

Significant Amendments to Turkish Securities Law

March 2020



Law for Amendments to the Banking Law and Other Laws that is published in the Official Gazette on 25 February 2020 introduced various amendments to the Turkish Capital Markets Law (“**Amendment Law**”) with an aim to increase the indepthness and competitiveness of the capital markets while changing investor-centered approach in order to reflect certain experiences as an outcome of practices and to meet needs of the real sector.

We have put together this brief note to inform the reader only on key changes made to the Turkish Capital Markets Law through this omnibus bill, covering also new and diverse topics under Turkish securities law such as bondholders meeting, security trustee and project-backed securities. This note does not include changes about increased penalties in response to, among others, market manipulation, expanded sanctions pertaining to use of proceeds and false, misleading and omitted information in offering materials.

It should be noted that the Amendment Law has introduced concepts and drawn the general framework, leaving to the Capital Markets Board of Turkey (“**CMB**”) with authority to issue implementing regulations in the form of new communiques or amendments to existing communiques.

Financing Major Projects through Capital Markets

Financing of Turkish major infrastructure projects through capital markets rather than bank financing was in the agenda for a long time. The Amendment now brings in a general legal framework and takes an initiative with the introduction of project finance funds that aim at financing of major long-term projects such as infrastructure, energy, industrial and technology projects using a non-recourse financing structure. Accordingly, a project finance fund in the form of a special purpose vehicle is sought to be established, unlike other funds in Turkey, by a Turkish investment institution and it will issue bonds to domestic and international investors, where the proceeds will be invested in the project finance assets. The investors in return will receive cash flow and revenues that are generated by these assets. In other words, the project finance fund will issue project backed

securities to finance major projects, and the proceeds used to finance the projects will be paid back from the cash flow and rights generated by the project finance assets in the portfolio which is operated by the investment firm as fiduciary for the benefit of investors. The structure of debt securities, in essence, relies primarily on the project's cash flow for repayment, with the project's assets, rights, and interests held as secondary collateral. The founder of the fund (i.e. investment institution) or the fund, where applicable, holds the project assets as fiduciary in its own name but to the benefit of investors.

Same as other types of funds regulated by the CMB, the assets of the project finance funds will be protected and ring-fenced until the project backed securities are redeemed. On this basis, the rights and assets of the fund cannot be seized and pledged, and cannot be subject to other encumbrances, preliminary injunctions and precautionary attachments or form part of bankruptcy estate, even if the management or supervision of the founder and the fund users are transferred to public authorities.

Security Trust Deed and Security Trustee¹

Although there has not been a specific provision regarding the concept of a security trustee or security agent under Turkish law due to Turkey being a civil law jurisdiction, the concept has been recognised by the Turkish legal doctrine, and it has been widely used in English or US law governed financings received by Turkish borrowers. It is also worth to mention that Turkish court precedents exist that recognise fiduciary transactions (*inançlı işlemler*), where the fiduciary, for instance, is under an obligation to transfer immovable back to the beneficiary after holding such immovable as security, although the land registry records show the beneficiary as the legal owner of the immovable². This has also been the case in few Turkish court precedents as analogy in transactions involving indirect representative (*dolaylı temsilci*), where the indirect representative acts in its own name, but on behalf of and for the benefit of a third party.

Furthermore, secondary legislation in the capital markets space has also provided fund structures that regulate holding assets to the benefit of investors. The concept of trust, in its strongest term, however, has never been introduced through a substantive law. Therefore, this is the first time, and is a notable point, that we see both the security trustee and security trust deed concepts are recognised in the Amendment Law as a matter of Turkish law in line with its meaning under common law.

The Amendment Law provides that the debt securities which will be determined by the CMB can be secured through the collaterals that will be again determined by the CMB in order to collateralise secured obligations under such debt securities. On this basis, the title of the assets, as a matter of Turkish law, can now be transferred as security to the security trustee or *rights in rem* can be established on such assets in favour of the security trustee, both in respect of the secured obligations owed by the issuers to the investors. In case of transfer of the title of assets, such transfer will have to be annotated to the relevant registry applicable to the security.

