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NEWSLETTER

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WINDS OF CHANGE

In 2011, Turkish authorities had been anticipating an exciting year with major elections coming up and with new economic and welfare packages en route. The only remaining factor on the current government's agenda was to win the election, make their mark on Turkish political history, and to continue building on their previous terms with another 4 years of a "Term of Expertise," so to speak.

Great legal changes had been promised, with Europe's largest courthouse being inaugurated in Istanbul, coupled with the new Turkish Commercial Code and Code of Obligations entering into effect. These major overhauls in the legal system were expected to pave the way for a more efficient commercial system with endless opportunities, both for local and foreign investors. While we were bracing ourselves for these legal winds of change to sweep through, yet another gale was blowing the Arab Nations asunder: Tunisia, Egypt, and Libya were all caught up in the storm, and suddenly the prime focus of the world shifted from Iraq to these nations, and while the Arabian Peninsula barely managed to contain itself against the storm, Syria faltered.

What began as an ordinary year turned out to be one of the most historic years of the Millennium. Amidst the storm, however, Turkey continued to shine, with its unprecedented growth rate for the first quarter even surpassing the ferocious Asian Tiger, China. The second-quarter growth for Turkey was slower, but it was still an impressive climb for a country that stood in the middle of the storming world, with its eyes hungrily focused on new business opportunities. When the dust settles, the legal implications of the "Arab Spring" will start to unfold.

Turkey is a major investor in all of the affected countries, especially Libya, with over 10,000 expats fleeing the country, along with their companies and investments. Their return trip is bound to have more than a few bumps in the road, and as the closest "prospering" Muslim country with a brilliantly overhauled legal system, Turkey is ready to set the example of "how things should be done." This year, the Republic of Turkey celebrated her 88th birthday and, during this period, Turkey has been caught in the middle of everything from wars to petroleum shortages – one did not have to look far to see a problem then, and one does not have to look far now.

Looking back on previous years, Turkey has gained much ground regarding legal restructuring, and is still making incredible strides forward. This newsletter takes a look at the numerous changes that are eagerly awaited by some, and not so by others.

In the later part of 2011 and 2012, it remains to be seen whether we will be able to effectively complete spin-off transactions, and whether implementation of the United Nations Convention on the International Sale of Goods will be utilized successfully.

We will also be dealing extensively with real estate issues. With the enactment of the "Re-allocation of Land that has Lost Forest Status Law" - in short, "Law 2b," disputes will surely ensue between the public and the government. Along with the Preservation Board's authority being divided into separate cultural and natural asset administrations, the volume of real estate transactions and disputes is bound to increase.

Looking upwards to the sky into the invisible world of the airwaves, this, as well, will no longer be the same with the enactment of the New Broadcasting Law that has given this sector somewhat of a jolt as it has been caught resting on its laurels.

Employer obligations will come with subtle twists as of July 12, 2012 with the enactment of the Code of Obligations. Perhaps all of the solutions to our problems lie with the alternative dispute resolution method - that is, mediation, but the question which begs answering is whether or not we will start using it effectively. Most people are unaware of the existence of mediation, and even less are aware of its implications. Perhaps instead of outbursts of law-enacting we need to slow down, cool down and refresh.

Nevertheless, the new and upcoming changes to the railway system will keep us occupied with the new high speed rail lines being put into service and the next step of privatizations most likely targeting the railways. We anticipate looking forward to a greener future, both concerning the environment and legal matters, perhaps encouraged by the amendments to the Law on the Utilization of Renewable Energy Resources for Electricity Generation.

This past year has also been a "windy" year for Hergüner with the expansion of our Arbitration Team through welcoming 'Of Counsel' Mr. Noyan Göksu, and the invaluable 'Of Counsel' addition of

Ms. Esra Biçen to our Corporate Team. Although we were saddened by the departure of our veteran partner, Mrs. Itır Sevim-Çiftci, the winds also carried Mrs. Aslı Budak to the status of partnership with Hergüner Bilgen Özeke, at the start of her 5th year with the firm. We take this opportunity to introduce both Mr. Göksu and Ms. Biçen, along with our newest Partner Ms. Aslı Budak, as part of the ever-dynamic and strong Hergüner Team, wishing them great success in the coming years.

Ms. Aslı Budak is a Partner specializing in, Hergüner Bilgen Özeke's General Corporate Practice. Working mostly out of our Ankara working premises she provides legal and business advice given in general corporate matters of project finance, and especially within the areas of mergers, acquisitions, joint ventures, securities transactions, and foreign investment. She has also participated in extensive negotiations with governmental and private counterparties.

Mr. Kurtcebe Noyan Göksu is Of Counsel heading the firm's arbitration practice. His practice draws on his diverse experience in international arbitration and litigation. He has acted for or advised states and private parties in *ad hoc* and institutional arbitrations under the ICC, ICSID, LCIA, AAA, Stockholm Chamber of Commerce, GAFTA, FOSFA, and the Hamburg Stock Exchange rules. Among other fields, he particularly focuses on disputes involving energy projects, engineering and construction projects, FIDIC contracts, government procurement contracts, JVs and M&As, telecom services, agency and distribution contracts, and cross-border commodity sales.

Ms. Esra Biçen is Of Counsel to the Firm's General Corporate Group and Dispute Resolution Group. She has extensive experience in Turkey and in the United States. Her Turkish practice involves providing advice in mergers and acquisitions, cross-border financings and commercial disputes. In the United States, she practiced complex civil litigation matters with a leading US law firm focusing on mass tort actions. Prior to joining Hergüner Bilgen Özeke, she was general counsel to one of the Big Four accountancy firms in Turkey. She is certified by the ICC International Court of Arbitration and is licensed in Istanbul and New York.

by Hergüner Bilgen Özeke

GROUP OF COMPANIES AND PROHIBITION OF ABUSE OF DOMINANCE UNDER THE NEW TURKISH COMMERCIAL CODE

The concept of a group of companies is set forth under Articles 195-209 of the New Turkish Commercial Code (the "New TCC"). The principles of "dominance" and "abuse of dominance" are also regulated under the same provisions[1].

Concept of Group of Companies and Relation of Dominance

In accordance with Article 195, paragraphs 4-5 of the New TCC, a group of companies is composed of a parent company (dominant company) and subsidiary company(ies) under the exercise of its dominance. In other words, the existence of a group of companies depends on the existence of dominance among the group members. Such relation of dominance may be direct or indirect (through shareholdings of the dominant company in other companies at different levels).

The New TCC does not specify the definition of "dominance." The doctrine defines dominance as the power to determine and control decisions of a company concerning its finances and operations, and also covers decisions relating to its budget, investments and all other financial matters, dividend policy, production, marketing, sales and HR[2]. The New TCC lists the sources of dominant power in Article 195, paragraph 1 as: (i) dominance through voting rights, (ii) dominance through agreements and (iii) dominance through other sources. The first classification covers three different circumstances: the dominant company directly holding the majority of voting rights of the subsidiary company; the dominant company holding the power to elect the majority of the members in the management body;

1 The New TCC sets forth notification, registration and reporting obligations with regard to group companies.

2 Please see Gül Okutan Nilsson, Türk Ticaret Kanunu Tasarısı'na göre Şirketler Topluluğu Hukuku, Istanbul, 2009, p. 98.

and the dominant company holding the majority of the voting rights through corporate bylaws[3]. The second classification covers operational agreements, not seen in Turkish practice, relating to management/domination agreements (*hâkimiyet sözleşmesi*) or the transfer of dividends. Finally, the last classification covers situations of *de facto* dominance.

Article 195, paragraph 2 of the New TCC provides for a presumption of dominance. The provision underlines that a company owning the majority of the shares of another company, or which owns the shares of another company that procures control in the management and financial decisions of the other company, dominates the latter.

According to Article 195, paragraph 1 of the New TCC, the rules of the New TCC regarding a group of companies will apply if one of the dominant or subsidiary companies' headquarters is located within the boundaries of the Turkish Republic.

The New TCC sets forth certain rules prohibiting abuse in the exercise of dominance in a group of companies under certain conditions.

Prohibition of Abuse of Dominance in Group of Companies

Article 202 of the New TCC underlines two situations of abuse of dominance: (i) abuse of dominance through transactions within the scope of authority of the board of directors (the "BoD") and (ii) abuse of dominance through transactions within the scope of authority of the general assembly (the "GA"). In addition to these, the legislator foresees a third situation of abuse in Article 209 of the New TCC that relates to (iii) the abuse of public trust in the goodwill of the group of companies. This prohibition is a projection of the obligation of the dominant company not to cause losses to its subsidiary through the exercise of its dominance.

(i) Abuse of dominance through transactions exercised by the BoD

This first situation of abuse relates to financial losses faced by the subsidiary company as a result of transactions/decisions exercised by the BoD of the dominant company that are considered to be violations of the BoD's duty of care. Article 202, paragraph 1 provides a sample list of transactions that may result in financial loss to the subsidiary[4]: (i) transfer of business, assets, funds, personnel, receivables and debts, (ii) reduction or transfer of profits, (iii) restricting rights on assets by granting real or contractual rights to third parties, (iv) undertaking liabilities such as securities or guarantees; (v) resolutions or prohibitions such as the restriction or interruption of investments that may negatively affect productivity or activities, or prevent the progress of the subsidiary. The New TCC prohibits these transactions unless, during the same activity year, any losses that are realized are compensated, or the subsidiary is granted a right of claim that firmly determines the date and the method of compensation in an amount that is strictly equal to the losses which have occurred.

The financial losses stated in the provision cover not only actual financial losses, but also potential losses, such as potential losses relating to the assets or the profitability of the subsidiary.

If the losses that have occurred are not compensated during the same activity year, or if the subsidiary is not granted an equal right of claim, each shareholder of the subsidiary may seek compensation from the dominant company or from the BoD members of the dominant company who are responsible for the realized losses[5]. A similar right of claim is also accepted for the creditors of the subsidiary under Article 202, paragraph 1(c).

According to paragraph 1(d) of Article 202, board members will not be held liable for any losses that may have occurred if they demonstrate that the

3 According to the New TCC, in cross-shareholding (a subsidiary company holding at least 25% shares of the dominant company), the dominant company will also be considered as a subsidiary.

4 The list is not *numerus clausus*; more examples exist.

5 If a lawsuit is filed by the shareholders of the subsidiary, the court may decide on acquisition of the shares of such shareholders by the dominant company or on another adequate remedy rather than indemnification. The right granted to the shareholders of the subsidiary company to demand the purchase of the shares before the court is an important exit right under the group of companies' provisions.

same decisions would have been made (or would have been avoided), under the same or similar circumstances by the board of a hypothetical independent company, acting prudently and in good faith, exercising due care and loyalty.

The lawsuit must be filed with the commercial court of the city where the dominant enterprise's head office is located. If the dominant company is registered outside of Turkey, then the lawsuit may be filed with the commercial court of the city where the subsidiary company's head office is located.

(ii) Abuse of dominance through important decisions adopted in the GA

The second situation of abuse relates to financial losses resulting from important structural decisions adopted in the GA, such as a merger, spin-off, change of type or dissolution; the issuance of stocks or securities, or amendments to the articles of association. Shareholders who vote against such a decision and have their objections recorded in the minutes of the meeting (or who object to the relevant decisions of the board of directors in writing) have the right to sue the dominant company for indemnification of their losses.

The shareholders may also request that the dominant company purchase their shares at their stock exchange value or, if this value is unfair, at their real value, or at a value to be determined through a generally acceptable method[6]. The Court may also adopt another equitable decision, such as payment of the dividend that the shareholder is deprived of due to any loss incurred by the dominant company[7].

It must be underlined that the statute of limitations for such a lawsuit is two years, commencing from the date of adoption of the general assembly decision or publication of the board resolution.

(iii) *Abuse of confidence or trust*

According to Article 209 of the New TCC, the dominant company is responsible for abuses in wielding the reputation of the group of companies if the group's reputation is such that it projects an air of confidence and reliability to the public at large. In fact, the dominant company is held responsible for the confidence or trust that it has foreseeably raised in consumers. An example of this is a comfort letter delivered by the dominant company in favor of its subsidiary.

Exception to Prohibition

In accordance with Article 203 of the New TCC, if a dominant company holds, directly or indirectly, 100% of the shares and voting rights of a capital stock company (subsidiary), the board of directors of the dominant company has the authority to instruct the subsidiary to follow its group policies, even if these instructions cause financial loss to the subsidiary. In such a case, the board of directors of the subsidiary must comply with the instructions of the dominant company and will be exonerated from liability[8]. However, the dominant company may not give instructions that would cause losses in excess of the value of the assets of the subsidiary, thereby compromising its existence and causing loss to its important assets.

by Dr. Meltem Küçükayhan Aşcıoğlu

6 The Court may, ex officio, decide on such compensation, if equity necessitates such a solution.

7 For more details please see Nilsson, pp. 385-386.

8 See Article 205 of the New TCC.

SHARE BUYBACKS UNDER THE NEW TURKISH COMMERCIAL CODE

The purchase by a company of its own shares is generally referred to as a "share buyback." Companies follow this process in order to reduce the number of their shares in the market. The two main reasons that companies may elect to reduce their shares in the market are: (i) increasing the value of shares still available; and (ii) eliminating any threats by shareholders who may be looking to hold a controlling stake.

