the area of filling stations, several competing corporations were created). The great majority of SOEs have been liquidated, however, so that their assets can be used by third parties. Such liquidation may be decided only through application of the employees' council, adopted after obtaining the opinion of the general assembly of the employees or their delegates.[29]

Article 38, paragraph 1, of the Privatization Act grants employees a right of first refusal to obtain the use of an enterprise's assets, provided they create a corporation whose shareholders would include a majority of the employees. The amount of share capital of the corporation should not be lower than twenty percent of the joint value of the founding fund and the enterprise fund of the liquidated SOE.[30] The right to use the liquidated SOE's assets may be transferred to a non-employee corporation only with the prior approval of the general assembly of the employees, or if the employees fail to create their own corporation within two months after the employees' council decided to liquidate the SOE.[31] The assets of a liquidated SOE are then used by third parties pursuant to a contract concluded by the founding body, in the name of the State Treasury.[32]

29. *Id.* art. 38, para. 1, §1.
30. *Id.* art. 38, para. 1, §5.
31. *Id.* art. 38, para. 2.
32. *Id.* art. 39, para. 1.

The parties may stipulate that after a specified period of time the user has the right to purchase the assets.[33] In determining the purchase price, the value of previously paid installments for the use of assets is to be taken into account.[34] Thus, the contract for use of assets can be an intermediary solution, prior to a subsequent privatization. The great majority of liquidated SOEs have been transferred to employees' corporations.

VIII. Mass Privatization Program

The new mass privatization program envisages the transfer of beneficial ownership of a large portion of former SOEs to the adult population through an intermediary—the National Investment Funds.[35] The Polish mass privatization program is linked to capital markets. The program provides all adult citizens domiciled in Poland with an opportunity to share in future profits of these companies and should improve the management of about 450-500 SOEs transformed into commercial companies.

The political, economic, and social aims of the mass privatization program include:

1. accelerating the privatization process of SOEs which has been hampered by a lack of domestic capital;[36]
2. strengthening the declining public support for privatization;
3. spreading private shareholding ownership;
4. accelerating the development of a securities market; and
5. attracting foreign investment.

IX. National Investment Funds

The mass privatization program will be implemented through National Investment Funds, established by the State Treasury in the form of joint stock companies.[37] The rights of the State Treasury as founder and shareholder are exercised by the Minister of Privatization. The idea of the funds is to remove the state from the management of the privatization process by creating a new owner of the transformed SOEs, who, being directly interested in increasing their market value,

33. *Id.* art. 39, para. 2.
34. *Id.*
35. *See infra* discussion of National Investment Funds.
36. The program enables a quick and effective privatization by avoiding the long and expensive process of valuating the SOEs.
37. NIF Act, *supra* note 4, art. 3, para. 1.

will adjust them to market requirements. According to Article 4 of the NIF Act, the funds seek to increase the value of their assets by enhancing the value of the shares of the companies which they hold. The funds endeavor to achieve this purpose by:

1. exercising rights with respect to the shares of former SOEs transformed into corporations to improve the management of the corporations and to obtain new technology and loans;
2. buying and selling shares of companies; and
3. granting and obtaining loans.

Article 44 of the NIF Act contains a long list of restrictions imposed on NIF activities. The purpose of these restrictions is to minimize the investment risk. The NIF Act provides for the establishment of two kinds of funds: ones created to provide economic benefits to all adult citizens, others designed to compensate certain state employees and pensioners for their claims to wage and pension increases for 1991. The State Treasury contributes to the funds sixty percent of the shares of each corporation taking part in the program. Of these shares, thirty-three percent will be allocated to one of the funds in order to give it a lead shareholding interest and twenty-seven percent will be distributed in equal portions among all other funds. Fifteen percent of the shares in each company will be distributed free of charge to the employees. In all, the Minister of Privatization envisages the establishment of about 15-20 NIFs.

X. Governing Bodies of National Investment Funds

The governing bodies of NIF's are the General Meeting, the Supervisory Board, and the Management Board.[38] Until the first general meeting in which the new shareholders participate, the members of the supervisory board of a fund are appointed by the Minister of Privatization with the consent of the President of the Council of Ministers. They must be appointed from among persons selected through a competition conducted by a special Selection Commission, which is composed of nineteen members: five elected by the Parliament, twelve appointed by the Prime Minister, and two designated by the Solidarity and OPZZ trade unions. The Commission has started to examine 6800 applications submitted by the candidates for about 200-240 positions in the NIFs. The management board of a fund is appointed by the supervisory board for a period not exceeding two

38. *Id.* art. 14.

years. So long as the State Treasury remains the sole shareholder of a fund, only a Polish citizen may be a member of the management board.[39] The management board convenes a general meeting of shareholders within ten months after the end of each fiscal year.[40]

