

## LIQUIDATION OF THE BANKRUPTCY ESTATE IN POLAND / Rafał Adamus

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**Abstract:** *The purpose of this study is to present the general principles and general issues of liquidation of the bankruptcy estate under Polish law. It should be stressed that liquidation of the bankruptcy estate is intended to satisfy the creditors of the insolvent debtor. Therefore, the manner of liquidation of the bankruptcy estate has an obvious impact on the final bankruptcy dividend for the creditors. The rules governing the liquidation of the bankrupt's assets are of the key-importance for the theory of law and the practice. The article defines the directional principles of liquidation of the bankruptcy estate, procedure of liquidation of the bankruptcy estate. The subject of this paper there is the liquidation of the bankruptcy estate in dealing with insolvent consumers and the so-called prepared liquidation (pre-pack), which is to simplify and accelerate the liquidation of the debtor's assets. The issue of the liquidation of the bankruptcy estate became seriously important because of the crisis after SARS-CoV-2 epidemic.*

**Key words:** *Bankruptcy, insolvency, liquidation, bankruptcy estate, trustee, prepared liquidation, lex concursus, bankruptcy law, civil law, commercial law, Polish law*

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### 1. PRELIMINARY REMARKS

Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings stipulates in Article 7 section 1, 2 b,c that as a rule the law applicable to insolvency proceedings (*lege non distinguente* procedural and material provisions) and their legal effects shall be that of the European Union Member State within the territory of which such proceedings are opened (*lex concursus*: the "State of the opening of proceedings"). *Lex concursus* determines the assets which form part of the bankruptcy estate and the treatment of assets acquired by or devolving on the debtor after the opening of the bankruptcy proceedings and the respective powers of the debtor and the insolvency practitioner. Thus, Polish Bankruptcy Law Act<sup>1</sup> regulates the rules of liquidation of the bankruptcy estate in proceedings opened in Poland.

Liquidation of the bankruptcy estate (liquidation of assets could be defined as follows: selling out assets belonging to the bankrupt on the day of declaration of

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<sup>1</sup> Bankruptcy Law Act of February 28, 2003, Official Journal No. 60 item 535 as amended.

bankruptcy and acquired by the bankrupt in the course of bankruptcy proceedings; liquidation is mainly a competence of the trustee) to satisfy creditors is one of the basic stages of bankruptcy proceedings. "Liquidation of the bankruptcy estate" is also the wording of Title VII, Part I of the Bankruptcy Law Act of February 28, 2003, including the provisions of art. 306 - 334 B.L. (Cieślak, 2004, p. 15; Horosz, 2013, p. 67; Janda, 2005, p. 63; Lewandowski & Wołowski, 2011, p. 189; Pannert, 2010, p. 16; Podel & Olszewska, 2012, p. 302). This study is a general commentary on the indicated legal regulation.

An application for the declaration of bankruptcy may be accompanied by an application for approval of the terms of sale of the debtor's enterprise or its organized part or assets constituting a significant part of the enterprise. The court shall accept the application for approval of the terms of sale, if the price is higher than the amount that can be obtained in bankruptcy proceedings on liquidation under general rules, less the costs of proceedings that should be incurred in connection with liquidation in such mode. The court may accept the application if the price is close to the amount possible to obtain in bankruptcy proceedings on liquidation under general rules, reduced by the costs of proceedings that should be incurred in connection with liquidation in this mode, if there is an important public interest or the possibility of preserving the enterprise of the debtor. Taking into account the application, the court in the decision on the declaration of bankruptcy approves the terms of sale, specifying at least the price and the buyer of the assets being the subject of the sale referred to in this chapter. In the order, the court may also refer to the terms of sale specified in the draft contract.

The bankruptcy estate is property belonging to the bankrupt on the day of declaration of bankruptcy and acquired by the bankrupt in the course of bankruptcy proceedings, which serves to satisfy the creditors of the bankrupt (A. 61 - 62 B.L.). In civil law, assets are sometimes understood as assets and liabilities. Nevertheless, the mass of bankruptcy - as is rightly accepted in the science of law - is only the assets of the bankrupt. The provisions on the liquidation of the estate of bankruptcy do not apply to assets belonging to the bankrupt but not included in the estate (see Articles 64 - 67 B.L., Articles 70 - 74 B.L.). As a matter of fact, non-property rights do not form part of the bankruptcy estate and are not subject to liquidation by the trustee. Non-property rights (personal rights) may still be exercised by the bankrupt themselves.

## 2. BANKRUPTCY PROCEEDINGS AND ITS COMPARISON TO OTHER PROCEDURES

The liquidation of the bankruptcy estate has certain **similarities to enforcement proceedings**, which may also involve forcing the debtor's assets forcibly cash by the enforcement body to satisfy the creditor (or creditors) for whom enforcement was initiated. The liquidation of bankruptcy estate - by virtue of law (*ipso iure*) - covers all assets of the bankrupt, referred to as the estate. It is a kind of "general" enforcement proceedings. Enforcement, in principle, extends to those assets that will be seized by the enforcement authority at the request of the entitled creditor. At the same time, the bankruptcy proceedings cover all the creditors of the bankrupt who have filed their claims to the trustee or who are subject to the list of claims *ex officio*, irrespective of whether those creditors have a valid court ruling or a decision of a proper administrative authority confirming their claim. In bankruptcy proceedings, private and public law claims are satisfied on equal rules. In turn, the Polish legal system provides for separate judicial (for private claims) and administrative enforcement (for public claims). For the purposes of the bankruptcy proceedings, a number of enforcement law institutions have been

adopted (e.g. the structure and effects of the so-called enforcement sale). Bankruptcy proceedings are sometimes referred to as so-called general execution.