Although share buybacks are allowed in many common law countries along with many European Union countries since the mid-1970s, share buybacks are generally prohibited under the currently applicable principles of Turkish law. However, New Turkish Commercial Code No. 6102 that was enacted on 13 January 2011, and which

will be effective from 1 July 2012, allows for share buybacks by companies under certain conditions.

i. System Under Currently Applicable Turkish Commercial Code

Although there are other specific regulations that may be applicable depending on the nature of the company in question, the main legislation regulating share buybacks is currently the Turkish Commercial Code - Law No.6762 (the "**TCC**"). According to the TCC, save for a few exceptions, companies are prohibited from acquiring their own shares. The following situations are listed as exceptions of this principle under Article 329 of the TCC, and share buybacks are temporarily permitted and not deemed void in these instances: (*i*) buyback based on the capital decrease of the company; (*ii*) company acquiring its shares in consideration of its receivables arising from a debt that was incurred other than due to the subscription of share capital; (*iii*) company indirectly acquiring its own shares by way of the transfer of an estate or business that holds its shares; (*iv*) purchase or pledge of shares being a part of the scope and objective of the company; (*v*) company pledging its own shares as collateral in exchange for the obligations of its directors, managers and/or officers; and (*vi*) company acquiring its own shares free of charge.

In the event that any of the above-stated exceptional circumstances exist, the company in question may acquire its own shares for a temporary period of time. Although Article 329 of the TCC is silent on how long such temporary period of time may be, the company is still obliged to dispose of these shares within the shortest time possible.

As a consequence of a share buyback, it should be noted that the rights attached to such shares cannot be exercised by the general assembly of shareholders. Therefore, the buyback shares shall not be taken into consideration during the calculations of meeting and decision quora at general assembly meetings.

Any agreement of the parties contrary to Article 329 of the TCC as stated above shall be considered void. Also, failure to comply with such principles may lead to the liability of the members of the board of directors of the company in question and the shareholders whose shares have been transferred in violation of the prohibition.

ii. System Under New Turkish Commercial Code

The new Turkish Commercial Code (the "**New TCC**") generally enacts the principles regulated under the Second Council Directive of European Economic Community numbered 77/91 regarding share buybacks. Similar to Article 19 of the said Directive, share buybacks are allowed under certain conditions. For instance, the board of directors should be authorized by the general assembly, which authorization should include the terms and conditions of such acquisition (the maximum number of shares to be acquired, the duration of the period for which the authorization is given, and the minimum and maximum amount of consideration, *etc*.). In accordance with the abovementioned Directive's requirements, the New TCC determines the upper limit for share buybacks at 10% of a company's basic or issued capital.

a – Joint Stock Companies

Under the New TCC, share buybacks of joint stock companies are allowed subject to certain conditions as stated in paragraph 1 of Article 379. A company may not acquire and accept its own shares as a pledge in return for a consideration that exceeds, or will exceed, as a result of a transaction, 10% of its basic or issued capital. It is further noted that such restriction will also apply to shares that a third party acquires or accepts as a pledge in his/her name, but on account of the company.

Another requirement regulated under the New TCC is the authorization of the board of directors by the general assembly to approve share buybacks or the pledges over the company's own shares. This authorization may only be granted for a specific period of time. The New TCC stipulates the maximum period for such authorization as five years. The lower and the upper limit of the amounts that may be paid for shares to be acquired, and the

total nominal value of the shares to be acquired or accepted as a pledge, must be stated in the authorization. The board of directors must also state in each of its requests for authorization from the general assembly that all legal requirements for the share buyback have been met.

Share buybacks must not cause a reduction in the company's net assets under the sum of: (i) the company's reserves that are not allowed to be distributed according to law and the company's articles of association; and (ii) the company's basic or issued capital, calculated after the cost of the shares to be acquired are deducted from the company's net assets.

Share buybacks are only allowed for shares, the amounts of which have been fully paid.

The acquisition of a parent company's shares by its subsidiary company is also considered as the acquisition of a company's own shares under the New TCC and, therefore, fulfillment of the above-listed criteria is also required for such transactions.

The New TCC regulates, in Article 382, six exceptional situations in which the above principles are not required to be adhered to:

- (i) Buyback is made through the application of Articles 472-475 of the New TCC that regulate share capital decrease;
- (ii) Buyback is made as a result of universal succession (*külli halefiyet*);
- (iii) Buyback is made by virtue of a legal obligation for acquisition;
- (iv) Buyback is made with the intent of collecting the receivables of the company through an execution proceeding, provided that the concerned shares are fully paid;
- (v) The company is a securities company; or
- (vi) Buyback is made gratuitously, provided that the concerned shares are fully paid.

According to Article 381, if the share buyback is required in order to avoid an imminent and serious loss to the company, then the company in question is entitled to acquire its own shares in the absence of a general assembly resolution for authorization, although the other requirements remain. However, the board of directors is obliged to provide, at the next general assembly, and in writing, the reason and the purpose for the share buyback, the number of shares acquired, the total amount of the concerned shares' nominal values, the percentage of the capital they represent, and the price and terms of payment.

Although share buybacks are allowed by the New TCC under certain circumstances, according to Article 384 of the New TCC, companies are still not entitled to hold such shares permanently, unless the total amount of these shares owned by the company and the subsidiary company exceeds 10% of the company's basic or issued capital. The acquired shares must be disposed of as soon as possible after their transfer is effected without causing any loss to the company and, in any event, within three years from their acquisition. Such disposal is not required for share buybacks occurring as a result of a share capital decrease and for share buybacks by securities companies.

If the shares are acquired or accepted as a pledge in breach of the above principles, such shares must be disposed of, or such pledge must be released, within a period of a maximum of six months commencing from the date of their acquisition or acceptance as a pledge. If the shares cannot be disposed of in either of the above two ways, then they must be immediately redeemed through a capital decrease.

The New TCC prohibits the subscription of a company's shares by the company itself. Subscription of a company's shares by a third party, or by such company's subsidiary in its own name but on account of the company, is also considered as a subscription by the company for its own shares. In the event of share subscriptions in breach of the above, the subscribed shares will be considered to be subscribed by the incorporators (if they are effected through the incorporation process) or by the board members (if they are effected through a capital increase process), and the incorporators or the board members, as applicable, will be liable for the cost of the shares.

The New TCC states that except for the gratuitous acquisition of shares, share buybacks do not grant any shareholding right, and such shares shall not be taken into consideration in the calculation of a general assembly meeting quorum.

b – Limited Liability Partnerships

Under Article 612 of the New TCC, share buybacks in limited liability partnerships are not regulated in as much detail as share buybacks in joint stock companies. However, generally, similar principles apply.

A limited liability partnership may acquire its own capital shares, only if it has the necessary equity that may be freely used to purchase them, and if the nominal value of the shares to be purchased does not exceed 10% of the total share capital. This maximum limit of 10% will be increased to 20% in the case of acquisition of capital shares, due to a withdrawal or dismissal from the partnership as provided for in the articles of association, or as a result of a court ruling.

Capital shares acquired in excess of 10% of the share capital of a partnership must be disposed of or redeemed through a capital reduction within a maximum period of two years.

Limited liability partnerships are required to allocate reserves in an amount equal to the amount paid for the acquired capital shares.

Parallel to the regulations concerning joint stock companies, voting rights and the other rights attached to the capital shares subject to the buyback are suspended for the period that such capital shares are in the possession of the partnership.

Supplementary and related payment rights attached to the acquired capital shares cannot be demanded during the period that such capital shares are in the possession of the partnership.

The limitations applicable to a limited liability partnership's acquisition of its own shares shall also be applied in the event of acquisitions of a partnership's shares by a subsidiary in which the majority of the shares are owned by the concerned partnership.

In light of the foregoing, it may be concluded that while the current TCC generally prohibits share buybacks in principle, and allows this process only in exceptional cases, the New TCC allows for a more permissive approach.

The new regulations concerning share buybacks are generally in harmony with the European Union's directives and intend to prevent trading companies from causing undue damage to shareholders through manipulative transactions.

The new regime regarding share buybacks remains to be tested following the New TCC's entry into force on 1 July 2012.

by Pınar Çulha Moler, Melike Gençalp

OVERVIEW OF THE NEW CODE: SPIN-OFF TRANSACTION AND LIABILITY OF THE PARTIES IN THESE TRANSACTIONS

The joint Communiqué of the Ministry of Finance and Ministry of Industry and Trade No. 25231 dated 16 September 2003 (the "**Communiqué**") is the primary regulation that governs the partial spin-off of a joint stock company or a limited liability partnership, whereas the Turkish Commercial Code (Law No. 6762) is silent on the issue. Pursuant to the Communiqué, a spin-off may only be realized by way of partial division. Accordingly, in the event of a spin-off, a portion of the assets of a joint stock corporation or limited liability partnership are transferred to the target company as capital in kind, and the shareholders of the spin-off company acquire shareholding of the target company, which may be either a newly established company or one that currently exists.

The New Turkish Commercial Code (Law No. 6102 or the "**New TCC**") that will become effective on 1 July 2012, on the other hand, regulates spin-off transactions in detail in comparison to the currently applicable legislation. It introduces principles concerning not only different types of spin-offs (*i.e.*, full spin-offs and partial spin-offs) but also the liabilities of the companies that are involved in such transactions, as well as the liabilities of their shareholders. Fundamental principles of the New TCC with respect to spin-off transactions is summarized as follows:

(i) Share capital companies, *namely,* joint stock corporations, limited liability partnerships and limited partnerships, the share capital of which is divided into shares, and cooperative companies may be spun-off into share capital companies and cooperative companies. On the other hand, such companies may not be split into partnerships nor *vice-versa*.

(ii) In the event of a full spin-off, all assets of a company are divided and transferred to the target companies. As a result, the spin-off company's shareholders acquire the shares and rights of the transferee companies, and the spin-off company then ceases to exist.

(iii) In the event of a partial spin-off, a part or certain parts of a company's assets are transferred to the target companies. As a result, the spin-off company's shareholders acquire the shares and rights of the transferring companies, or the spin-off company acquires the shares and rights of the transferring companies in consideration of the transferred assets and, consequently, it establishes its own subsidiary.

(iv) The assets subject to the spin-off are transferred on the basis of principles of general subrogation (*külli halefiyet*), regardless of the underlying transaction type, and no transfer of the respective assets as capital in kind occurs. Upon the establishment of a subsidiary (*i.e.*, if the spin-off company acquires the shares and rights of the target companies in consideration of the transferred assets), however, the spin-off company transfers its assets to the transferring company as capital in kind, then the transfer of the assets is not carried out on the basis of subrogation.

Liability of the Companies Involving a Spin-Off

The liability of the companies involved in a spin-off transaction is currently a controversial topic pursuant to scholarly opinion. Accordingly, certain scholars are of the opinion that the joint liability of the transferor towards the creditors in a business transfer, for a two year-period with regard to the debts and liabilities relating to such business, must also be applicable in the event of a spin-off with respect to the spin-off company; whereas, certain other scholars argue that the liabilities are vested with the transferee.

The New TCC, on the other hand, introduces specific provisions concerning this issue. In this respect, the company to which the claims were assigned by the spin-off agreement or plan is deemed as the primarily liable company, and the other companies (the companies that are secondarily liable) are jointly and severally liable for those claims that have not been paid by the primarily liable company.

The New TCC also restricts the cases wherein creditors may make claims against companies that are secondarily liable. According to Article 176 of the New TCC, secondarily liable companies may be pursued only if:

(v) A claim has not been secured; and

(vi) The primarily liable company (i) has become bankrupt, (ii) has obtained a composition moratorium or stay of bankruptcy, (iii) has been sued for debt enforcement until a final certificate or shortfall is issued, (iv) has relocated its principal office abroad and may no longer be pursued in Turkey, or (v) has

relocated its principal office abroad and, as a result, a claimant's rights to pursue the enforcement of the debt are seriously affected.

Personal Liabilities of Shareholders in the event of Spin-Off

With respect to the personal liabilities of the shareholders in the event of a spin-off, the New TCC refers to the provisions applicable in the event of a merger. In light of referenced Article 158 of the New TCC, the spin-off company's shareholders, to the extent they had been personally liable for the company's debts, remain liable for any debts that were incurred prior to announcement of the spin-off resolution, or for any debts whose legal liability is established prior to that date. The statute of limitations for personal liability of the shareholders is three years from the announcement of the spin-off resolution. However, if a receivable becomes due following the announcement, then the three-year statute of limitations with respect to this receivable will begin from the due date. This limitation of personal liability does not apply to shareholders who are also personally liable for the debts of the transferee companies.

