

## THE EVOLUTION OF CORPORATE MANAGEMENT - A MIXED SYSTEM?<sup>1</sup>

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### **Abstract**

There are two systems of corporate governance typically employed worldwide: monistic and dualistic. Traditionally, in some Central and Eastern European countries, the dualistic approach has been dominant, requiring a strict separation of the executive and supervisory bodies. In the last few years, in a movement that can be considered an intra-European legal convergence, there have been various corporate legislation reforms. This article is devoted to analyzing the results of those reforms, and they have, in fact, created in hitherto traditionally dualistic systems the legal possibility of transitioning to a monistic system. While the dualist system has not been totally abandoned, an alternative option of organ formation has been introduced in selected companies, modelled on certain case law jurisdictions. The article thus shows the evolution and reasons for such a process and assess its effectiveness. The article does not, in principle, analyse the traditional Western European legal systems, where the issues in question have been discussed for years in a theoretical context. Instead, it focuses on new legislation in Poland and Ukraine, two countries which have recently made very significant changes to their legal frameworks. This approach makes it possible to highlight the latest European trends. In the article, reference is made to a number of arguments supporting the introduced mixed system, while simultaneously rejecting the previous view that legislation must adopt either a single-tier or a two-tier system. This therefore relates to the private nature of companies, the freedom to shape their internal relations, and the experiences of European companies.

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## **Introduction**

In general, there are two systems of corporate governance typically employed worldwide: monistic and dualistic. Without going into unnecessary detail, monistic essentially refers to a system with a single authority which governs, represents and oversees, while the dualistic system means that these functions are split into two bodies in which one governs and represents, while the second body supervises (Szumański, 2015, p. 497). Traditionally, in some Central and Eastern European countries connected with the German legal tradition, the dualistic approach has been dominant, requiring the strict separation of the executive and supervisory board (Ibid. p. 497). Sometimes, depending on the type of company, e.g. in limited liability companies, it was possible, under certain conditions, not to appoint a supervisory board or an audit committee (§ 1 article 213 and § 2 article 213, Commercial Companies Code, 2020). Nevertheless, even then, the supervisory function was carried out by shareholders and not by a separate part of the executive body (Ibid., § 1 article 212).

However, in recent years, corporate law reforms have taken place, resulting in intra-European legal convergence. While the dualistic system has not been abandoned, an alternative has been introduced in some companies, modelled on the approach adopted in certain common law jurisdictions. Within a single legal system, the freedom to form corporate bodies has therefore been bolstered. This article shows the evolution and reasons for this process and assesses its effectiveness. In particular, an amendment to the Polish Commercial Companies Code (CCC) and selected provisions of the new Law of Ukraine on Joint-Stock Companies will serve as a reference point for the wider arguments advanced. In addition, this article addresses a more profound question as to whether or not there is any point in maintaining an exclusively monistic or dualistic approach to corporate management in national legislation.

## **Polish and Ukrainian Commercial Law from a European Perspective**

In civil continental legal systems, which includes Poland, (David, 1989, p. 159), it is generally accepted that a basic division can be made between different branches, or more accurately, “fields”, of law, such as civil law, criminal law or administrative law. Some scholarly debates in the past focused on discussions about the boundaries that delineate these fields (Ibid. pp. 89-90), i.e. taxonomisation. These laws consist of many, to a certain extent, autonomous parts, with their own methods, principles, rules and legislation

(acts, bills and codes) (Ibid. pp. 89-90). The situation in Ukraine is similar as regards the law and doctrine, and one can even find a greater level of intensity in the debate concerning the proper place of corporate law or, more broadly, civil and economic law (Turłukowski, 2008, pp. 77-89). Ukrainian legal doctrine has inherited the debate over the existence of so-called economic law from Soviet doctrine, which should be seen as an attempt to combine elements of private and public law, and which would lead to the marginalisation of private law principles (Ioffe, 1983, pp. 51-52; Bowring, 2013, p. 54). In Ukrainian law, one of the most far-reaching consequences of this approach has been the enactment of a separate economic code alongside the civil code (Economic Code of Ukraine, 2003, p. 144).

At present in Poland, commercial law is quite clearly a part of civil law. There are a number of practical implications that arise from this. In comparison with other countries, Poland has no commercial code, but only a code of commercial companies. This makes a lot of practical sense and it is not just a matter of a formal change of nomenclature. After declaring independence in 1918, Poland was wholly under the influence of the European idea of commercial law as an independent field regulating the establishment, organization, functioning, winding-up, merger, division, and transformation of commercial companies, as well as the execution of commercial contracts and the status of enterprises, etc (Jastrzębski, 2019, p. 25). Practically speaking, the existing rules of civil law could not be applied to commercial relationships according to such an idea.