The liquidation of bankruptcy estate also has certain similarities to the **internal liquidation proceedings** of a legal person or an organizational unit (Adamus, 2010, p. 51; Kidyba, 2010, p. 53; Kopaczyńska-Pieczniak, 2010, p. 68; Michalski, 2010, *passim*; Sołtysiński, 2010, p. 877, 2016, p. 830; Witosz, 2011, *passim*), in which - as a rule - the assets of the liquidated entity are credited (with which the assets of the liquidated entity may be taken over by its shareholders).

The **liquidation of bankruptcy estate consists** - in principle - of cashing in the components of the bankruptcy estate in order to satisfy the claims of creditors whose claims have been recognized during the bankruptcy proceedings. In other words, the term 'liquidation' can (with certain exceptions) be replaced by 'cash'. The liquidation of the bankruptcy estate does not apply to funds at the disposal of the bankrupt at the time the bankruptcy is declared (cash on bank accounts, cash on hand). These funds will be used to cover the costs of bankruptcy proceedings and their distribution among creditors under the so-called subdivision proceedings. From a theoretical point of view, if the only (exclusive) component of the bankruptcy estate were cash, then in such proceedings the liquidation (cash) phase of the bankruptcy estate would be superfluous. The liquidated assets are primarily covered by the costs of bankruptcy proceedings (see Art. 230, 231 para. 1, 342 sec. 1 B.L.). The consequence of the liquidation (monetization) of the bankruptcy estate is the distribution among creditors of funds obtained from the sale of assets under the so-called division proceedings (Articles 335 - 360 B.L.). Under bankruptcy proceedings involving the liquidation of assets of the bankrupt (however it is possible to conclude an arrangement and stop the liquidation of the estate - Article 266a B.L.), it is not possible to satisfy creditors by providing them with individual components of bankrupt's property (*in natura*).

In some cases, liquidation of assets may involve indirect, two-step cashing of assets. For example, if the subject of the benefit is recovered from non-monetary claims, the trustee "liquidates" the claim. The trustee then sells (in other words, cashes) the subject of a non-cash benefit. If one exercises some of third-person rights, they may not be cashed in.

The issue of **initiating the liquidation stage** (Jankowski, 1999, p. 245; Strus-Wołos, 2011, p. 25) of the bankruptcy estate has been regulated in the content of Art. 308 - 310 B.L.

The course of the liquidation of the bankruptcy estate is independent of the procedure for determining the list of claims by the trustee (see Article 244 B.L.). In other words, the liquidation of the bankruptcy estate by the trustee may take place before the deadline for filing claims. *De lege lata* submission of claims is addressed directly to the trustee. Completion of the list of claims and its final approval by the judge-commissioner - in principle - enables the start of the so-called subdivision proceedings, which is a consequence of monetizing the assets included in the estate.

The liquidation of the bankruptcy estate does not have to be fully completed for the bankruptcy proceedings to enter the so-called subdivision proceedings. On the contrary, the legislator aptly adopted a flexible regulation model allowing for partial division plans as the liquidation of the bankruptcy estate progresses. In accordance with art. 337 section 1 B.L. the distribution of bankruptcy estate funds is made once or several times as the bankruptcy estate is liquidated. As a rule, the liquidation of the bankruptcy estate should be carried out in full, which means that all assets in the bankruptcy estate should be monetized. It should be assumed that the limit of liquidation (cashing) of the bankruptcy estate is the state of satisfaction of all creditors within the meaning of Art.

189 B.L. The above conclusion should be drawn from the content of art. 368 section 2 B.L, pursuant to which the bankruptcy court declares the termination of bankruptcy proceedings involving the liquidation of the assets of the bankrupt also when all creditors have been satisfied.

In this context, it is worth referring to the decision of the Supreme Court of 22 January 2010<sup>2</sup>. The ruling indicated the view that if the bankruptcy proceedings involving the liquidation of the assets of the bankrupt led to satisfaction of all creditors and remained the company's assets, "there are not always grounds to remove the company [from the National Court Register] and deprive the company of legal existence. The company, which collects the remaining assets after the bankruptcy proceedings, decides about its fate. There are no obstacles to object being removed from the register and to take up business again. In such a situation, there are grounds to depart from the literal interpretation of Art. 477 sec. 1 and sec. 2 of the Code of Commercial Companies and Partnerships, because it is difficult to remove a company [from the court register] after conducting proceedings in which its creditors were satisfied, but it still has its assets and in accordance with the law stipulates the will to continue existence". Further, the Supreme Court consistently argued that after the company has restarted its activities, its removal from the register may take place after liquidation or, if applicable, subsequent bankruptcy. In the examined case, the Supreme Court stated that the entity "subject to liquidation bankruptcy, would exceptionally only want to renew its activity under the same company". According to the Supreme Court, "if after the bankruptcy proceedings of a joint-stock company remain the company's assets, its removal from the register does not have to be preceded by the announcement and liquidation." The Supreme Court allowed the transfer of assets remaining after the end of the bankruptcy proceedings and after full satisfaction of the creditors of the company's shareholders. The opinion expressed by the Supreme Court deserves approval.