Conclusion

The New TCC undoubtedly will put a new face on the Turkish commercial legislation. Spin-off transactions are included in the matters that the New TCC regulates in depth to satisfy the needs of today's business and legal world, and aims to find solutions for today's debated or unanswered problems, such as liability of the companies involved in a spin-off. This Article, of course, merely reflects the wording of the New TCC, and the method through which to implement the same by the Turkish courts is yet to be tested.

by Zahide Altunbaş

BOARD OF DIRECTORS' LIABILITY IN CRIMES OF SMUGGLING

The increase in the volume of international trade will lead to an increase of the Customs Authority's inspections.

Statistical information compiled as of 31 December 2010 from the official website of the Ministry of Customs and Trade concerning seized goods through smuggling investigations is presented below:

	2006	2007	2008	2009	2010
Number of Inspection	1,818	1,912	1,541	1,378	3,260
Total Value (TL)	268,878,427	296,260,150	329,227,647	292,054,505	424,531,576

The Customs Authorities are charged with duties to oversee matters such as protection of intellectual property rights, protection of public health, prevention of unfair competition, and protection of cultural heritage. As a consequence, in recent years, import companies are undergoing periodic inspections by the Customs Authorities. Within this framework, determination of liability of board members and their legal representatives is an important issue with respect to the legal perspective of transactions that are made on behalf of their company.

According to Article 317 of the Turkish Commercial Code, a board member has the authority to represent and manage the company. Management and representation duties are to be distributed since this is the best option available according to the provisions of the Articles of Association, and these articles set out how these duties may be best distributed. Authorization of management, representation and administration works, such as customs works, may also be delegated in their entirety, or in part, to the directors. In this manner, individual directors may be recognized, separately, as customs transactions.

Article 38/6 of the Turkish Constitution sets forth that criminal responsibility shall be personal. However, no person shall be held responsible for another person's actions and no punitive sanctions may be imposed upon the legal entities associated therewith. These provisions explain the general principle of law: "*Each person shall be liable for his/her own actions*." According to this Article, it is a clearly regulated general principle under our Criminal Law provisions that one person's actions shall not cause the liability of another. However, the Customs Authorities sometimes fail to take into consideration this principle, and board members may be held objectively responsible in their capacity as board members, even if they are unaware of the criminal activity. In this respect, in cases where there is strong suspicion of smuggling in importation transactions based on documents related to the transaction, criminal investigations may be initiated against the managers of the company and all of its board members.

This has been criticized in Turkish jurisprudence as well. The Criminal Chamber of the Court of Appeals has emphasized on many occasions that, the basic criminal principle is that no person shall be liable for another's actions. Board members will not be held liable unless the intention to commit a crime exists. The Criminal Chamber of the Supreme Court reiterated this principle through its decision No: 2005/2340 dated 3 May 2005.

With regard to smuggling activities, the related legislation is the Law on Anti-Smuggling No. 5607 and promulgated on 31 March, 2007. This is specific legislation, as opposed to more general legislation, and references are made therein to the Turkish Criminal Code and the Turkish Criminal Procedure Code.

The noteworthy provision is Article 3 of the Law on Anti-Smuggling, entitled "Crimes and Misdemeanors" Article 3(1): *"Importing a product into Turkey without subjecting it to customs formalities shall be penalized with imprisonment of one to five years and a fine of up to ten thousand days. If the product is imported into the country through a location other than the customs gateway, the penalty shall be increased by one-third to one-half of the assessed amount."* Article 3(2): *"Importing the product to Turkey by using false documentation, and refraining from paying partially/fully the related customs duty, shall have a penalty imposed from one to five years, in addition to a fine equivalent of up to ten thousand days."*

Moreover, the provisions below hold greater importance when a smuggling act is committed by more than one person: Article 4(2): *"If the crimes and misdemeanors stipulated in this Law are committed by three or more persons, the penalty shall be increased by one-half."* Article 4(3): *If the offenses stipulated in this Law are committed in the context of the activities of a company or to its benefit, the related security measures shall be ordered."* Article 4(5): *"If the offenses and misdemeanors stipulated in this Law are committed using false documents, a separate penalty shall be imposed."*

Another provision that may affect board members is Article 53 of the Turkish Criminal Code. This Article states that if the perpetrators are convicted and sentenced to imprisonment by the Court, they will not be able to exercise certain rights they have enjoyed, such as being employed in the public sector, exercising political rights, joining labor unions, foundations, organizations, or acting as a merchant in business sectors that are subject to administrative approvals, nor may they be appointed as legal guardians over another person.

As a result, due to the increase in the number of customs authorities and customs investigations being conducted, especially in criminal processes that require directors to be brought to task by customs authorities and prosecutors, care must be given especially on financial matters and the tracking of customs transactions, and concerted and diligent effort should be exerted towards the safe maintenance of documents and information.

by Ayşegül Akbal

THE CONCEPT OF AFFECTED MARKETS: MISCONCEPTIONS AND COMPLICATIONS

The Merger Control Communiqué[1] of the Turkish Competition Authority, entered into force on January 1st, 2011, brought some drastic changes to the merger control procedure that are accompanied by some confusion amongst companies. Parallel to the increasing number of decisions and the clarification efforts of the TCA, some of the concepts that have caused hesitation are becoming clearer.

One of the central concepts of the new Communiqué that attracted the special interest of companies and competition law practice is the concept of "affected market." The reason for the elevated interest in the concept of the affected markets is the exclusion provision of the Communiqué that abolishes the requirement for notification of a concentration if there is no affected market, even if the turnover thresholds are exceeded.

An affected market is defined by the Communiqué as[2] "Relevant product markets that might be affected by a transaction to be notified and where:

a) Two or more of the parties are commercially active in the same product market
(horizontal relationship); and

b) At least one of the parties is commercially active in the downstream or upstream market of any product market in which another party operates (vertical relationship)
constituting the affected markets."

At first glance, we discover that this definition has similarities to that of the European Commission.[3] A closer look, on the other hand, reveals that the concept of affected market as defined by the TCA:

1. Does not have a geographic dimension;
2. Is a probabilistic concept and does not require (neither does it exclude) the existence of factual overlaps; and
3. Does not have any market share criteria,

unlike the affected market concept defined by the EU Commission.

These characteristics of the concept define a substantially larger space of markets as objects of interest for merger notifications in Turkey. In other words, compared to the European definition of affected market that is an intersection of commercial activities of the parties defined in terms of relevant product markets and geographic markets, Turkish interpretation of the concept is hypothetic and probabilistic. Taking into account the lack of geographic dimension, the probabilistic approach and the width of the scope, the term "affected market" is a misnomer. In order to avoid misconceptions, the concept should have been called "factually or possibly affected market" instead.

Taking into consideration the confusion caused by the elusive character of the concept, the Turkish Competition Authority clarified its understanding of an affected market in a guiding document published on May 3, 2011[4]. According to this document, the existence of an affected market in the sense of the Communiqué is assumed, even if only one of the parties is producing goods or rendering services in Turkish markets, and the other party is active in the markets for the same products (or services)

1 Communiqué Concerning Mergers and Acquisitions Calling for the Authorization of the Competition Board (Communiqué No: 2010/4).

2 Section 5 of the Communiqué.

3 Commission Regulation (EC) No. 802/2004, Annex 1, Section 6.

4 Guidelines on Undertakings Concerned, Turnover and Ancillary Restraints In Mergers and Acquisitions

anywhere else in the world. Likewise, the existence of an affected market is assumed if one of the parties is active in Turkish markets for a certain product (product A) and the other party is active in upstream markets (markets for products that are an input for product A) or downstream markets (markets for which product A is an input) of this product anywhere else in the world. It is well placed to mention that the existence of a factual business connection is not required for the assumption of a vertical or horizontal relationship in this sense.

For example, take the acquisition of a company (alias T) producing and selling computer hardware, established in Turkey by another company (alias G) producing and selling computer hardware globally. Assume that G is producing and selling computers worldwide except in Turkey. At the same time, G is a seller of computer components in South Korea. On the other hand, T is assembling computer components into finished computers in Turkey. In this illustrative example, there are horizontal (both G and T are active in the production of computers) and vertical overlaps (G is selling computer components and T is buying computer components, albeit from another supplier) between the activities of the parties, even if the parties do not have any business relationship.

Considering that most of the acquisitions realized by strategic investors who are the real economic actors in the area of acquirers' expertise, the existence of an affected market is the rule rather than the exception for these transactions. The relief of notification based on the non-existence of an affected market is mainly constructed for the acquisitions of companies established in Turkey by financial investors, such as private equity companies that are holding portfolios of companies active in markets other than those in which their target company is operating. In other words, acquisition of a domestic undertaking by a financial sector company that already has a company in its portfolio, and which is operating in the same market as the Turkish target company, will be subject to notification so long as the turnover thresholds are met.

The hypothetic and probabilistic nature of the affected market concept causes a peculiar information submission burden upon notifying parties. Consider the case of a globally active company that attains a market share in Turkey through its subsidiary purchasing one of its local competitors (or suppliers). In this case, there is at least one factually affected market to consider. The hypothetic and probabilistic dimension is no more relevant. According to experience, in cases like this (much of the time) the Turkish Competition Authority considers the information related to the Turkish markets as sufficient. On the other hand, if the acquiring party in this transaction were not to have any activities in Turkey, the (possibly) affected markets will be defined as Turkish with global markets for the relevant products, which in turn will mean that the parties are expected to submit turnover and market share information concerning their activities in the global and Turkish markets. The peculiarity is that the parties are expected to submit more sensitive information in cases that are less prone to cause competitive concerns.

The new Merger Communiqué brought some clarification to parties concerning their notification obligation by abolishing market share thresholds for the notification requirement, but a portion of this clarity has been rescinded through with the exception provision of the new Communiqué. The broad scope of the affected market concept renders the exception useless for both the parties as well as the Turkish Competition Authority. It does not provide a real exception despite the anticipation it creates and misguides the undertakings upon self-assessment. At the same time, it fails to sieve the transactions that do not create any competition law risk and, hence, the exception rule does not serve the aim of better-allocating Competition Authority resources. There is a need for further elaboration regarding the complications stemming from the elusive definition of the affected market concept.

by Süleyman Cengiz

THE NEW CODE OF OBLIGATIONS: AN OVERVIEW

In accordance with Turkey's growing social needs, as well as considering its technological enhancements, the need to amend and improve major codes has become indispensable. Accordingly, the current Turkish Code of Obligations[1] (the "TCO") will be replaced by the New Code of Obligations (the "New TCO") as of 1 July 2012.

There are specific articles addressing some of the new regulations in this newsletter, as well as articles in some of our earlier newsletters. With this article, we present a general overview of previously unaddressed regulations of the New TCO.

In the following section, each subject is addressed separately for ease of reference.

(i) New Regulations Regarding Employment Agreements:

- The concepts of "sexual harassment" or "mobbing" do not exist in the TCO or Labor Law[2]. The legal gap, especially in the case of mobbing, was filled by court rulings.

  The New TCO, however, regulates both sexual harassment and mobbing through a specific article. The employer is now obliged to take necessary actions that will prevent employees from exposure to such acts and minimize the damage for those who are already exposed to such behavior. However, we believe that the lack of a clearer definition for "mobbing" remains a problem.

  One of the most important sanctions that the New TCO provides for sexual harassment and mobbing cases is the determination of liability for compensation. Any breach of contract or the law by the employer that causes damage to the employee (physical or non-physical damages) will be resolved in accordance with the rules of "contractual liabilities," instead of through tort rules, to ensure that the victim's rights are better protected.

- The TCO did not have a specific provision on the time limit of "non-competition" agreements for employees after termination of employment; rather, it indicated that such agreements would be applied only if they are effective for an "appropriate time period." The New TCO provides an upper limit for such agreements of 2 years.

- The New TCO also provides that the employer may have general regulations that cover job performance, and may give "special instructions" to employees. These employees are obliged to follow the instructions to the extent that they are reasonable. We believe that application of the "special instructions" practice will differ from the current TCO practice.

- There is also a new regulation regarding the payment of "intermediation fees" to the employee. If the employer and the employee agree, the employee will be entitled to an intermediation fee to assist in establishing a commercial relationship between the employer and a third person.

- Moreover, if the employer and the employee agree that the employee may use his/her own vehicle for the performance of the employer's commercial activities, the employer shall pay the taxes, mandatory liability insurance premiums and an appropriate compensation for depreciation of the vehicle.