XI. Management of the Assets of an NIF

The NIF Act provides that each fund may contract for the management of its assets with a management firm provided that the fund is represented by the supervisory council in so doing.[41] The aim of this provision is to improve management of fund-held companies. A fund in which the State Treasury is the sole shareholder may conclude a management contract only with firms previously selected by way of a competitive tender. The criteria of selection was established by a Regulation of the Council of Ministers of September 13, 1993.[42] The deadline for submitting bids expired on December 31, 1993. Approximately 100 firms and banks grouped into thirty-three Polish and Polish-foreign consortia to submit bids. The NIF Act establishes certain criteria for fees that may be paid to the management firms, such as annual performance fees and final performance fees.

XII. Share Certificates

Share certificates, transferable bearer securities representing the property rights to an equal number of shares in every fund existing at the time of their issuance, will be issued by the State Treasury for which the Minister of Privatization acts.[43] Two kinds of share certificates will be issued: universal share certificates and compensation share certificates. All citizens who are registered as permanent residents in Poland, and who were at least eighteen years old by December 31, 1993, are entitled to receive an equal number of universal share certificates. These certificates will be exchanged for an equal number of shares of funds, other than those designated for compensation purposes.

The main reasons for not initially giving the beneficiaries the right to choose the funds include administrative simplicity and the fact that small investors typically do not have access to adequate informa-

39. *Id.* art. 19.
40. *Id.* art. 20, para. 3.
41. *Id.* art. 21, para. 1.
42. J.L., No. 84, item 394 (1993).
43. NIF Act, *supra* note 4, art. 29.

tion. The delivery of a universal certificate is subject to a fee, the amount of which is determined by a regulation of the Council of Ministers. Its amount may not, however, exceed ten percent of the average monthly wage in the national economy as announced by the President of the Central Statistical Office for the last month covered by the available statistics.[44] The right to receive a share certificate is not transferable or inheritable.[45] The share certificates may be freely traded on or outside the stock exchange.

XIII. Exchange of Share Certificates for NIF Shares

A share certificate is exchangeable at the National Depository of Securities for an equal number of shares in every fund existing at the time of the issuance of the share certificate and designated by the Minister of Privatization for that purpose. The exchange, however, may take place only after shares in all such funds have been admitted to public trading under Article 49 of the Act of March 22, 1991 on Public Trading in Securities and Trust Funds.[46] The Minister of Privatization determines the date after which the share certificates may be exchanged for shares of funds and the mode of such exchange. All shares of a given NIF are to be exchanged for share certificates, except for a package of fifteen percent of shares in every fund reserved for other purposes.[47]

XIV. Results of the Privatization Process

From 1990 through 1993, the privatization processes have led to a significant quantitative growth of the private sector. The number of individuals undertaking business activities has surpassed 1,700,000 and the number of companies with foreign capital participation has reached 14,000.

Of 8,441 SOEs which existed at the end of 1990, 2,571 had been included in the ownership transformation process by the end of 1993. Of these, 522 SOEs have been transformed into corporations, though only 98 of them have privatized (twelve of which are listed on the Warsaw Stock Exchange). The decision to liquidate 1999 SOEs—either based on Article 37 of the Privatization Act or Article 19 of the

44. *Id.* art. 33, para. 2.

45. *Id.* art. 34, para. 1.

46. Public Trading of Securities and Trust Fund Act, J.L., No. 103, item 447, *as amended* in 1993.

47. NIF Act, *supra* note 4, art. 38.

SOE Act—was fully implemented with respect to 881 SOEs. The process of liquidation of certain SOEs has been prolonged by difficulties in finding purchasers of their assets as well as by unclarified ownership problems, due among other things to a lack of proper regulation of the legal status of some of SOE's assets. In all, 700 SOEs have been liquidated in order to transfer their assets to employees' corporations.

XV. Privatization Policy — The 1994 Agenda

In 1994, the Polish government aims to combine existing privatization efforts with:

— restructuring programs and increasing domestic and foreign investment;

— efforts to bring share prices in line with their market price;

— efforts to include employees in the process, especially in the case of small and medium size enterprises;

— government supervision of contractual obligations undertaken by the owners of newly privatized companies.

In addition, the government has prepared a new draft Act on the Privatization of SOEs which is intended to consolidate all proposed amendments to the 1990 Act. This draft provides, among other things, for the easing of the conditions under which liquidated SOEs are leased and for the right of employees to acquire free of charge fifteen percent of the shares of a privatized SOE. The Minister of Ownership Transformations, however, is seeking to reduce this employee right of acquisition to ten percent. Lastly, the government is preparing a draft act on the State Treasury which will determine the principles of management of state property and ownership supervision carried out in the name of the state.