

# Changes to the corporate governance rules for companies listed on the Warsaw Stock Exchange ("GPW")

On 1 January 2016, new corporate governance rules will come into force for companies listed on the Warsaw stock exchange entitled "Best Practice of GPW Listed Companies 2016" (the "**New Code**"). The New Code generally follows the structure of the regulations currently in force but there are a number of new provisions. It is important to take note of these because not much time remains to comply with them.

Like the current regulations, the New Code remains based on the "comply or explain" principle. However, it is now expected that the GPW will be more proactive in monitoring the level of compliance. As a result, when non-compliance has to be explained, it is recommended that the explanations that are given are both as precise and comprehensive as possible.

Moreover, one must not forget that listed companies are also obliged to report on the implementation of the GPW's corporate governance recommendations in the company's annual report. As of 1 January 2016, the supervisory board will also have to give its opinion on this report.

## Recommendations relating to the management board and the supervisory board

The New Code introduces new mechanisms of actions of management boards and supervisory boards and these seem to be the recommendations the most important from the practical point of view. Firstly, the management board will be obliged to establish an internal division of competences into individual areas of a company's activity and place an outline of such division on the website. Secondly, in a quest for greater pro-activity from the supervisory board, the scope of evaluations and reports which the supervisory board must submit to the shareholders' meeting has been expanded and specified in more detail. A novelty in this respect will be the obligation to present an evaluation of how the company fulfils the disclosure requirements on the application of the corporate governance recommendations as referred in the GPW's rules and the rules on disclosing current and periodic information.

To that extent, the New Code is in step with other changes to regulation, which envisage imposing high administrative sanctions for failure to comply with disclosure requirements by companies not only on individual members of the management board, but also on individual members of the supervisory board.

Furthermore, there is a proposal to limit the freedom of management board members to hold other positions. In particular, the New Code states that the main area of professional activity of a management board member should be the fulfilment of his/her obligations resulting from that position. Holding positions on management boards or supervisory boards of companies outside the listed company's capital group will require the supervisory board's consent.

Furthermore, the recommendation relating to a balanced proportion of men and women in management and supervisory functions has been deleted from the New Code. This recommendation has been replaced by the suggestion of a policy promoting diversity in the composition of a company's governing bodies and its key managers. Apart from the criterion of gender, the diversity policy should also apply to age and education. A company should place the goals of its policy and the manner of its implementation each year on its website. If a company fails to draw up and implement such policy, it should place a relevant explanation on its website.

## Recommendations relating to internal systems and functions

The New Code introduces a section recommending that companies maintain effective control and internal audit systems, a risk management system and a compliance system. While the functioning of such systems in companies is nothing new, the New Code introduces detailed recommendations in this respect and requires the separation within the company's structure of the units responsible for the performance of these functions, along with detailed rules concerning the liability and actions of such units.

Moreover, it should be noted that the chairman of the audit committee will have to fulfil the criteria of independence which apply to certain supervisory board members and resulting from relevant EU regulations.

## Recommendations relating to the shareholders' meeting and relations with shareholders

Changes have also been made with respect to the shareholders' meeting and relations with shareholders. The first recommendation requires the company to strive to convene an ordinary shareholders' meeting as soon as possible after the publication of its annual report.

More detailed recommendations relate to, among other things, changes in the by-laws of shareholders' meeting that should take effect at the earliest as of the next shareholders' meeting. Circumstance when a break in the proceedings of the general meeting is allowed has also been specified.

A significant new provision is the obligation to prepare draft resolutions of shareholders' meeting with a justification that must be included if required to properly inform shareholders. Also any shareholders proposing resolutions will also have to provide justification for them. The New Code does not specify any deadline by which the justification must be sent out, but the assumption is that it should be sent so as to give shareholders sufficient time to take it into account.

Another recommendation also important for management boards is one specifying a 30-day time limit for replying to a shareholder's demand to provide information on the company (and also on refusing to provide information in response to a request).