- The New TCO also amends the termination notice periods for employment agreements of indefinite duration based on the length of the employment period. With this amendment, the actual termination notice will be two weeks for employment of at

1 No. 818, enacted in 1926.

2 No. 4857, enacted in 2003.

least one year, four weeks for employment of one to five years, and six weeks for employment of more than five years that is similar to the corresponding regulation in the Labor Law.

It is worth noting that the regulations of the New TCO do not remove or repeal the Labor Law regulations. The new regulations will only apply in circumstances where the New TCO governs employment.

(ii) For parties who have not determined the yearly contractual or default interest under their agreement, the New TCO rule establishes the application of the valid and relevant regulations for the accrual of interest.

While parties are free to set a contractual interest rate, there will now be an upper limit. The annual interest rate shall not exceed the statutory interest rate by more than 50%.

Where interest accrues due to the debtor's default, the contractual ceiling is higher: statutory interest+100%.

(iii) The New TCO also provides for a new set of rules of "Standard Terms and Conditions" (*Genel İşlem Şartları*) that had previously gone unaddressed by the TCO. With these provisions, the law aims to protect persons from abstract and one-sided agreements unilaterally drafted by a company so as to not be negotiatable. A detailed definition for Standard Terms and Conditions is provided, and validity conditions of such agreements are also regulated.

(iv) Statutes of limitation for compensation for both torts and unjust enrichment claims are extended by the New TCO. A one year time limit for both claims is extended to two years.

(v) A new regulation on the effectiveness period of the annotated rights of purchase, pre-emption and buy-back arising from sales agreements in the land registry is determined as 10 years by the New TCO, thereby harmonizing Articles 735 and 736 of the current TCO.

(vi) The New TCO, consistent with the Law of Intellectual and Artistic Works, requires publishing agreements to be in written form. Moreover, the printing freedom of publishers granted under the TCO has been amended. The New TCO requires a statement of the time period or printing amount in the publishing agreements to have fixed terms.

(vii) In accordance with the Electronic Signature Law, the New TCO recognizes an electronic signature as an original signature in written forms of agreements. With this rule, an electronic signature will be sufficient to execute an agreement. Pursuant to this Article, documents that contain secured electronic signatures or documents that are sent via fax or other transmission methods with confirmation may also be considered as written.

(viii) The New TCO introduces the concept of "Danger Liability." Liability for the owner of an enterprise and its operator, if any, will now be joint liability for damages arising from a significantly dangerous commercial activity. Even though such activity is duly authorized by the relevant public authority such as via a license, the person suffering damages will be entitled to compensation.

(ix) Under the TCO, as soon as the agreement is established, all of the profits and losses of the tangible goods will be transferred to the buyer. However, under the New TCO (setting aside agreements to the contrary and other reserved probabilities) for moveable estates, the profits and losses will now be transferred to the buyer, together with the transfer of the possession and ownership of the goods; whereas, for immovable estates, registration under the title registry will effect the transfer.

by Berk Ali Çobanoğlu

SURETYSHIP UNDER THE NEW TURKISH CODE OF OBLIGATIONS: "JUST SIGN HERE!"

The New Turkish Code of Obligations will enter into force in July 2012 and will introduce many noteworthy changes to the suretyship (*kefalet*) institution, which is a widely used legal instrument of personal guarantee, perhaps most commonly invoked to secure loan agreements in Turkey.

The amendments introduce new limits to the extent of a surety's liability against the lender, and a more elaborate written form requirement that seems to be a reaction to the "just sign here" attitude that the current legislative scheme enabled. In this article, we have summarized various of the noteworthy provisions in the New Code of Obligations pertaining to suretyship contracts that either did not exist previously, or will significantly amend the current legislative scheme once the new law enters into force.

The most practical implication of the amendment is the new requisite written form for entering into a surety contract. The former regime required that an agreement giving rise to a suretyship obligation be in written form in order to create a valid and binding obligation. The New Code of Obligations goes one step further and requires that the following elements of the contract be handwritten by the person agreeing to act as surety for another person's debt or obligation: (i) the maximum amount of liability to be assumed by the surety; (ii) whether joint and several liability is assumed; and (iii) the date of the agreement. The prevailing banking practice in Turkey has been the "just sign here" attitude, whereby the surety contract was reduced to filling in printed forms, and the surety signed the signature block without the bank having to document the surety's signature or the aforementioned primary elements of a surety contract. The goal of this amendment appears to be to ensure that the person providing the surety considers, understands and actively consents to the subject matter, amount and duration of this undertaking. Any power of attorney issued to allow the attorney to take on the liability for the debt or obligations of a third party, resulting in the principal becoming a surety, is subject to the same formal requirement. Any amendments to an existing surety contract, such as an extension of term or a variation in the amount of liability must also be in writing, setting forth the aforementioned contractual elements in the handwriting of the person agreeing to act as provider of the surety.

The new legislation appears to be partly driven by social policy, as it requires the written consent of the spouse of a natural person agreeing to act as surety. Spousal consent is also sought where the amount or nature of the surety contract is being amended.

A general principle of the suretyship law is that the liability of the surety is secondary to that of the debtor, unless the surety assumes joint and several liability (acknowledging this in writing, as noted above). The New Code of Obligations does not result in the surety becoming primarily liable *per se*, even where joint and several suretyship is established by contract. The new legislation requires that the creditor first demand that the defaulting debtor pay off the outstanding amount, and allows the creditor to seek repayment from the surety's assets if and when the creditor fails to recover such amount from the debtor, or if the debtor is insolvent and it does not seem likely that any such debt recovery effort will be successful.

The obligation to first seek repayment from the original debtor enables the surety to delay the creditor in seizure of the surety's assets. In cases where the debtor is in default and fails to make payment despite having been notified of his/her obligation, or he/she is in apparent financial hardship, the creditor may seek to recover its debt from the jointly and severally liable surety provider. Another significant change that would comfort joint and several sureties is that the creditor is required to, firstly, accept pledged assets or receivables through which to recover its debt. If the debt is secured by a pledge on receivables or personal property, the creditor must first force a

sale of the pledged property in order to satisfy the debt before proceeding to recover from the joint and several surety. There are also some exceptions to this provision. Should the court determine that the value of the pledged property does not suffice to satisfy the debt, or the debtor is bankrupt or enters into an arrangement with creditors, the creditors may then resort to the joint and several surety without having to resort to the aforementioned procedure.

The surety will not only be able to delay payments for reasons enumerated above, but will also be able to refrain indefinitely from payment should one of the causes identified in the New Code of Obligations emerge. To begin with, a surety will be liable only for those debts or obligations that came into existence after the formation of the surety contract, unless the contract expressly provides otherwise. The typical general loan agreement provision whereby the surety assumes responsibility for all kinds of debt and liability incurred, or that will be incurred, by the debtor against the bank will now have to be reconsidered. The person acting as surety may also object to payment should the debtor be rendered unable to make payment as a result of circumstances preventing his/her payment, e.g., restrictive foreign exchange controls. The debtor's waiver of a defense against the creditor (e.g., statute of limitations) will not preclude the surety from raising such defenses.

Finally, the liability of a natural person surety will expire at the end of ten years from the date of a surety contract. Should the contract provide for a period longer than ten years, the contract will still be enforceable for no longer than ten years, unless it is extended or renewed by duly observing the special written-form requirements identified above. The extension may again be for no longer than ten years, and it should be agreed to no earlier than one year prior to the expiration of the ten-year term of the initial surety contract.

The provisions of the New Code of Obligations pertaining to the special requirements in written form, eligibility for suretyship, and spousal consent will also apply to other forms of personal guarantees to be provided by natural persons. This provision is an attempt to prevent lenders from replacing sureties with guarantors in an effort to avoid the protective measures introduced to strengthen sureties against creditors.

Provisions 581 to 603 of the New Code of Obligations that address surety contracts, self-admittedly, aim to provide protection to sureties against economically superior lenders. These changes seem to restrict the freedom of contract as an instrument of social policy, most notably in the areas of the scope, enforceability and duration of the surety contract.

by Deniz Tuncel, Pelin Demirdere

UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS (CISG)

The United Nations Convention on Contracts for the International Sale of Goods (the "CISG") is a set of rules created with the aim of being "a modern, uniform and fair regime for contracts"[1] for the international sale of goods. The CISG entered into force on 1 January 1988 with eleven signatories and since that time, the number of member states has continuously increased. As of 1 August 2011, there are 77 states from different levels of economic development and legal traditions that have adopted the CISG. Since the majority of the states with which Turkey has commercial relations are members of the CISG, the convention is quite significant for Turkey. Finally, Turkey accessed the CISG on 7 July 2010[2] and it entered into force on 1 August 2011.

1 UNCITRAL. "United Nations Convention on Contracts for the International Sale of Goods (the CISG)." http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG.html

2 Turkey accepted the CISG on 7 April 2010 under decision numbered 2010/247, and Turkey submitted the Certificate of Accession to the United Nations on 7 July 2010.

After two previous conventions[3] failed to achieve high participation rate, the CISG is widely accepted as the rule book for the international sale of goods. Today, the CISG is the uniform international sales law of countries that account for over three-quarters of all world trade. There are various reasons for the wide acceptance of the CISG. There is no doubt that one of these reasons is the contractual balance it provides. The balance established between the interests of the seller and the buyer is structured so that the weaker party is protected from disadvantages it may experience under the applicable law. This balance is important in the motivation for the accession of, in particular, developing countries. It was also argued that another reason for the wide acceptance of the CISG is its flexibility[4]. With respect to the CISG's goal of unification of the international sale of goods, its terminology has been created in such a way that it comprises differing legal concepts. Hence, you will find terminology such as "exemptions" (CISG, Article 79) instead of "force majeure," "hardship," or "act of God." Similarly, "avoidance of contract" has been used, implicating different domestic legal concepts and interpretations.

The CISG is comprised of four parts. Part I covers the sphere of application and general provisions. Part II is concerned with the formation of international sale contracts. Part III provides for the sale of goods, and it includes provisions regarding the obligations of the seller and the buyer, remedies for breach of contract, passing of risk, exemptions and the effects of avoidance. In addition, Part IV sets out final provisions with respect to accession to the Convention and declarations and reservations that a contracting state may make under the Convention.

It should be noted that the CISG only applies to contracts for the international sale of goods between parties whose places of business are in different states. In addition, in order to apply the CISG, both parties' places of business must be in contracting states, or the rules of private international law must lead to the application of the law of a contracting state[5]. The autonomy of the parties is fundamental under the CISG. In this respect, the parties may both determine the CISG to be the applicable law by choosing the law of a contracting state as the applicable law,[6] or they may opt out from using the CISG in the contract by choosing the law of a non-contracting state as the applicable law or, the parties may choose the law of a contracting state and at the same time agree to derogate from the CISG[7].

Before the CISG entered into force in Turkey, in the event of an application to the Turkish courts for the resolution of disputes arising out of a contract for the international sale of goods, conflict rules were applied in order to determine the applicable law. However, as of 1 August 2011, the CISG became a part of the national law. In this respect, in the case of a contract between parties with a place of business in contracting states, the CISG will apply directly, and without the necessity of recourse to the rules of private international law. Furthermore, if Turkish law is determined as the applicable law in the contract, or if the rules of private international law lead to Turkish law, the CISG will prevail over the rules of the Code of Obligations or any other related legislation. Notwithstanding that the CISG is a set of substantive rules that aims to reduce obstacles, especially those associated with choice of law issues, the CISG still does not cover every issue that may arise from an international sale contract, such as validity of the contract, the effect of the contract on title to (the ownership of) the goods sold, error, mistake, fraud, and duress. These types of issues are left to be resolved by the applicable law determined by the rules of private international law. Therefore, the parties should bear in mind that a choice of law clause must be included in their contracts. The

3 The Uniform Law on the Formation of Contracts for the International Sale of Goods and Uniform Law for the International Sale of Goods

4 Introduction to the Digest of Case Law on the United Nations Sales Convention Note by the Secretariat. United Nations Commission on International Trade Law Thirty-Seventh Session New York, 14-25 June 2004.

5 The CISG, Article 1.

6 Hergüner, Ümit. "Applicability of the UN Convention on Contracts for the International Sale of Goods to Sales Contracts Concluded by Turkish Companies and their Affiliates Abroad;" Mistelis, Loukas. "CISG'nin Uygulama Alanı: Yer, Zaman ve Kişi Bakımından." p.15.

7 Schlectriem, Peter. "Requirements of Application and Sphere of Applicability." http://www.cisg.law.pace.edu/cisg/biblio/schlechtriem9.html.

parties of an international sale contract must also take into consideration the fact that there are no special tribunals created for the CISG. National courts or arbitration panels will apply the CISG when a dispute arises from an international sales contract.