The first attempt at a doctrinal approach was the First Polish Commercial Code, which was introduced in 1934 (Code of Commerce, 1934). After the Second World War and the start of the socialist transformation of classical commercial relationships in Europe, its importance was severely restricted or it was even forbidden (Włodyka, 2009, pp. 21-22). However, during this period of socialism in Poland, part of the commercial code was in force (Ibid. p. 6). The real resurrection of commercial law, however, took place after 1989, which is the year that the socialist system was overturned (Wyrozumska, 2005, p. 7). The old Commercial Code remained in force for several years (Code of Commerce, 1934), but from the 1<sup>st</sup> of January 2001, a new code was in effect.

Poland has no commercial code, but only a code of commercial companies. This reflects the dominance of the idea of the unity of civil law. This means that civil law should apply to commercial relationships. This is a reference to the common, or general, first part of the civil code of Poland. The Polish civil code was adopted in 1964 (Civil Code of Poland, 1964). In comparison with other countries from the former Eastern Bloc, the Polish regime was not influenced very deeply by the socialist concept. In 1990, during the widespread reform of the civil code, major changes were made to the core institutions of socialism in order to transition to a market-oriented system (Civil Code of Poland, 1990). At the same time, neither the structure nor the majority of its provisions were reformed. This is the best evidence that Poland's civil code cannot be regarded as a typical product of a socialist system, but instead

that it is an expression of true private law. After the Second World War, despite the implementation of various socialist policies, the codifiers of the new law relied on materials which had been produced by codification commissions before the start of the war.

The situation was fundamentally different in the former Soviet republics, where there were civil codes in force that contained regulations distorted by socialist nationalisation and the notion that classical private institutions should be restricted (Makovsky, 2010, p. 281). This explains the replacement of the old codes with new ones, as occurred, for example, in Ukraine in 2004. Of course, selected provisions concerning company law found their way into the new Civil Code of Ukraine, e.g. norms relating to partnerships and companies. This came into effect in January 2004 following a long period of reform and new economic realities: a completely new code was established to regulate relations under free market conditions.

At present in Poland, there are regular discussions regarding the merits of recodifying the civil law (Radwański, 2006; Stec & Załucki, 2015) but, because the need for a new code is not universally perceived, these discussions are unlikely to lead to new laws. Despite this, the now defunct civil law commission proposed a series of reforms which were never implemented (Flisek, 2009). It may be that, in ten years, Poland will create a new civil code, but a more active debate on this topic has not yet started. The composition of the Polish civil code is simpler than most modern civil codifications in Europe. This was typical of Socialist legal codes, not including family law and private international law. There are only four so-called 'books' in the Polish civil code: General provisions, Ownership and other Real Rights, Obligations, and Succession law.

Another reason why it is still possible to successfully apply the civil code is that there was practically no regulation of commercial companies from the day that it was adopted. Instead, a regulation that could be applied was found in the old commercial law (Code of Commerce, 1934). The easiest way for Poland to revert to a classical market economy was to adopt a separate regime regulating company law without changing the civil code. This emerged from a consensus that a new partnership and company legal framework was needed during the period of reform and this approach was thus prioritized.

In this way, the idea of the unity of the civil law is not only a theoretical idea but a notion that has had a real influence on how the provisions of the Company Code are interpreted. For instance, according to Art. 2 of the Commercial Companies Code, all matters set out in the code which are not regulated by it are governed by the provisions of the Civil Code. Hence, where the nature of the legal relationship of a commercial company so requires, the provisions of the Civil Code apply accordingly (Commercial Companies Code, 2020). Commercial law consists not only of the Companies Code but also of many other acts adopted by Parliament such as the Act on Freedom to Conduct Business (Freedom of Economic Activity Act, 2004). The Company Code can be regarded only as a single, albeit significant, component of the field of company law and not as the entirety of commercial law.

The Ukrainian legal position was incomparable, since after the collapse of the Russian Empire in 1917, and despite strenuous efforts and military sacrifices, the independence of the Ukrainian state could not be preserved (Shemshuchenko, 2004, pp. 191-192). Instead, most Ukrainian territory fell within the borders of the Soviet state. Although it was still possible to find provisions regulating commercial companies in the first civil code of Soviet Ukraine (Civil Code of USSR, 1923) by the early 1930s, centralisation and widespread nationalisation had taken hold, leading to the wholesale repeal of any and all commercial relationships (Belyanovich, 2002, p. 11). Ukraine did not have the tradition of a separate Commercial Code or Commercial Companies Code. As such, it is only possible to speak of a revival of company law from the late 1980s onwards (Turłukowski, 2008, pp. 61-62). Correspondingly, company code reforms took place primarily on the basis of individual laws newly enacted after 1991, all of which was followed by the incorporation of some company regulations into the new Civil Code of Ukraine (article 1264, Civil Code of Ukraine, 2003). In addition, the foundation of the commercial company code comprises several specific provisions on individual types of companies (article 682, Law of Ukraine on Business Associations, 1991). The new Law of Ukraine on joint-stock companies became effective on 1<sup>st</sup> January 2023 (Law of Ukraine on Joint Stock Companies, 2022).