The legal actions of the person who performed the functions of a trustee, consisting in the sale of assets that were included in the bankruptcy estate, made after the final termination, cancellation and revocation of the bankruptcy proceedings will be invalid.

The liquidation may not be carried out in full: the bankruptcy proceedings may be discontinued (Article 266a B.L.), annulled (Article 371 B.L.). It is possible – as an exception to the general rule - to conclude an arrangement in the course of insolvency proceedings involving the liquidation of assets of the bankrupt (Article 361 B.L.). In such a case liquidation of assets should be stopped. In accordance with art. 368 section 1 B.L. a bankruptcy court will conclude that the bankruptcy proceedings have been completed after the final division plan has been completed.

The liquidation of the bankruptcy estate is a fragment of the court proceedings, which is the bankruptcy proceedings. Therefore, it is subject to significant formal requirements. Because bankruptcy law consists of substantive and procedural norms, provisions on the liquidation of the bankruptcy estate are of different legal nature.

As part of the liquidation of the bankruptcy estate, two basic functions of insolvency proceedings should be implemented, expressed in Article 2 B.L. First, liquidation should lead to satisfaction of creditors as much as possible. In other words, the liquidation of the bankruptcy estate should be carried out in such a way as to cash its components in the most favourable way from the point of view of the interests of all creditors. Secondly, the liquidation of the insolvency estate should take into account, as far as possible, the salvation of the current debtor enterprise. The content of Article 2 B.L.

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<sup>2</sup> V CSK 208/09.

should be the basis for settling any emerging legal problems related to the liquidation of the estate.

The liquidation of the bankruptcy estate is carried out by single-source sale or auction of the bankrupt enterprise in its entirety or its organized parts, real estate and movables, claims and other property rights included in the bankruptcy estate or by collecting debts from the bankrupt debtors and executing other property rights.

After the declaration of bankruptcy, a bankrupt enterprise may be continued if it is possible to enter into an arrangement with creditors or it is possible to sell the bankrupt enterprise in its entirety or its organized parts. If the trustee runs a bankrupt enterprise, they should take all actions ensuring the company's position at least in a non-deteriorated condition. The bankrupt enterprise should be sold as a whole unless it is not possible. The sale of a bankrupt enterprise may be, after the consent of the judge-commissioner, preceded by a fixed-term lease contract with a pre-emptive right, if economic reasons support it.

The sale made in the bankruptcy proceedings has the effects of the execution sale. The buyer of the components of the bankruptcy estate is not responsible for the bankrupt's tax liabilities, also arising after the declaration of bankruptcy. The sale of real estate results in the expiration of the rights and land personal claims disclosed by the entry in the land and mortgage register or not disclosed in this way but reported to the judge-commissioner within the prescribed period of time. In the place of the expired law, the right holder acquires the right to be satisfied through the sale of the encumbered property.

The liquidation of the bankruptcy estate in the bankruptcy proceedings involving the liquidation of the assets of the bankrupt belongs to the **trustee** (Feliga, 2013, p. 114; Gil, 2007, p. 39), (Articles 173, 308 B.L.). When liquidating the bankruptcy estate, the trustee is subject to supervision by the judge-commissioner (Article 152 B.L.).

Certain powers, in connection with the liquidation of the bankruptcy estate, were reserved directly for the benefit of the judge - commissioner, the board of creditors, the bankruptcy court. This will be shortly discussed in further parts of this study.

When carrying out activities related to the liquidation of the bankruptcy estate, the trustee is obliged to take actions with due diligence in a manner enabling the use of the bankrupt's assets to satisfy creditors to the highest extent, in particular by minimizing the costs of bankruptcy proceedings (Article 179 B.L.).

### 3. LIQUIDATION OF BANKRUPTCY ESTATE DUE TO THE CRITERION OF THE SUBJECT OF LIQUIDATION

Due to the criterion of the subject of liquidation, liquidation of the bankruptcy estate may consist, first of all, in selling the bankrupt enterprise as a whole (enterprise in the meaning of a subject of legal action, not a person; (Adamus, 2011b, p. 49; Bielski, 1999, p. 29; Habdas, 2007, p. 63; Katner, 2007, p. 1221; Kidyba, 2009, p. 1221; Komosa & Tropaczyńska, 1996, p. 27; Litwińska, 1993, p. 7; Norek, 2007, p. 29; Pełczyński, 1998, p. 71; Strzępka, 2005, p. 1393, 2007, p. 5, 2004, p. 23; Świdorski, 1999, p. 82; Szydło, 2002, p. 72; Widło, 1997, p. 30, 2004, p. 9; Wilejczyk, 2004, p. 16). The sale of the bankrupt enterprise as a whole is due to, among others on the content of Article 2 B.L., a model way of liquidation, and also the most favourable from the point of view of the economic environment of the bankrupt to avoid the so-called domino effect, where the bankruptcy of one entity in the chain of economic connections results in the bankruptcy of other entrepreneurs. At the same time, the liquidation of the bankruptcy estate may consist of selling the bankrupt enterprise as a whole, but excluding some components of the