In taking into consideration the fact that merchants in Turkey have many contracts for the international sale of goods, and also remembering the wide acceptance of the CISG, it was desirable for Turkey to access the Convention. Finally, as the CISG becomes a part of the national law, it is inevitable that Turkey will further benefit from the predictability of the CISG, together with the advantages of being subject to the same law with parties coming from different countries.

by Aysu Aliefendioğlu

THE NEW METHOD OF ALTERNATIVE DISPUTE RESOLUTION: ARE WE READY TO MEDIATE?

Mediation, as an alternative dispute resolution method, has been on the agenda of the European Union (the "**EU**") and Turkey for a long time. In 2002, a Model Law on International Commercial Conciliation was drafted by the United Nations Commission on International Trade Law as a guideline in order to harmonize the laws of mediation that may be enacted by member states. In 1998, the EU focused on resolving disputes occurring within EU borders through mediation and, in 2002, a "Green Paper" was published that established the main principles of mediation. Finally, through Directive 2008/52/EC (the "**Directive**"), certain aspects of mediation in civil and commercial matters were announced for member states. The Directive draws a framework within which mediation law is to be drafted and adopted by the member states, mainly concentrating on recourse to mediation, enforceability of agreements resulting from mediation, confidentiality, effects on limitation and prescription periods.

Looking at recent developments in Turkey, the Bill on the Mediation of Civil Disputes (the "**Bill**") prepared by the Ministry of Justice (the "**Ministry**") is still on the waiting list of the sub-committee of the Turkish Parliament. The Bill follows the framework set out by the Directive on certain issues mentioned above.

The Bill, as explained on its legal grounds, aims to decrease the volume of disputes brought before the courts, encourages litigants to reach amicable solutions voluntarily and facilitates easier access to justice, which is a right protected under the Constitution of the Republic of Turkey (the "**Constitution**").

The scope of mediation is defined as civil law matters, including those with foreign elements, in which the parties are free to decide. Under this Bill, the mediator is defined as a real person who conducts mediations and is registered with the Mediators' Registry through the Ministry. At the end of the mediation process, the mediator does not make a decision on behalf of the parties, but facilitates an amicable solution by encouraging communication between the parties. Since mediation strictly depends on the mutual agreement of parties, litigants are free to commence, continue or terminate the mediation process. The parties have equal rights when applying for, and during, the mediation process.

As per Article 13 of the Bill, litigants may agree to apply for a mediator prior to, or during, litigation before the courts. Also, the courts may counsel parties regarding the mediation procedure and encourage them to appoint a mediator. Unless otherwise agreed, if one party does not respond within thirty days to the offer of the other party to appoint a mediator, such offer is deemed to be rejected. Moreover, the parties are free to appoint one or more mediators and to agree on the mediation method to be used. In the event that the parties decide to apply for mediation after the dispute has been brought to the attention of the courts, court hearings will be adjourned for a period of three months. The adjournment period may

be extended upon the parties' mutual application to the court.

With respect to confidentiality, which may be the most sensitive issue of the mediation process from the view of the litigants, the Bill obliges mediators to keep confidential all information that comes to light during the mediation process, and the parties are also bound by such a confidentiality obligation unless otherwise agreed. Moreover, the parties, the mediator(s) or any other third party, including those involved in the mediation process, shall not present the following documents and statements as evidence before a court or arbitration tribunal regarding the same dispute: *(i)* invitation to mediate by one party, or either party's willingness to participate in the mediation process; *(ii)* comments and offers made by either party to resolve the dispute through mediation; *(iii)* proposals made by one of the parties, or acceptance of a claim or incident during the mediation process; *(iv)* documents drafted solely for the mediation process. However, such information may be disclosed where it is required by law, or to the extent that it may be necessary to implement or enforce the agreement reached at the end of the mediation.

Moreover, in order to avoid any loss of right, the Bill specifically regulates the effect of mediation on limitation and prescription periods. Accordingly, the period between the commencement and cessation of the mediation process shall not be counted in the calculation of limitation and prescription periods.

Furthermore, with respect to enforceability of agreements, the Bill enables the parties to apply for an execution court to ensure that the agreement arising from the mediation is enforceable. The examination made by the court will be a limited examination as to whether such dispute is a matter wherein parties are free to decide, and that the final mutual agreement is executable.

Finally, it is accepted that mediation is terminated if: *(i)* the parties reach a mutual agreement on the dispute; *(ii)* it is ascertained by the mediator following consultations with the parties that efforts towards mediation have been rendered useless; *(iii)* either party notifies the other party or the mediator of its withdrawal from the mediation; or (iv) the parties mutually agree to terminate the mediation process.

As mentioned above, the Bill has parallel provisions with the Directive. However, despite the moderate views on mediation in the EU member states, there are many counterviews and criticisms in the legal arena within Turkey regarding the mediation process. Opponents base their arguments on a number of grounds in the Constitution, namely, Article 6 that imposes the "state governed by the rule of law" principle; Article 9, which states that the judicial power shall be exercised by independent courts on behalf of the Turkish nation; Article 138, which affirms that no organ, authority, office or individual may give orders or instructions to courts or judges relating to the exercise of judicial powers, send circulars, or make recommendations or suggestions; and, finally, Article 142, which states that the organization, duties and authorization of the courts, their operation and execution procedures shall be regulated by law. The Bill's opponents claim that, if enacted, it would be struck down by the Court of Constitution based on the Articles of the Constitution mentioned above. Moreover, Turkish bar associations and attorneys have also expressed their opposition to mediation each time it comes up as an item on the agenda of the Turkish Parliament, alleging that the Bill is a political instrument, rather than a legal one that aims to facilitate easy access to fair and swift resolution of disputes.

It seems that we will witness a sizeable change in the judicial environment in the country during the implementation of this dispute resolution instrument in practice, if opposing parties are able to achieve their own mediation and the Bill becomes law.

by M. Tuğçe Özdeş

TURKISH RAILWAY SECTOR, QUIET BUT NOT QUIESCENT

Privatization of existing highways and construction of new roads, bridges and tunnels, massive PPP projects in the healthcare sector, and the tender for the 3rd Bosporus Bridge spiced up the PPP and privatization activities in 2011. Although privatization of the railways or any other type PPP projects in the railway sector is not officially scheduled for the near future, when the pieces are put together, it appears that PPP activity in this sector is highly likely in 2012.

Railways in Turkey

According to the Decree-Law regarding Organization and Duties of the Ministry of Transportation, Maritime Affairs and Communications (the "**Ministry**") that entered into force in the last quarter of 2011[1] (the "**Decree-Law**"), the General Directorate of Infrastructure Investments[2] is responsible for the planning, design and construction of railway infrastructure and transfer of these to the relevant authorities for operation. On the other hand, operation, maintenance and renewal, *inter alia,* of railways is a duty assumed by the Turkish State Railways[3] (the "**TCDD**") that is organized as a public economic enterprise pursuant to the Decree-Law dated 8 April 1984 and numbered 233 on Public Economic Enterprises[4] ("**Decree No. 233**"). Accordingly, the TCDD has its own legal personality as well as articles of association and separate capital and, notwithstanding certain exceptions, it is subject to private law instead of administrative law in its activities.

As per the statistics published in 2010 by the TCDD, the total length of Turkish railways is 11,940 km, composed of 888 km of high-speed train lines and 11,052 km of conventional lines. Around 85 million passengers were transported by train in 2010[5]. When the capacities of road and air transport are taken into account, the share of rail transportation is 4% for passenger carriage and 7% for freight carriage in the overall transportation pie[6]. Thus, railways made a rather insignificant contribution to solving Turkey's transportation problems. The TCDD's balance sheet for the 2010 fiscal year confirms that state subsidies constitute a considerable portion of its income. While in recent years, the TCDD focused on investments in high-speed train lines and sought to finance them through privatization of six (6) ports owned and operated by the TCDD, its capital needs are still immense. In this sense, establishing partnerships with private investors under the PPP model is now being articulated by the TCDD alongside many other authorities.

Developments in Foreign Railways

Examples from around the globe demonstrate that especially in countries where railways' contribution to transportation is relatively low, private companies' involvement increases productivity and resource allocation efficiencies.

Privatization methods differ depending on the political and financial landscapes of the countries in which private companies assume railway activities. For example, in the UK, in order to privatize British Railways, rolling stock assets were transferred to private companies through lease agreements, whereby rail track maintenance and renovation activities were left to regional rail infrastructure companies, and the operation of passenger carriage services were franchised to operating companies.

Unlike the UK example in which operations, maintenance and infrastructure investment activities were assumed by different private sector participants,

1 Published in the Official Gazette dated 1 November 2011 and numbered 28192

2 "Altyapı Yatırımları Genel Müdürlüğü" in Turkish

3 "Türkiye Cumhuriyeti Devlet Demir Yolları" in Turkish

4 Published in the Official Gazette dated 18 June 1984 and numbered 18435

5 Source: TCDD

6 Source: General Directorate of Railways Harbors, and Airports Construction (DLH)

in some African countries, private companies were engaged in railways under concession methods and were responsible both for the rolling stock operations and maintenance of the infrastructure.

Where European and African countries tend to engage private companies in railways through the privatization of existing infrastructure and rolling stocks or by concessions, new projects implemented in the Middle East pursue the PPP model. As a recent example, the 1,080 km railway projected implemented in Jordan will be completed under the build-transfer-operate model foreseeing the project to be funded by a state-owned company, built by private investors and transferred to the government, and then operated by private investors in return for infrastructure usage fees.

Developments in Turkish Railways

In 2005, the TCDD introduced a restructuring program and as a part of this program, a regulation for allowing private investors to engage in railway carriage activities was adopted in the same year. According to the Regulation on Operations of Rolling Stock owned by Third Parties on Railways of TCDD[7] (the "**TCDD Regulation of 2005**") both Turkish and foreign private entities were allowed to operate passenger and cargo trains within the TCDD's infrastructure under operation agreements. By permitting the private sector to engage in railway operations activities, the TCDD Regulation of 2005 has been perceived as a quasi-privatization of rolling activities without any tender or competition from amongst the interested parties.

The Council of State, by its decision of 27 February 2007, stated that in order for privatization of TCDD's services, the procedure provided for under Law No. 4046 on Privatization Procedures[8] (the "**Privatization Law**") should have been followed and the mere enactment of the TCDD Regulation of 2005 is, by no means, the legal basis for private parties to assume rolling activities. It thereby cancelled the TCDD Regulation of 2005. Nevertheless, limited private sector activities still continue under various pieces of TCDD regulations and the powers of TCDD under its articles of association.

Another striking development on the railways front is the draft law prepared in mid-2008 regarding the restructuring of the TCDD and the establishment of a new subsidiary for railway operations activities. In harmony with the relevant EU legislation aiming to unbundle railway infrastructure and carriage activities, the TCDD issued the first draft of the Law on Restructuring the General Directorate of the TCDD and on Establishment of Türkiye Demiryolu Taşımacılığı A.Ş[9] (the "**Draft TCDD Restructuring Law**"). According to the Draft TCDD Restructuring Law, the TCDD will be responsible for, *inter alia,* the construction and maintenance of railways and operations of train stations and traffic management, whereas Türkiye Demiryolu Taşımacılığı A.Ş. ("**DETAŞ**") will engage in passenger and freight carriage and other supplementary activities. Moreover, in its general preamble, the TCDD states that private companies will also be allowed to engage in railway carriage activities.

The Draft TCDD Restructuring Law also establishes procedures in connection with privatizations under the leasing and/or the transfer-of-operation-rights method. Accordingly, the board of directors of the TCDD will be authorized to adopt privatization decisions and to submit tenders for the leasing and/or transfer of operation rights in accordance with Law No. 4046 for a period of no longer than 49 years.

Aside from these legislative drafts, inclusion of the private sector into the railway industry is cited also in recent strategy documents and development plans. For instance, the 9th Development Plan[10]

7 Published in the Official Gazette dated 19 April 2005 and numbered 25791

8 Published in the Official Gazette dated 27 November 1994 and numbered 22124

9 "Turkish Railway Carriage Joint Stock Corporation" in English

10 Published in the Official Gazette dated 1 July 2006 and numbered 26215

relating to the period between 2007 and 2013 foresees partnerships with private companies for the construction of new railway infrastructure and, in particular, construction of new high-speed train lines. Moreover, following general elections in 12 July 2011, the program issued by the 61st Government has also reiterated Turkey's need for new railway infrastructure and stated that new PPP projects will be implemented for construction of new transportation infrastructure. At his recent speech last December, the Turkish Minister for Transportation, Maritime Affairs and Communications announced that in order to enable private sector participation in the railway sector, the Ministry commenced studies for creating the necessary background.