### **Companies versus Partnerships**

There is a clear division between the regulation of companies and partnerships both in Polish and Ukrainian law. In Polish law, partnerships do not have any legal personality. Polish law, alongside physical and legal persons, has a third category - the quasi-legal person (Lewandowski, 2007, p. 35). All partnerships are quasi-legal persons. In their own name they may acquire rights, including the ownership of real property and other property rights, assume obligations, and sue or be sued. (Lic, 2013, pp. 9-12). Interestingly, Ukrainian law does not recognise a third category at all and adheres to a rather rigid dichotomy, i.e. the division between natural and legal persons, with the exception of business owners who can register without legal personhood. Accordingly, under Ukrainian law, both companies and partnerships have the status of independent legal persons.

From the civil law perspective, there are no fundamental differences between a legal person and a quasi-legal person. A clearer line of division can be found in Polish tax law. The tax rate payable depends on one's legal status. Theoretically, a legal person can act through their specific organs. Thus, a quasi-legal person, as a rule, has no particular organ that can bind them to legal commitments, such as a management board. In partnerships, the decision making can be more relaxed without the formality of a management board. For example, a resolution can be passed either formally or by normal communication channels such as email.

Apart from a few permitted exceptions, every Polish company has the following authorities which are separate from the shareholders:

- A management board
- General meeting
- A supervisory board/an auditors' committee (Lewandowski, 2007, pp. 53-55, pp. 58-62)

These authorities are specifically mandated separate bodies, each with a defined role in respect of the company. Shareholder meetings should be regarded as a separate organ of the entity, even if it has only one shareholder (§ 1 article 173, Commercial Companies Code, 2000). Naturally, a shareholder meeting consists of the shareholders, but it is convened by special rules which are based on the voting rights of the shareholders. The law does not provide for a “meeting of the partners” in such cases. “The running of the external and internal affairs of the general partnership is in the hands of all partners. As a general rule, each partner has the right to represent the general partnership in relation to third parties and to manage internal business affairs” (Lewandowski, 2007, p. 36). On the other hand, members of the management board may be appointed and removed by a resolution of the shareholders (§ 4 article 201 and § 3 article 300<sup>62</sup>, Commercial Companies Code, 2000). In this way, there is clearly a close relationship between the relevant organs with the power to bind the company. As a rule, partnerships do not have a set of organs that are distinct from the partnership and which may commit it to certain actions or take decisions on its behalf. For instance, according to Polish law, in a registered partnership (Ibid., § 1 article 25<sup>1</sup>), each partner has the right to represent the partnership (Ibid., § 1 article 29). A partnership deed may provide that a partner has been deprived of this right to represent the partnership, but it is forbidden to disentitle a partner from representing the partnership. There are also some exceptions to the rules described above. Although it is, formally speaking, not a company, a limited joint-stock partnership has the power to appoint a supervisory board and a general meeting of shareholders is obligatory (Ibid., § 1 article 142 and article 145).

There are other features that enable a distinction to be drawn between companies and partnerships which are less important for the purposes of the present study. Nevertheless, they are significant for the preservation of the distinction between the two. It is also important to distinguish the responsibilities of shareholders and partners in respect of the obligations of the company and the partnership. Commonly, each partner is personally liable for the obligations of the partnership without limitation with all his assets jointly and severally with the remaining partners and the partnership (Ibid., § 2 article 22). However, in each type of partnership, there are some modifications of, or exceptions to, this rule. For instance, a partner at a professional partnership is not liable for the partnership's obligations arising in connection with the practicing of a freelance profession within the partnership by the remaining partners, or for obligations that the partnership has resulting from actions or omissions of persons employed by the partnership under an employment

contract or on the basis of a different legal relationship, if those persons reported to another partner when performing services related to the activities of the partnership (Ibid., § 1 article 95).

At a limited partnership, a limited partner is liable for the partnership's obligations towards its creditors only up to the limited liability amount (Ibid., article 111).

At a limited joint-stock partnership, a shareholder is not liable for the obligations of the partnership (Ibid., article 135). However, in a joint-stock partnership, at least one partner (general partner) bears unlimited liability towards creditors for the obligations of the partnership and at least one partner must be a shareholder (Ibid., article 125).

An additional point must be mentioned at this juncture, and that is the profound difference between a partnership and a company with regard to the treatment of property. A partnership does not have share capital. As such, a partnership in Poland has no shareholders but instead, it has partners or members; "Partners are the essence of a partnership. Usually there are only a few of them [...] The activity of a partnership is based on the trust partners have in each other because the interests of a partnership are identical with the interests of its partners." (Wyrozumska, 2005, pp. 250-251) A partnership only has its own assets and liabilities, but the partners are obliged to contribute some assets to the property of the partnership (article 25, Commercial Companies Code, 2000). Despite the fact that a partnership does not have share capital, each partner is required to pledge at least some symbolic asset. According to the Company Code, there is no fixed or specific amount for a partner to contribute. But bearing in mind the partners' unlimited personal responsibility for the partnership's debts, it is not too important whether the partnership has enough assets to cover all of its obligations or not.