enterprise, e.g. cash accumulated on bank accounts and in hand, claims, etc. The sale of the bankrupt enterprise without some of its components is subject to the bankruptcy law applicable to the sale of a business. The question arises here about the limit of exclusions so that one can still deal with the sale of the enterprise without some components. The literature aptly indicates that a functional criterion should be used, and as a consequence, the subject of the activity should constitute a certain whole that enables conducting business activity. This view is adopted in the practice of applying the law. In turn, the auxiliary criterion is the criterion of the type of ingredients that make up the enterprise, with the most important elements of the individualization of the enterprise, such as the name, clientele or reputation. The criterion determining the recognition of a given activity as having the whole enterprise (Poźniak-Niedzielska, 2003, p. 229) as its object is the objective criterion and not the subjective one. There is an opinion expressed in the literature that a bankrupt enterprise does not include money obtained from running the enterprise. Cash consists of insolvency funds with the sole purpose of satisfying creditors. Other authors also express the view that as part of the sale of an enterprise in bankruptcy, no legal title may be transferred to the buyer for cash at hand and in bank accounts, although this issue is not clearly assessed. When assessing this issue, however, one should refer to the content of art. 311 section 1 B.L.

Secondly, liquidation of the bankruptcy estate may consist in selling the so-called an organized part of the enterprise. The sale of an organized part of the enterprise is not directly subject to the provisions on the sale of the bankrupt enterprise as a whole but is largely based on their content.

Thirdly, as part of the liquidation of a bankruptcy estate, the sale of an "unorganized part of an enterprise", or groups of assets of a "former" bankrupt enterprise, may take place. The sale of unorganized parts of an enterprise (e.g. several devices) is subject to such rules as the sale of individual components of the estate. In practice, it happens that individual components are combined when sold in larger groups. This is due to various practical reasons, e.g. to sell attractive market components together with unattractive mass components.

Fourthly, liquidation of a bankruptcy estate may consist of the sale of individual components of the bankruptcy estate, which are subject to a separate legal regime than the sale of the enterprise. The above distinction has practical significance from the point of view of Article 6 section 1 of the VAT Act. In accordance with Article 6 section 1 of the VAT Act, the provisions of this Act shall not apply to "the sale of an enterprise or organized part of an enterprise."

#### 4. RULES FOR LIQUIDATION OF BANKRUPTCY ESTATE

Further on, there should be pointed out the guiding principles governing proceedings aimed at the liquidation of the bankruptcy estate.

The first rule to be mentioned is the principle of maximizing the satisfaction of creditors. The programmatic purpose of insolvency proceedings, and also the sense of its conduct, is to satisfy creditors' claims to the highest possible extent (Article 2 B.L.). Research shows that the amount of the liquidation dividend (i.e. the amount of money obtained by the creditor based on the distribution plan) is not high in the practice of bankruptcy proceedings in Poland. This state of affairs is influenced by a number of factors, e.g. late submission of bankruptcy petitions, under-capitalization of entrepreneurs, etc. Liquidation of the bankruptcy estate plays a key role in implementing this rule. The more profitably the trustee sells the assets of the bankrupt, the greater the liquidation dividend for the bankrupt's creditors. If the trustee organizes a tender or

auction for the sale of the assets of the bankrupt, the only criterion for selecting bids is the price. In accordance with Article 179 B.L., the trustee is obliged to take action with due diligence in a manner enabling the use of the assets of the bankrupt in an optimal way, in order to satisfy creditors as much as possible.

It should be remembered that sales made as part of the liquidation of the bankruptcy estate are so-called forced sales (quick sales). In fact, the prices obtained by the trustee may be lower than the prices obtained for the sale of similar assets, if the sale price is not forced (Baran, 2009, p. 143).

Reference should be made to the principle of the bankrupt enterprise's survival. The principle of preserving a bankrupt enterprise also follows from the content of Article 2 B.L. In the insolvency proceedings, the debtor's enterprise should be preserved, insofar as reasonable reasons allow it. A bankrupt enterprise cannot be run at the expense of reducing the prospects of satisfying creditors. In other words, the trustee cannot run a bankrupt enterprise if such activity is loss-making. If it is more beneficial for creditors, the trustee will sell individual components that are part of the enterprise instead of municipalities selling the enterprise as a whole.