In addition to these efforts, the Decree-Law also foresees establishment of the General Directorate of Railway Regulation[11], another public authority under the auspices of the Ministry that will be responsible, *inter alia,* for determining the working principles and financial capability thresholds for railway infrastructure operators, rolling stock operators, and for determining the minimum and maximum rates for infrastructure usage fees and supervising the infrastructure operators and rolling stock operators. It is expected that this will encourage involvement of private sector participants in the railway sector.

Future of Railway Activities in Turkey

Considering the legislative developments, the need for new infrastructure and the government's tendency to establish partnerships with private companies, it will be of no surprise that private entities will be introduced into the Turkish railway sector in the coming years. In light of the government's statements, it may be assumed that rather than privatization, involvement of private entities in the sector will most likely be realized through PPP projects.

When the population of Turkey and the potential for transportation is taken into account, it is obvious that if managed efficiently, Turkish railways will be a profitable investment for private entities as well. As per the current picture, interested parties must await the enactment of the Draft TCDD Restructuring Law; however, once the long-awaited draft PPP-specific law that will clarify several key points of the PPP projects, such as risk-sharing, direct agreements, etc. enters into effect, possibly within 2012, these activities are likely to boom in Turkey.

by Utku Ünver

11 "Demiryolu Düzenleme Genel Müdürlüğü" in Turkish

RECENT DEVELOPMENTS IN THE TURKISH RENEWABLE ENERGY MARKET

The Law on the Utilization of Renewable Energy Resources for Electricity Generation (the "**RES Law**"), enacted in 2005, was far from satisfying the needs of investors who have carried the burden of costly investments. The initial form of the RES Law also had limited impact on the market due to its modest and uncompetitive feed-in tariff regime. In order to overcome these shortcomings of the RES Law, the government has prepared a bill that includes amendments to offer higher feed-in tariffs. While these amendments were not put into effect for a long time for various reasons, the Turkish Parliament finally saw fit to enact them on 29 December 2010, and they became effective as of their publication; *i.e* 8 January 2011 (the "**Amendments**"). Even though the effects of the Amendments in the market are still to be witnessed over time, they introduce numerous advantages that have been long-awaited by investors.

Conditions to Benefit from the Advantages

Scope of the RES Law: The RES Law defines renewable energy facilities that are within its scope as wind, solar, geothermal, biomass, biogas (including landfill gas), wave, drift, tide, and hydroelectric power plant facilities that are either (i) channel-type or river-type, or (ii) whose reservoir area is less than 15 km^2.

RES Certificate: The generation licensees that generate electricity from the above-mentioned

renewable energy resources are eligible to receive a RES certificate from the Energy Market Regulatory Authority (the "EMRA"). Facilities holding a RES certificate are allowed to participate in the Renewable Energy Support Scheme according to the generation amount indicated under their RES certificate.

Advantages Introduced by the Amendments

Investment Incentives

Priority for system connection: During the evaluation of the license applications, with regard to the preparation of the system connection opinion, generation facilities using renewable energy resources have priority over other applications.

Financial Incentives

Renewable Energy Support Scheme (the **"Support Scheme"**): The electricity supply companies are obliged to financially participate in the Support Scheme *pro rata* to the electricity amounts they have supplied. In other words, it is indirectly imposed upon these companies to purchase electricity that is generated from renewable resources. Generation license holders have the right to receive such payments *pro rata* to the generation amounts indicated under their RES certificates. However, it is not mandatory, but optional, for generation facilities to enter into the Support Scheme. The licensee may decide to receive the RES certificate that is a pre-condition for participation in the Support Scheme. The Support Scheme is organized annually, and the licensees that wish to benefit therefrom must apply by 31st of October in order to be eligible for the following year.

Feed-in tariffs: The highest tariff under the Support Scheme is determined for biomass and solar energy facilities. Furthermore, the facilities that utilize components manufactured in Turkey benefit from a higher feed-in tariff. Below is a list of the financial incentives granted to electricity generation facilities using renewable energy resources:

Type of Electricity Generation Facility using Renewable Energy Resource	Applicable Prices (US Dollars cents / kWh)
Hydroelectric	7.3
Wind	7.3
Geothermal	10.5
Biomass (including landfill gas)	13.3
Solar	13.3

Use of Made-in-Turkey Technology: Generation facilities that fall within the scope of the Support Scheme and which become operational prior to 31 December 2015, benefit from an extra financial incentive in addition to their corresponding feed-in tariff, if they use mechanical and/or electronic components that are manufactured in Turkey. Below is a list showing the incentives that vary depending on the domestic component used:

Type of Electricity Generation Facility using Renewable Energy Resource	**Components Manufactured in Turkey**	**Additional Price (US dollars cents/kWh)**
Hydroelectric	*Turbine*	1.3
	Generator and power electronics	1.0
Wind	*Wing*	0.8
	Generator and power electronics	1.0
	Turbine	0.6
	Entire mechanical components in rotor and nacelle groups (excluding payments for wing group and generator and power electronics)	1.3
Photovoltaic ("PV") solar energy	*Production of PV panel integration and solar structural mechanics*	0.8
	PV modules	1.3
	Cells constituting the PV modules	3.5
	Inverter	0.6
	Material that focuses solar rays to the PV module	0.5

Condensed solar energy	*Radiation collection*	2.4
	Reflector surface	0.6
	Solar tracing system	0.6
	Mechanical parts of the heat storage	1.3
	Mechanical parts of the tower steamer collecting solar rays	2.4
	Stirling engine	1.3
	Panel integration and structural mechanics of the solar panel	0.5
Biomass	*Fluid-bed stream boiler*	0.8
	Fluid or gas-run steam boiler	0.4
	Gasification and gas cleaning group	0.6
	Steam of gas turbine	2.0
	Internal combustion or stirling engine	0.9
	Generator and power electronics	0.5
	Co-generation system	0.4
Geothermal	*Steam or gas turbine*	1.3
	Generator and power electronics	0.7
	Steam injector or vacuum compressor	0.7

Purchase Obligation: Under the RES Law, all electricity supply companies are obliged to purchase electricity that is generated from a renewable resource.

Electricity Generation for Self Needs: The generation facilities using renewable energy resources with an established capacity lower than 500 kW are allowed to deliver the electricity that they generate beyond their own needs to the distribution system at the above-mentioned prices for ten years. In this case, the relevant distribution company is obliged to purchase such electricity.

Land Allocation:

Forest lands and state-owned lands: For the purposes of electricity generation from renewable energy resources within the scope of the RES Law, the Ministry of Environment, Forestry and Urbanism or the Ministry of Finance may, in consideration for remuneration, lease forest lands and state-owned lands, or establish servitude or usage rights thereon, or grant authorizations thereto, if such land will be used as a facility, access road and electricity transmission line up to the network connection point.

Discount: Facilities that hold a RES certificate and are already in operation, or will become operational by 31 December 2015, benefit from a 85% discount in relation to authorization, lease, servitude right and usage rights fees regarding their generation facilities, access roads and electricity transmission lines up to the network connection points as set forth in their licenses for the first ten years of the investment and operation. Moreover, certain additional fees such as ORKÖY or forestry special funds are not collected in relation to such lands.

National parks, natural parks and other environmentally significant areas: Generation facilities using renewable energy resources may be established on national parks, natural parks, natural monuments, natural preservation areas, forests, fields for developing wild life and special environment protection zones and protected areas, subject to the positive opinion of the relevant ministry or relevant protection regional council.

Treasury share: The 1% treasury share is not collected from the generation facilities that possess a RES certificate.

Turkey's national strategy documents prove the country's desire for growth in the renewable energy market. Accordingly, Turkey is expected to establish 10,000 MW wind and 300 MW geothermal capacities by 2014. In addition, Turkey's solar energy potential is indicated as 380TWh/year according to the Ministry of Energy and Natural Resources' data. With these figures as forecasted, Turkey hopes that the new legislative developments will serve its purpose for becoming a major player in the renewable energy sector.

by Aslı Orhon and U. Sarper Boz

CROSS-BORDER ENERGY TRADING LEGISLATION FURTHER LIBERALIZED

The past decade has witnessed a giant leap forward in the Turkish energy sector since the 2001 enactment of the Energy Market Law. Both the government and the relevant supervisory authority, the Energy Market Regulatory Authority (the "**EMRA**"), have been actively working to find legislative methods for gradually transforming the energy sector into a more investor- and trader-friendly business environment. This is especially the case for the domestic energy trade, the latest steps of which introduced the day-ahead market, a radical decrease in eligible consumer consumption thresholds from 100,000 kW to 30,000 kW annually (with the hint of even further decreases), and retailer licenses made available to all eligible license-holders (replacing the previous exclusivity for distributors). All of these have come to fruition in 2011.

Along with this flurry of activity in the national market, the EMRA has also upgraded the energy import and export legislation. Many local and foreign energy traders have been waiting for legislative changes that would allow them to trade electricity across Turkish borders at more competitive prices.

Legislative Limitations on Cross-Border Trade

Today, Turkey has interconnection lines installed with pre-determined transfer capacities to Bulgaria, Azerbaijan (Nakhchivan), Iran, Georgia, Armenia, Syria, Iraq and Greece. All electricity import-export activities are currently subject to the EMRA's approval.[1] All interconnection allocations are granted for 1-year terms. As the construction of the cross-border interconnection lines is limited in nature, the EMRA closely monitors full exploitation of capacity by each respective right-holder. If the EMRA decides that a right-holder is not using the full capacity of the interconnection lines efficiently, it revokes the capacity allocation and reallocates the usage right of the lines to other interested applicants.

The EMRA, together with the Turkish grid operator, Türkiye Elektrik İletim A.Ş. ("**TEİAŞ**"), follow up the ongoing collaboration efforts with the European Network of Transmission System Operators for Electricity (the "**ENTSO-E**") to interconnect and synchronize the Turkish electricity network with the ENTSO-E. Once fully implemented, a network synchronized with the ENTSO-E will enable both networks to operate as a single energy market, where spot buy-sell transactions may be conducted on an hourly and daily basis. To this end, on 18 September 2010, TEİAŞ and ENTSO-E started test transmissions over existing lines in Bulgaria and Greece.

New Electricity Export Import Regulation

In an effort to provide a legal basis for the campaign for synchronization with the ENTSO-E, as of 01 June 2011, the EMRA renewed the governing regulation piece on cross-border energy trading, namely, the Electricity Market Export and Import Regulation (the "**New Ex-Im Regulation**"), annulling the Previous Ex-Im Regulation, identically named, dated 07 September 2005 (the "Previous Ex-Im Regulation").

The New Ex-Im Regulation does not directly pave the way for spot transactions, as the addressed transmission method applies to long-term capacity allocations. As was the case in the Previous Ex-Im Regulation, the New Ex-Im Regulation foresees that prospective import-export license-holders will be granted 1-year reserved capacities.

1 Before granting approval, the EMRA also seeks the technical opinion of the Ministry of Energy and Natural Resources, TEİAŞ and/or other distribution license-holders. Once the approval is granted, the application is announced on the EMRA's website for other potential purchasers. If there is more than one interested party for the same interconnection line allocation, the EMRA will decide on the winning contract in consultation with TEİAŞ and other relevant distribution license holders.

European and Non-European Connections

The New Ex-Im Regulation, as it was in the Previous Ex-Im Regulation, classifies cross-border electricity trade under two headings: **(i)** sales made over synchronous lines and **(ii)** sales made over asynchronous lines. What is referred to as a synchronous line practically addresses connections established with the ENTSO-E grid ("**European Connections**") and as ENTSO-E is currently the only synchronous line TEİAŞ has with its neighboring grid operators. What the New Ex-Im Regulation classifies as asynchronous lines refers to all cross-border connections other than ENTSO-E connections in place with Greece and Bulgaria ("**Non-European Connections**").

TEİAŞ is aiming to operate a synchronous grid using the ENTSO-E system. While much of the limitations imposed by the Previous Ex-Im Regulation still apply to sales on Non-European Connections, provisions applying to sales on European Connections have been further liberated.

Below are some points that are detailed for comparison purposes.

Right to Sell in Secondary Markets

Perhaps the foremost privilege granted by the New Ex-Im Regulation to traders on European Connections is the right to re-sell the allocated electricity capacities to third parties. Article 17 of the New Ex-Im Regulation resolves that capacity holders of synchronized parallel connections, having received the approval of the system operator, will be entitled to sell their capacity to third-party import-export license-holders in "*secondary markets*."

Secondary markets may be considered as spot markets currently available for domestic trade (in day-ahead planning and real-time balancing). This right was not granted under the Previous Ex-Im Regulation, and still is not granted to traders operating under Non-European Connections.

Apart from the New Ex-Im Regulation, the EMRA issued another set of rules to help clarify the transfer procedures to secondary markets on 17 June 2011, namely the *Electricity Market Export and Import Regulation Rules on Capacity Allocations and Secondary Commercial Transmission Right Market* (the "**Secondary Market Rules**").