Under Polish law, a company always has share capital. For instance, according to Art. 153 of the Company Code, the share capital of a limited liability company is divided into shares of equal or unequal nominal values (Ibid., article 153). The share capital of a joint-stock company is divided into shares of equal nominal values (Ibid., article 302). There are currently ongoing debates between different European legal schools (including Poland) about whether there is any need for radical reform of the institution of share capital as an instrument to incentivise greater investment in companies, and particularly in the case of limited liability companies (Żurek, 2018). The main problem requiring reform is the fact that the system does not effectively protect creditors. This is because there is no correlation between share capital levels and liability. In Europe, the influence of the German concept of the institution of share capital became the foundation that supported the whole idea and regulation of the company. The German concept is based on the idea that shareholders pledge their assets to the company and create share capital and they are freed from liability as shareholder capital becomes the sole guarantee to creditors. The common law system, however, is based on different rules and includes a mechanism for protecting creditors. Practically speaking, it is mainly the influence of common law concepts that should be seen as one of the main

reasons for the current change in thinking regarding the role of share capital. A simple joint-stock company is the first domestic shareholding company under Polish law that does not use the idea of share capital and enables a single board of directors to commit and bind the company, thus replacing the management and supervisory bodies.

A similar situation exists in Ukrainian law, in which also exists the traditional division between partnerships and companies. As indicated above, all companies are legal entities, whether they are general partnerships, limited partnerships, or limited liability companies, additional liability companies or joint-stock companies (article 83, Civil Code of Ukraine, 2003). It should be stressed that the proportions of commercial companies operating in the Ukrainian market vary greatly. There is a relatively small number of limited partnerships (367), additional liability companies (1,504) and general partnerships (1,289), in comparison with the dominant limited liability companies (761,776) and joint-stock companies (7,177) (State Statistics Service of Ukraine, 2023). Limited liability companies are the main form of business vehicle for larger private entities both in terms of the total number of companies and in terms of value. This state of affairs is reflected in legislation, since, in addition to the Modern Civil Code of Ukraine, which entered into force on 1<sup>st</sup> January 2004 and which regulates the functioning of partnerships, the Law of 19<sup>th</sup> September 1991 on Economic Incorporations (Law of Ukraine on Business Associations, 1991) is still in force. The 1991 Law also regulates partnerships but not those companies with limited or additional liability. The above-mentioned Act of 1991 is not of high legislative quality. Its passage was hurried and reflected the immaturity of the new system. It should be considered a transformational piece of legislation, one of many that were passed after the fall of Communism. These laws admittedly played an exceptional role during the formation of market legislation, after the demise of the planned economy era. Despite its positive historical significance, it is clear that the current law lags far behind contemporary market realities. The fact that this law is still currently in force might therefore be considered anachronistic (Dovgert, 2000, pp. 142-143). Nevertheless, with the enactment of the new Civil Code, legislators apparently did not consider such a state of affairs as requiring intervention. Perhaps it was thought that the small number of partnerships in the market was relatively stable, being unlikely to grow, and thus did not require urgent reformulation of the law. Therefore, further discussion will focus on how companies are structured and operate through their distinctive organs.

### **The Polish Dualistic Example**

As stated above, both Polish and Ukrainian legislation regulate limited liability companies, which are the most popular type of company chosen by the business community (State Statistics Service of Ukraine, n.d.). The structure of the separate and distinct organs of a Polish limited liability company and a joint-stock company registered under Polish legislation are very similar. The most significant difference in the structure relates to supervisory bodies, which will

be discussed below. It is clear that Polish legislation, with regard to both limited liability companies and joint-stock companies, was constructed to ensure a clear separation of the executive and supervisory spheres. Thus, both of these types of companies are obliged to have a management board that runs and represents the company as a mandatory organ with the power to represent the company. According to § 1-2 art. 201 of the CCC, “the management board shall manage the affairs of the company and represent the company. The management board shall include one or more members” (Commercial Companies Code, 2000). There is an identical provision in § 1-2 of Article 368 of the CCC with regard to the management board of a Polish joint-stock company. In Polish law, the principle of the presumption of competence of the management board is widely accepted, i.e. the management board has the power to commit the company in all respects unless this has been expressly reserved for another body (Ibid., § 1 article 227 and article 393). The shareholder meeting in a limited liability company, and the general meeting consisting of the stockholders in a joint-stock company, are separate organs with similar powers. Traditionally in Polish company law, the share capital of a limited liability company is divided into shares, but the share capital of a joint-stock company is divided into stocks. The legal position of the supervisory authority in a joint-stock company is quite clear - irrespective of the stockholders or the size of the business, a supervisory board must be appointed (Ibid., article 381). The situation with supervision is more complex in the case of a limited liability company. The Polish legislature, provided three possibilities for the company's participants: “The articles of association may create a supervisory board or an audit committee or both. The supervisory board or the audit committee shall be created where the company's share capital exceeds 500,000 zlotys and where there are more than twenty-five shareholders” (Ibid., § 1-2 article 213). In other words, a supervisory authority, or two may be established in any situation, whether required by law or not (it depends on the specifics of each company). According to Polish legislation, it's possible to create both a supervisory board and an audit committee. For instance, a supervisory board and an audit committee could have practically the same range of obligations and separately apply the same instruments of control because of considerations of the obligations among groups of shareholders. The shareholders may want to have reporting about company issues from two separate sources. At the same time, in a company's constitution, there could be a division between the duties of the audit committee and the supervisory board. If the aforementioned prerequisites are satisfied, there should be at least one supervisory authority, e.g. a supervisory board, which in practice is the most popular solution in Poland. The second option would be an auditing committee. On the other hand, if the statutory requirements are not fulfilled, a supervisory authority may not be established, which absolutely does not mean that there is no control over the management board's actions. There are three possibilities here: a supervisory board can be established at any time out of necessity; it can be established when and as the law prescribes; and it can be forgone and never established. In the latter situation, it is obvious that the right to supervise