The speed of liquidation proceedings is important. The principle of speed is the rule of all proceedings of economic value. Bankruptcy proceedings, which are aimed at satisfying creditors' claims, should also be conducted quickly. It should be remembered that interest on the claim to the bankrupt for the time after the declaration of bankruptcy cannot be satisfied from the bankruptcy estate (Article 92 section 1 B.L.), subject to the exception referred to in Article 92 section 2 B.L. Creditors in connection with the bankruptcy of the debtor are deprived of compensation for lack of capital. In addition, the liquidation dividend is usually much lower than the nominal value of the debt. From an economic point of view, the speed of obtaining a liquidation dividend is of key importance. In addition, the longer the insolvency proceedings last, the higher the costs it generates. Consequently, it may sometimes be more beneficial to lower the selling price of assets than continuing the bankruptcy proceedings for a longer time. It should be remembered that the sooner the trustee cash the assets of the bankrupt, the lower will be the expenses for protection, maintenance and insurance of the assets included in the estate. It should be added that, pursuant to Article 162 section 5 B.L. the trustee's remuneration is increased to 10% if the final division plan is carried out within a year of the expiry of the deadline for submitting claims or full satisfaction of the second, third and at least half of the fourth category (excluding the period of arrangement bankruptcy proceedings). In practice, there are cases when assets that are part of the insolvency estate become the subject of security in other proceedings. For example, according to Art. 755 sec. 1 (2) of the Code of Civil Procedure if the subject of security of other proceedings is not a monetary claim, the court shall provide security in such a way as it deems appropriate, and in particular, the court may impose a ban on the sale of items or rights covered by the proceedings. *De lege ferenda*, it would be appropriate to prohibit the provision of security in other proceedings regarding the components of the bankrupt's estate.

Another principle is the principle of minimizing decommissioning costs. From the provision of Article 179 B.L. the obligation to "minimize the costs of proceedings" clearly indicates that this means that the trustee should conduct liquidation proceedings with austerity policy.

Finally, the principle of complete liquidation of the components of the estate should be pointed out. In other words, all assets that are part of the insolvency estate should be liquidated. As a rule, the trustee should liquidate all assets. As mentioned earlier, the limit determining the liquidation of the bankruptcy estate is the state of satisfaction of all creditors of the bankrupt. As a rule, the bankruptcy trustee's liquidation

efforts should not lead to the accumulation of more cash than is needed to satisfy creditors. In other words, if the trustee were able to cover all costs of bankruptcy proceedings and satisfy all creditors, and the assets were not liquidated, there is no justification for further liquidation of the remaining components of the estate. Finally, it should be added that the fact that the trustee is able to satisfy all creditors does not mean that the trustee may sell assets below their liquidation value. In other words, the determinant of the sale price of assets included in the estate may not be the sum needed to satisfy creditors, but the actual value of these assets resulting from the assessment. It should be noted that any assets that may remain after the insolvency proceedings are transferred to the bankrupt (Article 364 B.L.).

Establishing a trustee and entrusting them with the right of management for property, as well as the right to dispose of this property, constitutes an exception to the principle of the right to property (Article 140 of the Civil Code). Consequently, it can be argued that the bankrupt, upon the final cessation of insolvency proceedings, has a vindication claim for surrendering the assets remaining after the insolvency proceedings. In addition, creditors of a former bankrupt may satisfy their assets after the bankruptcy proceedings. It should be remembered that in accordance with Art. 263 B.L. refusal to recognize a claim in bankruptcy proceedings (in bankruptcy proceedings, claims are dealt with in a simplified way) does not prevent it from being properly asserted. Recovery of the claim, recognition of which was refused, is possible only after the discontinuation or termination of the bankruptcy proceedings. In addition, in the event of liquidation bankruptcy, in accordance with Art. 92 section 1 B.L., interest on the debt due from the bankrupt may be satisfied from the bankruptcy estate for the period up to the day of declaration of bankruptcy. Consequently, the assets remaining after the bankruptcy proceedings have ended may serve to satisfy interest on claims that could not be satisfied in the bankruptcy proceedings.

##### 5. CIVIL LAW CONTRACT AS A CARRIER OF LIQUIDATION OF THE BANKRUPTCY ESTATE

It should also be noted that the carrier of liquidation of the assets of the bankruptcy estate is not an enforcement action but a civil law contract to which the bankruptcy trustee is a party (who, on their own behalf but on the bankruptcy account of the bankrupt, decides on the right of ownership of the bankrupt) and the buyer of the bankruptcy estate. The "sales contract" is explicitly mentioned in the content of Article 321 section 1 B.L. The civil law agreement under which the trustee sells the assets of the bankruptcy estate is an agreement that is subject to the provisions of the Civil Code relating to the sale agreement (Article 535 of the Civil Code). Nevertheless, account should be taken of the fact that the general principles relating to the sales contract are modified by bankruptcy law. This applies, for example, to the procedure for concluding the contract, but also to its content in relation to the initial acquisition of the components of the estate under this contract (e.g. exclusion of the seller's liability under the warranty). It should be noted that the Vienna Convention on Contracts for the International Sale of Goods does not apply to sales by auction, on execution or otherwise by the authorities of law (Article 2 (b) and (c) of the Convention). It should be assumed that the trustee is "authority of law" within the meaning of this Convention and therefore will not apply to bankruptcy sales. At the same time, the trustee should shape the content of the sales contract in this way - as a party to the civil law relationship - so as not to violate the rules of bankruptcy proceedings (Article 2 B.L.). Some aspects of the contract concluded by the trustee as part of the liquidation of the bankruptcy estate are subject to the mandatory provisions of the Bankruptcy Law Act.