Transfers Exclusive to License-Holders

In the Secondary Market Rules, secondary markets are defined under the term "Secondary Commercial Transmission Right Market", that is stated as being mechanisms which allow for transfer of the commercial transmission rights (capacity allocations) of a license-holder to other wholesalers.

As a set-back, however, the New Ex-Im Regulation, together with the Secondary Market Rules, although having introduced a secondary market sale option, still require that the transferring wholesalers be EMRA-licensed wholesalers. Secondary Market Rules Article 10 states that a "Commercial Transmission Right" (a "**CTR**") may only be transferred to another licensed market participant.

Despite its novelties, the new legislation did not change the existing framework of the physical energy trade, where such physical delivery undertakings are still exclusive to the EMRA license-holders (and to eligible consumers). Furthermore, this transfer is subject to the prior approval of the system operator (system operator being understood to be TEİAŞ or the bordering distribution license-holder).

Spot Sales Not Yet Addressed

Under the New Ex-Im Regulation, the interconnection lines are still made available to applicants as long-term capacity allocations, meaning that the transfer of this capacity to third parties may only be made similarly through long-term capacity transfers. Legal framework still does not address cross-border spot sales transfers.

No Physical Delivery Obligation

Sales conducted over European Connections are no longer required to fully exhaust their allocated

capacity. Unlike the Previous Ex-Im Regulation that obliged the cross-border energy sales parties to honor their physical delivery obligations, the New Ex-Im Regulation appears to have created legal space for option sales for the parties. Parties of the sale are allowed to not fulfill their physical delivery commitments, should they reach an agreement to do so.

Article 11 of the Secondary Market Rules specifically outlines that the CTR holders who do not fully use their allocated capacities will not be charged any fines or penalties. The Previous Ex-Im Regulation foresaw that license-holders for all cross-border connections both for European and Non-European Connections were expected to fully honor their physical delivery obligations, and were subject to cancellation of their import-export license if their cross-border trade fell below 60% of their monthly commitments, or under 70% of their quarterly commitments.

Article 20 of the new Export Import Regulation grants a favorable exception to European Connections, imposing the above-stated commitment threshold only on license-holders operating on Non-European Connections.

Free Contract Terms

Another difficulty facing cross-border traders under the Previous Ex-Im Regulation was that the EMRA had the authority to intervene in all energy import-export contracts. Import-export contracts had to be fully disclosed to the EMRA together with all of their annexes. Any amendment to the terms of the contract was also subject to the EMRA's approval. As the term, capacity and transmission methods were stated on the license of the import-export license-holder, any amendments and changes to these figures would also trigger amendment of the license. This is no longer the case for sales conducted on the European Connections under the New Ex-Im Regulation. CTR holders are not obliged to disclose their agreements, nor are those contracts subject to the EMRA's approval.

Derivatives Contract for Non-Physical Electricity Exchange

Besides the changes introduced through the Export and Import Regulation, the Turkish energy market saw another development in 2011, namely, the initiation of non-physical electricity exchange. The Turkish Derivatives Exchange (the "**TDE**"), in collaboration with the EMRA, and with the approval of the Capital Markets Board, issued a form contract for "Base Load Electricity" Derivatives Sales, numbered 601-613 (the "**TDE Contract**") dated 22 July 2001. As of 26 September 2011, market players are entitled to buy-sell electricity according to the terms of the TDE Contract.

The TDE Contract currently allows only for non-physical electricity sales. More accurately, the contracting parties position themselves for assuming buy-and-sell options fixed on index electricity prices that are calculated over the monthly average on the planning figures of the day ahead as defined in the Electricity Market Balancing and Settlement Regulation. So to speak, a transaction that is based on a TDE Contract will not affect the amount of electricity exchanged through the national grid or cross-border grids. Therefore, the current legislation allows all investors and traders to be a party to the TDE Contract, even if they are not EMRA licensed market players.

The TDE Contract may provide to interested parties, what the Export and Import Regulation lacks in defining secondary electricity markets: The transactional ability to freely exchange derivatized electricity across national borders between all interested parties, without requiring any permits or licenses to do so. However, one should remember that as of now, this ability is still limited to non-physical deliveries.

We are hopeful that the EMRA, with its current praiseworthy momentum, will continue to create more legal space to the liberalized energy market.

by Alper Koç

A NEW ERA IN RADIO AND TELEVISION BROADCASTING

After the enactment of Law No. 6112 on the Establishment of Radio and Television Enterprises and their Broadcasting Services (the "**New Broadcasting Law**") on 3 March 2011, the Radio and Television Supreme Council (the "**RTUK**") commenced work on the drafting of new regulations that needed to be issued within the scope of the New Broadcasting Law. The pace of drafting accelerated in May and June, and a total of ten new regulations[1] were issued to replace their former versions.

Among these newly enacted regulations are two that are particularly important because they are directly related to the media service providers. The remainder are mainly concerned with RTUK's internal structure and the basic principles of television and radio broadcasting, in terms of content and the technical aspects of broadcasting.

Of the important new regulations, (i) the Regulation on Administrative and Financial Conditions Applied to Media Service Providers, Platform and Infrastructure Operators, published in the Official Gazette dated 15 June 2011 and numbered 27965 (the "**Regulation on Administrative and Financial Conditions**") aims, among other things, to dispense with restrictions regarding the shareholding structure of media service providers in line with the New Broadcasting Law, while (ii) the Regulation on Annual Frequency Usage Fees Applied to Radio and Television Institutions for Terresterial Broadcasts, published in the Official Gazette dated 29 April 2011 and numbered 27919 (the "**Usage Fee Regulation**"), details the new "*usage fee*" that was a concept introduced by the New Broadcasting Law.

Regulation on Administrative and Financial Conditions

The New Broadcasting Law revisited the foreign shareholding restrictions applicable to media service providers. The law made an attempt to loosen foreign shareholding restrictions and to provide media pluralism and content diversity by preventing a concentration of media ownership. However, the drafting of the provision regarding foreign shareholding restrictions under the New Broadcasting Law is vague and leaves too much room for interpretation.

The New Broadcasting Law states that "*the direct foreign shareholding capital contribution cannot exceed 50% of the paid-in capital. A **foreign** real or legal person may become **a direct** shareholder in a maximum of two media service providers*."

Neither the Broadcasting Law nor the Regulation on Administrative and Financial Conditions clarifies how the above-mentioned restrictions will apply in the case of an "indirect" shareholder. The Regulation also basically recites the Law. While a literal reading suggests there are no longer any limits to indirect shareholdings that go above 50%, the matter should be approached with caution.

While explaining the general shareholder concentration restriction (applicable to all shareholders – not only to foreign entities) permitting shareholding in four different entities, both the New Broadcasting Law and the Regulation on Administrative and Financial Conditions refer to "direct" and "indirect" shareholding separately through the wording, "*a real or legal person may be a **direct or indirect** shareholder in a maximum of four media service providers that provide terresterial radio and/or television broadcasting services*." Neither the New Broadcasting Law nor

1 Eight of the new regulations pertain to licensing and other requirements applicable to broadcasting entities, such as: the Regulation on Administrative and Financial Conditions; the Usage Fee Regulation; the Regulation on Commercial Communications Revenues; the Satellite Broadcasting Regulation; the Cable Broadcasting Regulation; the Regulation on the Cancellation of the Regulation on Copyrights; the Regulation on the Cancellation of the Regulation on Closed Circuit Radio and Television Broadcasts; and the Regulation on the Cancellation of the Regulation on IPTV Licenses. The two remaining new regulations, namely, the Regulation on Examinations Applied to RTUK Experts for Admission, and the Regulation on the Disciplinary Principles of RTUK, concern internal administrative procedures of RTUK.

the Regulation on Administrative and Financial Conditions clarifies the questions on indirect shareholding as per the limit of 50% in one media service provider entity, even though this matter has been brought to the attention of RTUK many times through questioning. Thus, it may be argued that RTUK has deliberately refrained from clarifying the foreign shareholding restriction in the event of "indirect" ownership, in order to retain for itself some discretion and room for maneuvering.

Annual Usage Fee Regulation

The New Broadcasting Law also introduces another new topic of debate as to how the usage fee will be calculated and collected, and how it will be applied to media service providers throughout Turkey who operate on different financial scales.

The main point of discussion point is that if an identical or similar usage fee is applied to all media service providers regardless of their financial status and infrastructure, it would most likely hurt local and smaller providers, since they may not be able to afford such usage fees. In this respect, media market pluralism may be negatively affected. This debate ended when the Usage Fee Regulation entered into force in April 2011. The new regulations set forth a complex method of calculating the usage fees by taking into account many variables, such as the emission power of the relevant media service provider, the number of people within the coverage area, as well as the development level of the city where the media is broadcast, in addition to an annual co-efficient determined at the sole discretion of RTUK. In this respect, the calculation of the usage fees has a number of criteria that enable media service providers to pay according to their capabilities.

Immediately after the enactment of the Usage Fee Regulation, RTUK collected the first installment of usage fees in July 2011 that totalled TL 14,000,000 from media service providers who broadcast radio and television programming via terresterial transmitters. Taking into account the total amount paid to RTUK as the first installment, we assume that this will be one of the more significant revenue items for RTUK.

Tender for Terresterial Broadcasting License

RTUK commenced its preparations for frequency planning in order to open a tender for terresterial television and radio broadcasting licenses. To this end, in March, 2011, RTUK organized a tender for purchasing technical services from private software developers and frequency planners. In this respect, the objective of RTUK is to complete frequency planning by 2012 and to redistribute terresterial broadcasting licenses to media service providers in 2012. The Turkish media sector is at the brink of a material change as we enter 2012.

by Güneş Akman

CULTURAL ASSET OR NATURAL ASSET? THIS IS THE QUESTION

Through recent developments, the ministry structure of the Republic of Turkey has been reformed, including the division of the Ministry of Environment and Forestry into two separate ministries, now (i) the Ministry of Environment and Urbanzation (*Çevre ve Şehircilik Bakanlığı*) and (ii) the Ministry of Forestry and Waterworks (*Orman ve Su İşleri Bakanlığı*). In line with the new structure, Decree No. 644 (the "**Decree**"), introducing the principles of the new Ministry of Environment and Urbanization, was enacted. This Decree was followed by Decree No. 648 (the "**Amendment Decree**") that amends several laws and decrees, including the Law on Preservation of Cultural and Natural Heritage numbered 2863, dated 1983 ("**Law No. 2683**") ("*Kültür ve Tabiat Varlıklarını Koruma Kanunu*").

Until the recent amendments to Law No. 2683, the Preservation Boards, having autonomous board members who were directly appointed either by the

Ministry of Culture and Tourism or by the Higher Education Council, were only established under the Ministry of Culture and Tourism. Law No.2863 sets forth that all movable and immovable properties having a genuine cultural value related to a specific historical period in terms of science, culture, religion or fine art are defined as "cultural assets," while the environmentally or archeologically reserved properties established under or above ground are defined as "natural assets." As per Law No. 2863, the Preservation Boards were entitled to assess any property and define whether it is a natural or cultural asset. Upon such assessment, the Preservation Boards were entitled to set forth the preservation principles that are designated specifically for such asset and are applicable during the transactional period and, and remain in full force until the completion of the preservation zoning plan (the "**Transactional Period Preservation Principles**"), in coordination with the members of the relative professional chambers, non-governmental organizations and civilians, who will be affected by such decision. Furthermore, the Preservation Boards had also been entitled to impose orders and instructions upon such property owners regarding their maintenance and repair works on these assets, and all issues related to these assets were subject to the Preservation Board's approval. In other words, all construction-related issues regarding any building that is defined as either a "cultural asset" or "natural asset," were subject to the Preservation Board's approval.

The Amendment Decree brought with it a completely new set of fundamentals regarding the structure and operation of the Preservation Board. Accordingly, the authority of the Preservation Board covers both "natural assets" and "cultural assets."

Cultural assets are continuing under the auspices of the Preservation Board under the supervision of the Ministry of Culture and Tourism (the "**Cultural Preservation Board**"). The Cultural Preservation Board will continue to determine whether an asset falls under the definition of a "cultural asset." Furthermore, the Cultural Preservation Board is also authorized to take required measures for the protection of cultural assets, and to determine the terms and conditions for the maintenance, repair and renovation of "cultural assets." However, the memberships associated with the Cultural Preservation Boards have been terminated in line with Provisional Clause 10 of Law No. 2683. Accordingly, no decision may be made by the Cultural Preservation Boards until the new members have been appointed. This causes delay in investments relating to "cultural assets" and, therefore, investors are looking forward to the appointment of new board members.