belongs to the shareholders of a limited liability company. In any case, even if supervisory bodies are established, the shareholders do not automatically lose the right of individual supervision. If a supervisory board is established, the right of individuals to supervise could be curtailed according to art. 213 of the CCC. Having said that, § 3 Article 213 of the CCC stipulates that “If a supervisory board or an audit committee are created, the articles of association may exclude or limit the exercise of individual oversight by the shareholders” (Ibid., article 213). In parallel with the existence of an expanded supervisory body, there is nothing to prevent shareholders from retaining their individual supervisory powers, which could lead to corporate conflicts. This power is given by the code despite the presence of the supervisory board unless it is specifically limited in the corporation’s own governing documents. It should be stressed that any modification of rights (e.g. the addition of further powers to the supervisory board) which would reduce the powers of the management board, is of course possible, but on the condition that it does not disturb the fundamental structure of the company. In the constitution of a particular limited liability company, there may be deferential references to the powers of the controlling bodies, which effectively means that the shareholders have accepted the model proposed by the legislature. Where corporate constitutions do not craft their own rules, they default to the standard in the code. On the other hand, even with far-reaching modifications of the powers and relations between the bodies, the structure remains more or less standard because only the authorities prescribed in the code can be used. At this point, the question arises as to what arguments can be made in favour of a dualistic model when the code already provides flexibility.

The advantage of such a system lies in the independence of the supervisory authority and the possibility of bringing representatives of various groups of owners of shares or stocks into this organ of the company. There are several mechanisms, whether formalised in legislation or not, which can lead to the interests of various groups of share or stock owners being taken into account whereby they elect “their own” representatives to a supervisory authority. Even if the management board is loyal to a majority of the shareholders, some of the members of the supervisory authority can be elected by minority shareholders thanks to a compromise. Of the formal mechanisms enabling this, the so-called “election of members of the supervisory board of a public limited company by groups” can be cited as an example: At the shareholders’ general meeting, the persons representing the portion of shares (in terms of the division of the total number of the represented shares by the number of members of the board) may create a separate group for the purpose of electing one member of the board, and must not participate in the election of the remaining members. According to the law, the board of directors are not subordinate to the supervisory authorities. The supervisory authorities have oversight powers that must be respected by the members of the management board. The existence of two separate bodies allows a distance to be maintained and lowers the risk of personal links between members of the management board and members of the supervisory authorities. This allows, for example,

better supervision of the management board's actions where there is a majority shareholder with a large shareholding block. Besides, there is also the autonomy of the management board (even in relation to shareholders or stockholders), for example, in terms of incurring liability (not only civil but also criminal) for not filing a bankruptcy motion on time (Ibid., article 299 and article 483). In many situations, a board member may have to make their own decisions in order to avoid future personal liability to the company's creditors or criminal liability, despite the position of shareholders or stockholders. Other arguments can be brought to bear in support of the separation of the functions of management of the company from the supervisory function, such as the effectiveness of such a division for economic reasons.

However, the independence of these bodies is a mere fiction when the ownership body is dominant, e.g. when both the management board and the supervisory bodies simply execute the will of the shareholders. In Polish law, a shareholder may also be a member of the management board, in which case their oversight by the supervisory board (appointed at the shareholder meeting) may be illusory. This is particularly evident in the case of so-called municipal companies, where all existing bodies carry out the will of the municipal entity since 100% of the shares belong to the municipality. These companies are public bodies but they abide by the CCC for the purposes of corporate governance.

### **Simple joint-stock companies under Polish law and Ukrainian joint-stock companies as an example of a mixed system**