The sales contract is concluded in the form specified in the provisions of civil law. The sales contract (e.g. movable items) may be concluded orally (the trustee issues an invoice and receives prepayment from the buyer). The agreement on the sale of components of the bankruptcy estate also has certain effects in the area of tax law.

## 6. PREPARED LIQUIDATION (PRE-PACK)

The prepared liquidation (pre-pack) is a relatively new legal structure in Polish law (it has been in force since 1 January 2016), which aims to accelerate and simplify the course of bankruptcy proceedings. In this case, the liquidation stage of the bankruptcy estate (within the scope of the liquidation) will not take place separately after the declaration of bankruptcy. An application for the declaration of bankruptcy may be accompanied by an application for approval of the terms of sale of the debtor's enterprise or its organized part or assets constituting a significant part of the enterprise (Brulard & Huevelle, 2011, p. 18; Finch, 2006, p. 568; Frisby, 2007, p. 4; Hoffman, Hrycaj, Kubiczek, Pilitowski, & Tatar, 2017, *passim*; Kaliński, Tatar, & Trela, 2019, p. 119; Moulton, 2005, p. 2; Shuttleworth, 2015, p. 1; Walton, 2006, p. 113). The purpose of this arrangement is to speed up bankruptcy proceedings. At the same time, the scope of future duties of the trustee is reduced in connection with the preparation of liquidation even before the announcement of bankruptcy. In the literature as well as in practice, the pre-pack design raises mixed assessments. From a practical point of view, an economic alternative for negotiation between a debtor and a potential buyer is negotiating a future lease agreement with a potential buyer, however, the conclusion of the lease contract itself falls within the competence of the receiver and requires the consent of the judge-commissioner (Article 316 section 2 B.L.).

The problem of possible abuse of pre-pack has at least two faces. First of all, the provisions of Art. 56a B.L. cannot be a patent for unlawful activities such as "indebt property and buy it without encumbrances". In view of the potential for abuse of pre-pack institutions, special emphasis should be placed on adequate control, which is expressed by: a) description and estimation of the subject of the sale prepared by an expert from the list of court experts (Article 56a section 3 B.L.); b) limited trust in relation to purchasers as related persons (Article 56 b B.L.); c) control of the bankruptcy court of the application for approval of the terms of sale (Article 56c B.L.) d) the possibility for each creditor to lodge a complaint against the order to approve the terms of sale (Article 56d section 2 B.L.);e) the possibility for the trustee to submit an application for repealing or changing the decision on the approval of the terms of sale (Article 56h B.L.).

Second, the pre-pack institution cannot be used by the creditor to a hostile takeover of the debtor's property. The provision of Article 56 section 2 B.L. does not provide for the possibility of challenging the decision on the approval of the bankrupt's terms of sale. To the extent that the legislator does not provide for a complaint against a bankrupt, regulation of Article 56d section 2 B.L. is probably contradictory at least with Article 21 of the Constitution on the protection of property.

The subject of the prepared liquidation can therefore be an enterprise of the bankrupt within the meaning of Art. 55 [1] of the Civil Code, an organized part of a bankrupt enterprise or organized parts of a bankrupt enterprise, assets that constitute a significant part of the enterprise, which do not have the quality of an organized part of the enterprise, whereas the subject of liquidation may also be one asset. The term "a significant part of the enterprise" may refer to the property, technology, etc. criterion. Assets may include, for example, shares or shares in other commercial companies, etc.

According to Article 2 section 1 B.L. the priority should have a pre-pack of the company as a whole. For obvious reasons, the subject of the acquisition may not be shares in possession of the owners of the debtor. The question arises as to whether the subject of liquidation can be assets that do not form part of the enterprise (e.g. assets of a general partnership partner). As it seems, *mutatis mutandis*, the commented provisions can apply to assets that are not part of the enterprise.

The provision of Article 55 [2] of the Civil Code states that the legal act whose object is an enterprise covers everything that is part of an enterprise, unless the legal act or special provisions state otherwise.

In practice, when making a business valuation for pre-pack purposes, special attention should be paid to components with variable amounts, such as materials and utilities for production, production in progress, stocks, etc. It can be suggested that either this type of components on the basis of Article 55 [2] of the Civil Code may be released from the pre-pack transactions and make them the subject of "ordinary" liquidation or determine their quota of releases under the transaction and assess the value of this contingent in the estimate. Handing over of a significant amount of materials, production in progress, inventories disregarding the valuation to the buyer (as a result of Article 55 [2] of the Civil Code) could cause damage in the bankruptcy estate.

The conclusion regarding the liquidation can be submitted simultaneously with the application for bankruptcy, but also later during the proceedings for the declaration of bankruptcy. The regulations do not provide any procedural preclusions in this respect. The debtor and any of their creditors may file a petition regarding the liquidation. Whoever may be the first to file for the bankruptcy of the debtor and someone else for liquidation. The fact that there is a need to submit an application for liquidation does not in any way justify the failure to meet the deadline referred to in Article 21 sec. 1 B.L. One should defend the view that the application for liquidation is autonomous. The formal shortcomings of this application should not result in the return of a full-fledged bankruptcy petition. Examination of the files should lead to establishing whether or not a legislative adjustment which could clarify the applicable provisions is needed in this area.

