

Violation of articles of association not enough to annul shareholders' resolution



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Introduction

Appealing against shareholders' resolutions is one of the most controversial areas of Polish company law. A recent Supreme Court resolution found that the shareholders' resolution of a limited liability company cannot be annulled by the courts just because it is contrary to the provisions of the articles of association. **(1)** A resolution that infringes the articles of association may be annulled only if it further undermines the interests of the company or is aimed at harming shareholders. The Supreme Court resolution would appear to put an end to many years of controversy.

Controversy

Article 249(2) of the Commercial Companies Code states as follows:

A resolution of shareholders which is contrary to (a) the articles of association or (b) principles of morality and (c) adversely affecting the interests of the company or (d) aimed at harming the shareholder may be appealed against by way of an action brought against the company for an annulment of the resolution. **(2)**

The interpretation of the above provision has been the subject of controversy for many years. Most of the judiciary considered that for a resolution to be annulled, at least one of the elements (a) and (b) and one of the elements (c) and (d) should be fulfilled simultaneously. Nevertheless, some authors (as well as some courts) assumed that:

- a contradiction with a company's articles of association was an independent basis for repealing a shareholders' resolution; and
- only when a contradiction with good practices is claimed, one of conditions (c) or (d) must additionally be met.

The Gdansk Court of Appeals, examining the case for an annulment of the shareholders' resolution, submitted a motion to the Supreme Court to resolve the above controversy by way of a resolution. Supreme Court resolutions are not formally binding (with the exception of the case directly concerned); however, in practice, they are of fundamental importance and affect the shape of all court rulings.

Decision

The Supreme Court ruled that a shareholders' resolution of a limited liability company that is contrary to the articles of association may be annulled only if it further undermines the company's interests or is aimed at harming shareholders. The Supreme Court therefore approved the dominant interpretation of the provision.

First, the Supreme Court assumed that the provision's textual interpretation strongly supported a majority interpretation. Second, in the Supreme Court's opinion, the majority interpretation was more rational. (It allows the courts to examine whether the annulment of a resolution is really appropriate in certain circumstances.) A minority interpretation would require the court to repeal the resolution due to the mere formal contradiction of the resolution with the articles of association.

Third, the Supreme Court raised the argument that a majority interpretation is supported by the principle of stability of legal persons (ie, corporations). An alternative interpretation would allow minority shareholders that disagree with the majority to challenge resolutions on the basis of any formal conflict with the articles of association. According to the Supreme Court, a majority interpretation protects against such practices, as it requires the actual negative effects of such a resolution to be demonstrated.

Comment

The Supreme Court's authority means that this decision, although made in one particular case, must be considered in the context of the entire business practice. The decision is also in line with the prevailing views in Polish jurisprudence. Nevertheless, the Supreme Court's position raises some doubts.

The Supreme Court's resolution is an expression of two prevailing tendencies in the Polish judiciary. First, the general reluctance to appeal against resolutions by shareholders. Polish courts are cautious when it comes to challenging resolutions of corporate partners of legal entities such as limited liability companies. Second, the Supreme Court resolution reflects an excessive attachment to a 'safe' literal interpretation of rules, often without considering their purpose and function more broadly.

Meanwhile, the articles of association of a limited liability company form a company constitution. This is an internal law that is binding on shareholders and members of the company's governing bodies. Violation of a company constitution cannot be without consequences. Infringement of the fundamental rules of a company's functioning by nature undermines its interest in functioning in accordance with the principles adopted, as expressed precisely in its articles of association.

On the other hand, since a violation of a company's articles of association typically undermines company interests, the practical consequences of the Supreme Court's position appear to be relatively limited. In practice, this means that the plaintiff must additionally demonstrate in what specific way a resolution contrary to the articles of association violated company interests. It seems that in most cases, with a proper understanding of the essence of the articles of association as a corporate constitution, this should not give rise to major difficulties.

The previous company law (repealed on the entry into force of the current Commercial Companies Code on 1 January 2001) directly allowed shareholders' resolutions to be annulled on the basis of their contradiction of a company's articles of association without the need to prove additional circumstances, such as the violation of the company's interest.

Moreover, the Supreme Court resolution formally refers only to resolutions of limited liability company shareholders. Nevertheless, the rules for appealing shareholders' resolutions of joint-stock companies (Article 422 of the Commercial Companies Code) are virtually identical in this respect. Thus, the analysis and position presented by the Supreme Court are of equal importance for the functioning of joint-stock companies and the violation of the articles of association by resolutions of the general meeting.

Incidentally, Polish company law entitles the courts not only to annul shareholders' resolutions but also to declare them invalid (Articles 252 and 425 of the Commercial Companies Code). This applies to both limited liability companies and joint-stock companies. A resolution may be declared invalid if it is contrary to a statute. A resolution is considered to be 'contrary to a statute' if its content is contrary to the provisions of law or if it was adopted in a manner contrary to the procedure provided for in the Commercial Companies Code. The effects of the annulment and the declaration of invalidity of a resolution are similar. An action for the annulment or the declaration of invalidity of a resolution may be brought only by members of a company's governing bodies and its shareholders, and in the case of the latter, certain additional conditions must be met (objection to the resolution or occurrence of irregularities in the procedure for convening a meeting).

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Endnotes

(1) Supreme Court resolution of 10 March 2016, file ref III CZP 1/16, available here (in Polish).

(2) Letters (a) to (d) have been added by the authors of this article.

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