The new Law of Ukraine on joint-stock companies became effective on 1 January 2023 (Law of Ukraine on Business Associations, 2022). It introduced far-reaching changes into company law relative to both the socialist period and also the later solutions of the first decade of the 2000s. It is a rather large piece of legislation, but even a superficial analysis shows that according to Part 1, Article 4, the governance structure of a company can have one or two tiers (Ibid.,). This means that the founders of a joint-stock company can decide for themselves which model to adopt. This mirrors the similar choice available when selecting what type of joint-stock company it should be - private or public (Ibid., article 6). The choice can only be made in accordance with the solutions proposed by the legislature. In certain situations, the law may mandate the use of one or the other management system (this does not apply to private companies in general (Ibid., article 4). It follows from Part 2, Article 4 that with a single-tier structure, the governing bodies are the general meeting and the board of directors, which may include executive and non-executive directors. The board of directors is merely a group of individuals entrusted with oversight and governance (Ibid., article 4). Moreover, with a monistic structure, there can be an even greater simplification of the structure when it comes to a private joint-stock company. If such a company has no more than 10 shareholders, a single executive may be appointed instead of a board of directors. A rather interesting point that may give rise to controversy is contained in Section 10 of

the Act, which is devoted to the one-person executive body, which carries out the management of the day-to-day business of the company (Ibid.). However, it is additionally stated in the second sentence of Part 1 of Article 81 that the executive body is responsible for all matters relating to the company's day-to-day business unless this has been reserved for the general meeting or the supervisory board. This somewhat ambiguous statement creates the misleading impression that if a one-person executive is appointed, the single-tier structure is abandoned and a supervisory board ought to be appointed. Such an approach appears to be erroneous, since the appointment of a one-person body can take place instead of a supervisory board. In this context, it is interesting that legislation regulating Ukrainian joint-stock companies permits a situation where there is a one-person organ in the company (regardless of the number of shareholders), which is effectively the management board and is overseen by the supervisory board. This does not mean, however, that a single individual cannot fulfill this function in a monistic structure and, of course, this does not require the appointment of any supervisory bodies. Nevertheless, the legislation is fairly new, so controversies in case law may well arise. As for the situation in a classic single-tier structure, functions related to the day-to-day operations of a joint-stock company are carried out by executive directors, while functions related to risk management and control over the entire company are carried out entirely by non-executive directors (Ibid., article 4). Permanent or temporary committees may be set up within the board of directors (Ibid., article 68).

In the case of a two-tier structure, the organs of a joint-stock company with the authority to commit the company legally are: the general meeting (Ibid., article 4), the supervisory board, and the executive body, whether collegial (more than one person) or single-member. Such a system provides for a clear division between operational activities and the internal oversight function carried out by the supervisory board. Such a structure is similar to the system applicable in the case of a Polish limited liability company or joint-stock company. The law may impose restrictions (Ibid., article 4), but in general, a joint-stock company with a single-tier structure may convert to a two-tier structure and vice versa. Deciding to change the structure is not regarded as a reorganisation or transformation of the company (Ibid., article 4). Transformation would require a change in company type.

Comparable solutions have been adopted in Poland in respect of the most recent version of the joint-stock company. A simple joint-stock company is the first type of domestic company that does not apply the idea of share capital (instead of that, new joint stock capital was established) and allows the possibility of appointing only a board of directors without a management and supervisory bodies. Such a possibility has only existed in Polish legislation since 1<sup>st</sup> July 2021, when the Commercial Companies Code was amended (Act amending the Commercial Companies Code and certain other acts, 2019), and a third shareholding company appeared in legislation alongside the existing two varieties. It follows from § 1 - 2 of Article 300 of the Commercial Companies Code (Ibid.) that either a management board or a board of directors is established in a company. The company's constitution may provide that, in

addition to the establishment of a management board, a supervisory board must also be set up. Accordingly, the company's founders have the power to decide which model of company governance is more suitable for them. If the traditional management board is selected, a supervisory board may be established. In the case of the simple joint-stock company, unlike the Polish limited liability company, legislators have not laid out any requirements according to which a supervisory board must be established. In any case, it is exclusively an independent decision of the company's stakeholders (§ 1-2 of article 300<sup>68</sup>, Commercial Companies Code, 2020). The supervisory board must consist of at least three members, appointed and removed by a resolution of the shareholders, although the corporate constitution may provide for a different method of appointment or removal of supervisory board members (Ibid., § 1-2 of article 300<sup>69</sup>). One of the most important features of this dualistic system is that the supervisory board, despite overseeing the activities of a simple joint-stock company, does not have the right or obligation to give binding instructions to the management board regarding how to conduct the company's business. This is explicitly stated in the legislation (Ibid., § 1-2 of article 300<sup>69</sup>). Of course, after the supervisory board has carried out a review of the activities of the management board, the management board may adjust how the company's affairs are carried out in the future but only after a general meeting of the simple joint-stock company has passed appropriate resolutions.

If the stakeholders in the company opt for the monistic model, a board of directors must be appointed to manage the company's affairs, represent the company and supervise the company's affairs. The board of directors consists of one or more directors (Ibid., § 1-2 of article 300<sup>73</sup>). This approach allows great flexibility, as it is possible to set up an elaborate structure with several directors in charge of the day-to-day management and representation of the company, while the board of directors operates as a one-person board, enabling all of the functions to be concentrated in the hands of one individual (Polish law only allows natural persons to be appointed to boards or management boards, but shareholders are not so restricted and can also be legal persons (Ibid., article 18). Obviously, in the case of a one-person board of directors, it is difficult to say that this one natural person exercises control over themselves when they represent the company or fulfill a management role. This may give rise to increased risks of self supervision for a simple joint-stock company, but this is counterbalanced by the broad powers of the shareholders, who not only appoint and remove the directors but may, for valid reasons, suspend by resolution any member of the board of directors (Ibid., article 300<sup>73</sup>). In any case, a director may be removed at any time without stating reasons, which of course does not deprive them of any legal claims they may have as part of the employment relationship or their directorship position in general (Ibid., article 300<sup>74</sup>). In smaller companies which are set up, for example, with the sole purpose of developing a new, innovative product (e.g. as a start-up), it may be neither economically necessary, nor financially feasible, to maintain a supervisory board consisting of several members. In the case of the personal involvement of shareholders in the company's work (which is possible in the