It is unacceptable to submit an application for approval of the terms of sale in respect of property components covered by a registered pledge if the agreement on establishing a registered pledge provides for taking over the subject of the pledge or its sale pursuant to Art. 24 of the Act on Registered Pledge unless the application is accompanied by a written consent of the pledgee. The provision of Art. 330 B.L. is used accordingly.

The application for approval of the terms of sale shall be accompanied by a description and estimation of the component covered by the application prepared by a person entered in the list of court experts. Unfortunately, neither the specification of the scope of specialization in the Act regarding the entry into the list of experts (it should be assumed that specialization should be adequate to the subject of liquidation) nor the obligation to select transparently the person for the valuation is specified. The literature on the subject aptly claims that the bankruptcy court may also hear the debtor, the creditor - the applicant, the buyer, the expert. The hearing may take the form of receipt of statements in writing.

The application for the approval of the terms of sale must contain the terms of sale by indicating at least the price and the buyer. The terms of sale may be specified in the submitted draft contract to be concluded by the trustee.

First of all, according to Article 56c section 1 B.L. the selling price should be higher than the amount possible to obtain in bankruptcy proceedings upon liquidation on general principles, less the costs of proceedings that should be incurred in connection

with liquidation in such mode. Secondly, the sale price may be close to the amount that can be obtained in bankruptcy proceedings on liquidation under general rules, reduced by the costs of proceedings that should be incurred in connection with liquidation in this mode, if there is an important public interest or the ability to preserve the debtor's enterprise (Article 56c section. 2 B.L.). Finally, the sale price to the entities in a personal or capital relationship closer indicated in Article 128 B.L. cannot be lower than the estimated price (Article 56b section 1 B.L.).

An application for the approval of the terms of sale may provide for the issuing of the business to the buyer from the date of the bankruptcy of the debtor. In this case, the application shall be accompanied by proof of payment of the full price to the court's deposit account. Issuing the buyer's business may also take place at a different date, for example after the bankruptcy order has become final.

It could be assumed that the later a bankrupt enterprise will be sold, the lower the selling price will be. The bankruptcy court grants an application for approval of the terms of sale if the price is higher than the amount that can be obtained in bankruptcy proceedings on liquidation, reduced by the costs of proceedings that should be incurred in connection with liquidation in such mode. However, the bankruptcy court may grant the application if the price is close to the amount that can be obtained in bankruptcy proceedings on liquidation under general rules, less the costs of proceedings that should be incurred in connection with liquidation in this mode, if there is an important public interest or the ability of the debtor's enterprise to be preserved. The legislator does not require the debtor's consent to the liquidation. The consent of the debtor is not, moreover, required when liquidating the assets included in the bankruptcy estate.

Taking into account the application for liquidation is possible only in the event of the bankruptcy of the debtor. The bankruptcy court, having regard to the application for liquidation, decides in the bankruptcy resolution the terms of sale, specifying at least the price and the buyer of the assets being the subject of the sale referred to in this chapter. In the order, the court may also refer to the terms of sale specified in the draft contract.

The ruling of the bankruptcy court rejecting the application for approval of the terms and conditions of sale may be appealed to the applicant, and the order granting the application to each of the creditors. A complaint may be filed within one week of the date of the announcement.

The trustee concludes a sale agreement with a buyer under the conditions specified in the court ruling (conditions may be defined in general terms but the contract form may also constitute an attachment to the ruling) not later than within thirty days from the day this order becomes final unless the terms agreed by the court provided for a different date. This period may be longer or shorter than 30 days. The trustee is in principle related to selecting the buyer, the object of sale, and selling price.

It could be defended an opinion that the trustee may conclude a valid and effective contract also after the deadline specified in the commented provision. The contract should be concluded with respect for general rules regarding the form of legal transactions (e.g. Article 75<sup>1</sup> Sec. 1, 155 Sec. 1 of the Civil Code).

Conclusion of a sales agreement incorporating the disposing effect may take place only after the buyer has paid the whole price to the bankruptcy estate or after the receiver has been given a price previously paid into the deposit. The entire price is the gross price including VAT. Depending on the object of sale referred to in Article 56 a section 1 B.L. the transaction may benefit from the subject VAT exemption.

The sale made as part of the liquidation has consequences of bankruptcy (enforcement) sale. The effects of sales apply to Articles 313, 314 and 317 B.L. depending on the type of the object of sale.

Handing over the buyer's business takes place directly to the buyer's hands, with the trustee's share. The provision of Article 174 B.L. is used accordingly. This means that the introduction of the buyer into the assets of the bankrupt may be made by the bailiff based on the court's decision on the declaration of bankruptcy without the need to obtain the enforcement clause.

Until the terms of sale and conclusion of the sale agreement become valid, the buyer "manages the purchased assets" within the limits of ordinary management at their own risk and responsibility. The legislator used here a bizarre phrase "manages acquired assets" because the scope of the designations of the term "assets" is not identical to the scope of the designations of the term "enterprise" used in the other part of the Act, and the form made is logically inconsistent with the whole regulation. This regulation also raises specific substantive doubts in the taking over of an "economic living" organism, as in question about: a) the right to collect benefits, b) bearing costs, c) "taking over" contracts, d) transfer of a workplace within the meaning of Art. 23 [1] of the Labour Code, etc.