In the regulations currently in force, there is already a recommendation to split the nominal value of shares, specifying the minimum level of such split at a level so as to avoid a very low unit market value of the shares, which could consequently pose a threat to a correct and reliable valuation of a company listed on the GPW. In the New Code, the minimum level has been set at PLN 0.50. However, in the case of shares with a nominal value below PLN 0.50, companies are not obliged to conduct a consolidation (reverse split), although, if they do decide to do so, then in the light of the New Code it would be preferable for the nominal value to be set above the new threshold.

### Recommendations relating to conflict of interests and transactions with related entities

In this context, the New Code significantly broadens the standard expected from companies. First of all, a company should specify in its internal regulations the criteria and circumstances in which a conflict of interest may arise, as well as the rules on how to proceed in the face of a conflict of interest or the possibility of the occurrence of a conflict. A company's internal regulations must take into account, among other things, how to prevent, identify and solve conflicts of interest, as well as rules on preventing a member of the management board or the supervisory board from participating in the examination of a matter covered or threatened by a conflict of interest.

Detailed recommendations also apply to members of management boards and supervisory boards who must avoid participating in professional or non-professional activity that could give rise to a conflict of interest or adversely affect their reputation as members of a company's bodies. If a conflict of interest arises, they are obliged to disclose it immediately.

Additionally, as part of the high standard of duty of care for a company's affairs, the possibility of recording an objection of a member of the management board or the supervisory board has been introduced, if such member decides that a decision made by that body conflicts with the company's interests.

### Recommendations relating to remuneration

Until now, there was only one recommendation related to remuneration policy, but in the New Code there is an entire chapter dedicated to this issue, which includes numerous detailed recommendations.

The basic recommendation is that companies should have a remuneration policy for at least the members of its bodies and key managers. The remuneration policy should be published and must specify the form, structure and manner of determining remuneration. A report on such policy has to be included in the company's annual report.

A number of the new recommendations could be interpreted in many different ways, such as the recommendation to determine a level of remuneration of the members of the management board, supervisory board and key managers that is sufficient to recruit, retain and motivate people with the competence necessary for the proper management and supervision of the company. The New Code also contains detailed rules on remuneration as follows:

- the level of remuneration should depend on the actual, long-term financial standing of the company,
- the period between the allocation of options or other instruments linked to the company's shares under the incentive scheme and when they can be exercised should be no less than two years, and
- the remuneration of the members of the supervisory board must not depend on options or other derivatives.

### Recommendations relating to the information policy and communication with investors

A significant change with respect to a company's information policy is that companies no longer have to have a website in the GPW's domain (although each company must have its own website). There is also a limitation on the recommendation to administer the website in English for companies qualified for the WIG20 or the mWIG40 indices and companies outside those indices, if their shareholding structure and scope of activity conducted warrants this. This regulation should be beneficial primarily for small companies or companies making their debut on the GPW. Many larger companies will probably choose to continue to

maintain a website in English for investor relationship purposes.

As with the present regulation, the New Code lists the information that must be placed on the company's own website. The new list has been expanded to include, among other things:

- information on the company's shareholding structure, together with the names of shareholders holding at least 5% of the votes in the company;
- materials concerning the company's strategy, financial results, a summary of financial data and financial forecasts; and
- details of persons responsible for communicating with investors.

The current regulations impose two specific obligations on a company as follow:

- firstly, to react if it considers false information has been disseminated concerning that company; and
- to disclose when it is acting as a sponsor or conducting charitable activity.

A third more general obligation is added by the New Rules whereby investors and analysts can ask questions about anything relevant to the company, which the company must respond to, subject to certain limited exceptions.

## Conclusion

Summing up, the New Code, although it does not break with existing corporate governance practice nevertheless introduces significant changes which companies should address in accordance with the "comply or explain" principle.

The biggest drawback of the New Code seems to be lack of specificity in its provisions leaving considerable room for interpretation. Currently, the GPW is working on a handbook explaining the specific recommendations and principles and is also preparing technical solutions aimed to help companies fulfil the disclosure obligations resulting from the New Code. However, it is impossible to predict when these materials will be available and therefore implementation of the New Code should not be delayed pending their publication.

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