case of a simple joint-stock company), the problem of there being a complete lack of control over the sole member of the board of directors is likely to be a marginal one. When the board of directors is composed of more than one director, the principle of collegiality in the conduct of the company's affairs applies, although this can be changed in the company's constitution or in the rules governing the board of directors. In common law jurisdictions, the institution of a board of directors enables a division between executive and non-executive directors (Lewandowski, 2021). Non-executive directors exercise permanent supervision over the running of the company's affairs, while executive directors run the company's business (article 300<sup>76</sup>, Commercial Companies Code, 2020). It should be noted that it is possible to set up further, more complex structures within the context of the board of directors. For example, an executive committee made up exclusively of executive directors may be established. Likewise, a committee composed of non-executive directors may be set up to exercise ongoing supervision of the company (Ibid., article 300<sup>76</sup>). Although it is not possible to speak of any administrative subordination of particular directors to others, the non-executive directors clearly are equipped with various powers to exercise effective control over the activities of the executive directors. Those powers include requesting access to documents, demanding explanations, and other formal actions (Ibid., article 300<sup>76</sup>). The legislature has endowed company founders with a great deal of freedom, not only in terms of the choice of the company's governance model, but also in terms of shaping the content of the various organs of the company once such a choice has been made. Depending on the company's line of business, and despite making an identical decision to appoint a board of directors, in two particular companies one may find two completely different situations. In one, there may be a single-person board of directors, while in the other there may be a board of directors with an extensive structure and internal committees and legislation governing that structure.

### **Evaluation of the current solutions**

The few selected examples given above clearly show that there has been a shift away from the absolute dominance of the dualistic system. Instead, there is a mixed system, offering a choice. For a number of years, it has been suggested that the Polish rules governing the principles of representation should be modernized to allow for a monistic management system in capital companies, in addition to the existing dualistic system consisting of a management board and a supervisory board (Sołtysiński, 2015, p. X). However, there has never been any intention to eliminate the dualistic system and fully replace it with a monistic one.

For many European continental legal systems, the introduction of the European company was the inspiration for such changes. It is clear that a European company is not, by definition, a domestic company, one registered under Polish law and regulated by the Commercial Companies Code. The European company came into being primarily as a product of European

legislation (Council of the European Union, 2001a; Council of the European Union, 2001b). The main idea behind the *Societas Europaea* (SE, Latin for a ‘European company’) is supranationality and the ability to solve some of the existing cross-border problems of enterprises within the European Union (Bilewska, 2006, p. 17). There is also no doubt that “in principle, the legal form of the SE should primarily serve to facilitate cross-border mergers and to facilitate the creation of international group structures” (Sokołowski, 2003, p. 10). Nevertheless, despite its lack of popularity in practice, it is now part of the legislation in EU member states. Pursuant to Article 38 of Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company, an SE’s management organs shall comprise:

- (a) a general meeting of shareholders and
- (b) either a supervisory organ and a management organ (two-tier system) or an administrative organ (single-tier system) depending on the form adopted in the statutes (Council of the European Union, 2001a).

It has been rightly pointed out that the 2001 statute, while regulating the monistic system, did not introduce an EU-wide name for the company’s organ, but instead used the term ‘administrative body’. As such, this caused certain terminological difficulties in legal systems such as Poland and Germany where the monistic system was unknown (Bilewska, 2006, pp. 184-185). In the end, the body was called the ‘administrative council’ in Polish domestic law (article 24, European Company and European Economic Interest Grouping Act, 2005) to resolve the initial misunderstanding.

Taking into account the influence of European legislation and the evolution of national practices and legislation, it makes little sense at the moment to maintain, or indeed impose, only one corporate governance system for a particular type of company, when it is always possible to provide the company stakeholders themselves with a choice.

The argument is not that anyone system is better or worse. Instead, it is about the suitability of a particular solution for a particular company, which may be attributable to internal or external reasons and/or unrelated to the balance of interests in the company. This article has set out some examples of new legislation passed in jurisdictions where the dualistic system has traditionally and exclusively been the norm, but it is obvious that both systems have their variations in particular jurisdictions. More often than not, the evolution of approaches adopted and found in monistic systems will lead to similar solutions, albeit within a single, only apparently unified body. On the other hand, the traditional advantages of the monistic system remain strong, viz. easier circulation of, and access to, information or joint decision-making by all directors, and the absence of the problem of the supervisory board being too passive.