By repealing the decision approving the terms of sale, the court obliges the buyer to return the enterprise to the receiver or the debtor. The decision is a writ of execution against the buyer. Theoretically, in the mode of Article 788 of the Civil Procedure Rules, it is possible to give an enforcement clause against a third party. Irrespective of the debt collection claim, the receiver may, depending on the circumstances, claim for reimbursement or compensation claims.

Once the order approving the terms of sale becomes valid, the court, *ex officio* or at the request of the receiver, decides to issue the price to the receiver with deposit. Secondly, on the issuance of the price, it adjudicates at the request of the buyer of the court within thirty days from the day of handing over the business to the trustee or debtor. The trustee or debtor may submit an application to keep the deposit price for the next two weeks needed to submit an application for securing an action for damages in accordance with general provisions. After this date, the court will immediately decide to issue a deposit price, unless a security application has been submitted.

The trustee may submit an application to the court for annulment or change of the decision approving the terms of sale if after the issuance of the order the terms and conditions of the sale agreement have been changed or circumstances have been disclosed that have a significant impact on the value of the asset being the subject of the sale.

It should be considered admissible, taking into account the nature of the purchase of the property with enforcement effect, to specify in the sales contract that if during the bankruptcy proceedings (or at another date specified in the contract), after signing the contract the circumstances existing before the date of the contract will be disclosed, which have a significant impact on the value of the asset being the subject of the sale, the receiver may demand an appropriate surcharge according to the appraiser's valuation (security clause).

The latest great novelization of Bankruptcy Law Act made confirmation by *expressis verbis* that a prepared liquidation regarding significant assets in consumer bankruptcy is possible; confirmation that pre-pack can be addressed to more than one buyer at a time; confirmation of the admissibility of submitting an application for approval of the terms of sale in the course of bankruptcy proceedings (after filing for bankruptcy), and by each of its participants; enabling the investor to take over management of the sale item more quickly after the court issues its decision in this respect, but before it becomes final; unifying the position of trustee and buyer (investor) by enabling the buyer to submit an application for a change in the resolution on prepared liquidation, when the value of

the subject of sale changes significantly. All of the above-mentioned changes relate to improving the detailed elements of the prepared decommissioning mechanism.<sup>3</sup>

## 7. LIQUIDATION OF THE BANKRUPT ESTATE IN BANKRUPTCY PROCEEDINGS AGAINST NATURAL PERSONS NOT CONDUCTING ECONOMIC ACTIVITY

Consumer bankruptcy has been a part of the legal landscape in Poland since 2008 (Adamus, 2011a, 2019c, 2019b, 2019a). Liquidation of assets in consumer bankruptcy is simplified. The trustee shall notify the creditors and court on the choice of the method of liquidation of real estate and the choice of the method of liquidation of the assets of the bankruptcy estate, whose value indicated in the inventory exceeds five times the average monthly salary in the enterprise sector without payment of awards from profit in the third quarter of the previous year, announced by the President of the Central Statistical Office. In the notification, the trustee indicates the method of liquidation and the minimum price (Article 491<sup>12</sup> B.L.). The trustee may authorize the bankrupt in writing to sell the property belonging to the bankruptcy estate. The power of attorney provisions shall apply accordingly.

## 8. CONCLUSIONS

The regulation regarding the liquidation of a bankruptcy estate is important from the point of view of the key objectives of the bankruptcy proceedings. This article presents the main principles of liquidation performed by the trustee.

Liquidation of the bankruptcy estate should be a compromise between: a) the need to follow transparent procedures and b) the need for flexible sale of the components of the estate.

Regulation of liquidation of the bankruptcy estate is not heterogeneous. In addition to the general procedure, simplified liquidation methods are provided for consumer bankruptcy. In the study, a lot of attention was devoted to the issue of a new institution of prepared liquidation, which is a *novum* in the Polish bankruptcy law. The Polish legislator reacts flexibly to the need to modernize the rules on liquidation of the bankruptcy estate.

Due to the high costs of maintaining assets and protecting them, the faster the liquidation of the bankruptcy estate is, the cheaper are bankruptcy proceedings. The liquidation system is subordinated to the common goal of bankruptcy proceedings: satisfying creditors as fully as possible.

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<sup>3</sup> A project of the bill proposed to introduce Article 317 section 1a of the Act according to which the buyer of the bankrupt enterprise enters into the place of the bankrupt in the rights and obligations arising only from those contracts that were mentioned in the contract of sale of the company. Unless the special provision provides otherwise, the other party to the contract will be able to withdraw from it within 30 days of the date of the notice on the sale of the enterprise, without the right to compensation. This regulation would have made bankruptcy sales more attractive, as the investor would be able to take over the bankrupt's order book. The above project referred to the model adopted in Art. 46 of the Commercial Code of 1934. The provision of Art. 46 Sec. 1 Commercial Code of 1934 stated that "if, at the time of the sale of the enterprise, the contract obliged the seller and the third to provide mutual benefits, the third may terminate the contract for important reasons connected with the change of the person's owner. A declaration of termination must be made within one month of receiving the information on the sale (Article 23)."

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