On the other hand, "natural assets" are excluded from the authority of the Ministry of Culture and Tourism, and the Ministry of Environment and Urbanization has assumed full authority with respect to "natural assets." Accordingly, natural assets will be subject to the examination and approval of the General Directorate of the Preservation of Natural Assets to be established under the Ministry of Environment and Urbanization (the "**Directorate**"). In other words, the former Preservation Board's powers and duties with respect to natural assets have been revoked, and their duty to assess and preserve natural assets has been transferred to the Directorate.

The Decree set forth a wide range of powers given to the Ministry of Environment and Urbanization over the regulation of secondary legislation, application and controlling of the legislation on zoning, construction and environment, preparation of zoning and parcelling plans, and taking relevant measures against the environmental pollution. With the recently delivered powers, the Ministry of Environment and Urbanization is also authorized to directly appoint the members of the Directorate.

The Ministry of Environment and Urbanization is assigned to review all of the necessary former decisions made regarding natural assets within six months and re-evaluate such decisions. Until the re-evaluation is finalized, in line with Provisional

Clause 6 of the Decree, all of the previous decisions remain in full force and effect. However, as the duties of the former Preservation Board members have been terminated and the new boards and directorates are not yet formed, it has thus become virtually impossible to apply for or receive any further decisions before the establishment of the new boards/directorates. Furthermore, the former decisions of the Preservation Boards regarding natural assets may also be reversed by the Ministry of Environment and Urbanization. As per Article 13/A of the Decree, the newly established Directorate will not be required to coordinate with any other legal or real person, other than the Ministry of Environment and Urbanization. This provision is criticized as it gives ultimate authority to the Ministry of Environment and Urbanization for the determination and disposition of "natural assets."

This recent change introduced by the Amendment Decree gives great flexibility to the current government to set the criteria for development of treasury lands and/or former forestry areas. The main discussion regarding the Amendment Decree is the amendment of a law, along with a decree. The implementation of a law requires certain procedures and the approval of the National General Assembly; however, a decree may be implemented by the sole discretion of the government. This constitutes a breach of the hierarchy of norms along with a breach of Article 91 of the Turkish Constitution that defines the decrees. Therefore, as the content of the Amendment Decree has also given rise to criticism, it is highly likely that a lawsuit regarding the annulment of the Amendment Decree will be filed before the Constitutional Court due to such inconsistency with the Turkish Constitution.

by İnanç Akalın, Nazlı Atalay

FINANCIAL ASSISTANCE BECOMING MORE CUMBERSOME UNDER TURKISH LAW

Frequently foreign and local lenders and investors inquire whether financial assistance is valid and enforceable under Turkish law. Another layer of complication is added, when the entity providing financial assistance is a publicly held company, *i.e.*, a Turkish company, whose shares are listed on the Istanbul Stock Exchange.

How to Respond to the Question on Financial Assistance?

The answer to this question depends on the changes that are being introduced by the new Turkish Commercial Code No. 6011 that will replace the existing commercial code upon its effective date of 1 July 2012 (the "**New Code**"). The very recent amendment introduced to the applicable capital markets legislation on 30 December 2011 further imposes on publicly held companies that are providing financial assistance the requirement to obtain proper corporate authorization in order for the security to be valid and binding.

The applicable capital markets legislation already imposes certain limitations on the circumstances under which publicly held companies may provide financial assistance. The existing commercial code governs all companies, including publicly held companies to the extent not governed by the capital markets legislation while, on the other hand, it does not stipulate financial assistance, neither does it prohibit it. The New Code, in contrast to the existing commercial code, introduces specific prohibitions directly applicable to the "financial assistance" provided by the affiliates to their parent companies by way of providing a surety, guarantee, *aval* and other types of security.

Thus, the response to this query will differ on a case-by-case basis and according to the timing of the financial assistance.

What is the Status under the Applicable Turkish Commercial Code?

Since the existing commercial code does not stipulate nor prohibit financial assistance, court precedents support that it is in the ordinary course of business life for commercial corporations to be entitled to provide security for each others' debts, particularly for the purpose of providing joint liability to the banks in order to obtain loans.

However, certain obstacles must always be taken into consideration even under the applicable commercial code.

Some of those issues are the fiduciary duties of the board of directors' members who are evaluated in relation to the benefits of the relevant company. The commercial code does not at all recognize the overall concepts of "group companies" or "group benefits." Therefore, each transaction must be considered and evaluated by the members of the board of directors of a company *per se* and be at arm's length. Any failure in the duty of care or duty of loyalty of the members of the board of directors may trigger the minority shareholders' right to sue the board for breach of its fiduciary duties. Minority shareholders may always try to cause nuisance by filing complaints with the Capital Markets Board as the capital markets regulator (the "**CMB**").

In addition to such issues, one other matter currently applicable under the existing commercial code is the relevant company's obligation to meet the *ultra vires* principle. The New Code abolishes the *ultra vires* principle. However, under the applicable commercial code, activities of a company are limited to the purpose and framework of each company as set out in its articles of association and the stand-alone agreement governing the relationship between the shareholders and the company. Transactions that are in violation of the *ultra vires* principle will automatically be considered null and void. The general principle and guiding rule in determination of the *ultra vires* principle is not only a review of the articles of association of such company, but also an evaluation of such transaction. As mentioned above, court precedents support that it is in the ordinary course of business life for commercial companies to provide security for each others' debts, particularly for the purpose of undertaking joint liability of the banks in order to obtain loans.

What is the Status under the New Code?

The New Code defines financial assistance as the abuse of dominant power of the parent company that causes loss to the affiliate.

Again, contrary to the applicable commercial code, the New Code defines the concept of the "parent company" and the "affiliate." The New Code prohibits financial assistance of a subsidiary to its parent company. A parent company cannot use its control over its affiliates to their detriment through forcing the affiliates to adopt certain resolutions, including resolutions related to financial assistance to the parent company by way of providing security.

If such financial assistance is given by the affiliate, the related losses of the affiliate must be covered/adjusted by the parent company within the same financial year, or the method of covering such losses must be determined within the same financial year. Failure of the parent company to cover/adjust the losses of the affiliate will grant any shareholder of the affiliate the right to request the parent company and the directors of the parent company to cover its losses, but will not invalidate the financial assistance given.

Furthermore, the creditors of the affiliate will also have the right to request compensation of the affiliate's damages even if the affiliate does not enter into insolvency. Compensation will not be

awarded where such conduct has been made, could be made, or could have been avoided by the board of directors' members acting in good faith and with a high level of duty of care under the same conditions.

What if the Financial Assistance was provided prior to the Enforcement Date of the New Code?

The enforcement of the provision introducing financial assistance has a specific regulation under the legislation regarding the transition period. Thus, if the company suffers any loss due to financial assistance given prior to 1 July 2012, this should be adjusted within 2 years from 1 July 2012. Upon the failure to make such adjustment, minority shareholders may seek recourse for their damages from the parent company, its members of the board of directors, or request that their shares be purchased by the parent company instead of being indemnified.

What is Different under the Capital Markets Legislation?

In 1998, the CMB allowed publicly held companies to provide pledges and mortgages or guarantees in order to secure third parties' debts, provided that necessary disclosure as required under the applicable legislation is made. However, in 2009, the CMB limited the instances whereby a publicly held company may provide pledges, mortgages or guarantees. As a result, since 2009, those companies are allowed to provide financial assistance either in the name and on behalf of their own legal entities, or for the benefit of companies that have been fully consolidated in their financial statements, or for the benefit of third parties, in order to conduct ordinary commercial activities.

On the other hand, 31 December 2014 is to be the date upon which all of the collateral that has been provided on behalf of any person who does not fall into the above-listed cases is unwound.

Is it Clear as to How to proceed in the Financial Assistance of a Publicly Held Company?

This procedure has certainly become clearer than before. Despite the fact that the CMB legislation and the decisions of the CMB have favoured financial assistance by publicly held companies, the CMB's Guide on the Principles of Corporate Governance that was issued in 2003 and amended in 2005 (the "**Guide**") has encouraged publicly held companies to resolve issues that cause changes in equity, management or assets of companies, and to provide guarantees and collateral in the meetings of the general assembly of shareholders of such companies. However, it has remained unclear whether such principle must have been complied with since the Guide itself was not itself binding, but was more advisory in nature.

The CMB adopted two new steps to have the corporate governance principles that were initially introduced under the Guide be adopted by, and be binding on, publicly held companies. The first novelty was introduced in October 2011 upon the issuance of Communiqué Serial IV, No. 54 regarding Determination and Implementation of the Corporate Governance Principles that obliged the Istanbul Stock Exchange 30 Index (*IMKB 30 Endeksi*) of publicly held companies to fulfill certain provisions of the amended corporate governance principles. Assuming that in response to the reactions of the Communiqué issued in October 2011, and which was in line with the global economic approach, the CMB, abolished this Communiqué and replaced it with one that was issued on 30 December 2011 - Communiqué Serial IV, No.56 - on Determination and Implementation of the Corporate Governance Principles (the "**New Communiqué**").

The provision regarding the financial assistance under the New Communiqué is slightly different than the version that was issued in October, 2011 and is a mandatory provision applicable to all publicly held companies trading on the Istanbul Stock Exchange (the "**ISE Companies**"). Similar to the former one,

the New Communiqué includes, on its face, a very broad provision regarding financial assistance; however, this time it focuses more on related party transactions and the collateral given to third parties rather than changes in equity, management or assets of companies.

Under the New Communiqué, the related party transactions or provision of security, pledges or mortgages in favor of third parties of an ISE Company requires a board resolution that must be approved by the affirmative votes of the majority of the independent directors. If the majority of the independent directors do not approve such a decision, this is to be disclosed to the public and the transaction will be subject to the approval of the general assembly of shareholders. While no meeting quorum is required in such general assembly of shareholders meeting, the decision will be subject to the simple majority of the shareholders entitled to vote in such meeting. ISE Companies are also obliged to amend their articles of associations in line with such new provision imposed by the CMB. Any board resolution or general assembly of shareholders resolution adopted in violation of such provision will be null and void.

Differing from the classification under the Communiqué of October, 2011, the New Communiqué classifies ISE Companies in three main categories based on the systemic risks of the average of the market value of the relevant company and the market value of the shares that are actually in trading.[1]: Under this categorization, while the companies in the first category are obliged to fulfill all the mandatory provisions of the New Communiqué, the other two category companies benefit from certain exemptions.

It appears that the New Communiqué attracts the importance of the corporate governance rules and places certain importance on the financial assistance decisions of the ISE Companies; therefore, it does not provide any exemptions to any of the ISE Companies. The wording of the relevant provision covers all types of securities for "third parties" and does not carve out affiliates. However, similar to the other regulations in place, we may observe certain distinctions in the implementation of the relevant provision in line with the necessities of daily practice.

by Yeşim Api Şamlı

CAPE TOWN CONVENTION FINALLY SEES ITS WAY TO TURKEY

Turkey has ratified the Cape Town Convention on International Interests in Mobile Equipment (the "**Convention**") and the Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment (the "**Protocol**") on 29 March 2011, with effect from 4 July 2011.

The Convention and Protocol intends to promote certainty and transparency in cross-border aviation financings by eliminating the uncertainties and problems that the creditors face under the laws of various jurisdictions, particularly with respect to the default or insolvency of the borrowers. Creditors also often find it difficult to locate aircraft when they need to enforce their rights on the aircraft as collateral, as the aircraft are flying in and out of countries on a daily basis. Needless to say, these factors create additional costs to the aircraft financing transactions, let alone being cumbersome and time consuming.

In an effort to reduce these risks, the Convention and Protocol introduce an internationally recognized collateral system to be used in international aviation financings that enables security interest to be created

1 Categorization of ISE Companies under the New Communiqué are as follows:
(i) Category I: ISE Companies with a market value exceeding TL 3,000,000,000 and a free-floating value exceeding TL 750,000,000;
(ii) Category II: ISE Companies with market value exceeding TL 1,000,000,000 and free float value exceeding TL 250,000,000, and,
(iii) Category III: All other ISE Companies that do not fall under (i) and (ii) above.

over the aircraft and related equipment, upon registration with an electronic global aeronautical registery in order to guarantee the priority of their claims against other parties. In this manner, the creditors of the aircraft and related equipment financings will have more protection against any default and insolvency risks as the existence and effectiveness of their collateral will be assured by the registry system.

Hence, while on the one side the creditors will have an effective collateral system, the airlines will, on the other side, have the benefit of low financing costs that is proving to be the case for a number of member countries which have ratified the Convention and the Protocol thus far. This is especially important for developing economies such as Turkey that pay relatively higher interest rates on their financings. Despite its obvious advantages, the ratification of the Convention and the Protocol may not have an instant impact in the Turkish aviation market as the Convention and Protocol do not apply retro-respectively. In other words, the existing financing agreements would have to be amended in order to benefit from the registry system. Coupled with the financial turmoil in the global loan markets, it may take a while to see aviation financings gaining momentum in Turkey.

by Umut Gürgey

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