The purpose of this article, however, is not to give preference to a particular governance system or to demonstrate their respective weaknesses,

but rather to answer the question of whether we should adopt one of the two systems at the statutory level when drafting legislation, or whether we should provide a choice to those intending to run a business. The latter option would be favorable, i.e. the introduction of a legal choice and the propagation of a mixed system.

Arguments supporting this approach include the following:

First, any prohibition or *jus cogens* should be justified in private law (Tarska, 2012, p. 17). There is no justification in private law which would serve as the basis for establishing an imperative norm or prohibiting the establishment of any type of system. Without prejudging the suitability of either system for the participants in a particular country's commercial activities, it is rather difficult to imagine a situation where one system, either the dualistic or monistic one, ought to be imposed top-down, since the simple existence of the alternative would lead to negative effects on a mass scale. When considering this topic, we should avoid over-generalisations, and instead focus on the suitability of different systems for companies in a range of various situations. As such, it is not possible to draw a single conclusion that applies to all companies, even if we limit ourselves to those registered in one country.

Second, there is no need to shift the burden of choice to legislatures, who will at most propose a model solution which might not be suitable in a specific situation. Although the option of introducing a monistic or dualistic system would be a good move, very often it would only provide a general framework for a particular company. Having the flexibility to choose either a dualistic or monistic system of corporate governance which suits the needs of the business would be more favourable and allow the business to choose the appropriate general framework for corporate management. For example, when choosing the dualistic system, a number of decisions have to be made, such as whether to endow the supervisory board with additional powers or whether to impose an obligation on the management board to obtain the supervisory board's approval for certain resolutions. If it is not advisable for the legislature to interfere too much, it is all the more inadvisable for it to impose a particular corporate governance system on all companies.

Third, the shareholders are free to make their own choice as to whether a particular share governance mechanism does or does not suit their purposes in a particular situation, thus avoiding a possible conflict of interest between organs, authorities or shareholders. At this point in the discussion, it is appropriate to refer to one of the cardinal principles of continental private law, namely the principle of freedom of contract (Ibid., p. 15). A company is not simply a manifestation of a private-legal agreement or contract; it is a private-legal organization that comes into being on the basis of a legal constitution. A private legal organization is based on a corporate constitution which is a contract and the freedom-of-contracting principle applies. At the same time, this contract brings a new legal entity into existence. It is true that the legislature can arbitrarily impose, and has imposed, certain structures on all companies but it is important to consider whether freedom of contract should be extended as far

as possible. The objective would be to choose in the contract an option from several proposed by legislators.

Fourth, there is no public interest at stake. State-owned and municipal companies also use private-law constructions and can make the same choice. They can rely on private law when making decisions about their corporate governance structures. However, their decision making would be irrelevant to private companies where no public or state interest exists. Indeed, it is difficult to make any argument about the existence of a legitimate public or state interest in the case of private companies. By definition, the participants in a company act in order to obtain a profit. Private companies exist for this purpose. The state interest in their activities is limited to regulating the sector. The state is not concerned with the operation of the business as long as it meets the standards for regulatory compliance. The same standard should apply to whether a company selects a monistic or dualist system of corporate governance. A state may have a general interest in the proper operation of a business sector, but it is indifferent when it comes to how individual companies perform or groups of businesses perform. Shareholders have some influence on the means of corporate governance by selecting a structure.

There is no rational justification for the fact that it is possible to choose a system of corporate governance in the case of some limited liability companies, but not so in the case of others. Limited companies often have great structural similarities and are even regulated in a confusingly similar way (e.g. the management board in a joint-stock company and the management board in a limited liability company). The question then arises as to why there are more options available to some of these business vehicles, but in the case of others, legislation leaves no choice.

It should be pointed out that the monistic system was historically the first corporate governance system that was made available, as even “the German supervisory board of the late 19<sup>th</sup> century and early 20<sup>th</sup> century in fact resembled the Anglo-Saxon board of directors or the French conseil d'administration, and the relationship between the supervisory board and management board resembled that between a board of directors and an officer” (Opalski, 2005, p. 13). As such, we are not dealing with two traditions, which must on no account be mixed. Instead, we are dealing with different approaches that apply in varied circumstances. Nowadays, more flexibility is desirable, and even if particular corporate governance forms are not used by individual market participants, this will not be detrimental to any extent. Even if “the history of the supervisory board is the history of legislatures’ 'breaking' the original model of combining management and oversight functions in one body,” (Lewandowski, 2021) these historical reasons – perhaps relevant in the past in some countries - are now gone.

One of the most compelling arguments for the introduction and preservation of the choice between the dualistic and monistic systems concerns the international connections of business and capital and the ease of registering a company in another jurisdiction. Founders themselves can tailor the company to the needs of foreign investors who come from different common law legal

traditions in their home countries. Without going into unnecessary detail, there are – at least in the European Union - far-reaching opportunities to use company structures from various jurisdictions. Countries with a case law tradition, such as the Republic of Ireland, are part of the European Union. In this case, if domestic companies are not found to be particularly appealing, this will lead not so much to capital flight as to the use of foreign constructions that investors may find more attractive.

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