According to the Amendment Law, the investment institutions which have the license of general custody can be appointed as a security trustee, and they are authorized on the protection and operation of all procedures in relation to such security. In case of default or other reasons set forth under the law or terms and conditions of the debt securities, the security trustee will be able to sell the securitized assets and distribute such funds to the investors, and pay back access amount to the security provider, or return the securitised assets to the security provider once the debt is repaid.

¹ This can also be called as Security Agent.

² Unlike trustee, the term fiduciary exists essentially under Turkish secondary legislation and has been used to describe arrangements where title to an asset is transferred to a person to allow them to manage the asset in the interest of others.

The security trustee will have to be authorised by the issuer through a security trust deed and approved by the CMB before the issuance in order to protect rights of the investors as well as fulfilling all procedures and transactions attained to a security trustee in relation to registration or removal of all mortgage or other *rights in rem* in any registry office in its own name but to the benefit of investors. Security trustee that is approved by the CMB will be registered by the issuer at the trade registry where the issuer is resident and disclosed in the trade registry along with information about its authorities and powers. Minimum requirements and conditions that need to exist in security trust deed will have to be regulated by the CMB, but in any case, any agreement or conditions that remove or decrease the liability of the security trustee will be invalid, although we believe that the security trust deed should also provide an indemnity of the security trustee for its actions (typically subject to the security trustee's gross negligence or wilful misconduct, and should be clear that all costs of enforcement are covered by the investors).

In case of incompliance with the liabilities mentioned above, the CMB is authorised to request compliance with the responsibilities within a certain period, or to restrict the scope of the activities of the security trustee or to suspend its activities temporarily or to take all kinds of other measures it may deem appropriate.

The security trustee is entitled to sell the secured assets and distribute them among the investors in case of default or in compliance with the reasons set forth under the law or terms and conditions without any need for notification or consent, or approval from administrative or judicial authorities, or obligation to comply with a pre-condition to sell through a formal process.

Secured assets will be protected for the benefit of investors as a matter of law, as they will be monitored separately from the assets of the security trustee. Therefore, they cannot be - even for public debt - seized, pledged and subject to preliminary injunctions and precautionary attachments or form part of bankruptcy estate.

The CMB has explicit power to take measures in case of incompliance with this rule, as Article 92 of the Turkish Capital Markets Law vests duties and authorities to the CMB in order to take necessary actions, including but not limited to, applying to the court for the invalidity of such transactions which are against the laws and take actions for managers who are involved in illegal transactions. CMB's effective use of this authority will be an important means of confidence for investors who will invest in these debt securities. The Amendment Law also refers to the rules of office misconduct (*görevi kötüye kullanma*) under Turkish Criminal Code and increases the sanction to five years of imprisonment under Turkish Criminal Code for use of secured assets out of its objective.

Bondholders Meeting

In parallel with the concept of bondholders' assembly which had been regulated under the repealed Turkish Commercial Code No. 6762, the Amendment Law recognizes the concept again under the term board of debt securities holders³, along with details for the purpose of active representation of the investors and protection of their rights.

The Amendment Law provides that the holders of all the outstanding bonds constitute a bondholders meeting under Turkish law. Investors holding a tranche of bonds can also convene a separate bondholders meeting. The Amendment Law presents that the bondholders act collectively in changing circumstances during the life of the bond, allowing bondholders and issuers to amend terms and conditions of the bonds without hurdles and to agree on bond restructuring before or after a payment default.

³ In order to use a universal and common definition, we will refer to the term "bondholders meeting", "bondholders" and "bond" respectively instead of "board of debt securities holders", "debt instrument holders" and "debt instrument". Bonds in this context will cover all debt securities defined under the debt securities regulation of the CMB, including convertibles and exchangeables.

The Amendment further envisages appointment of a joint representative to represent all bondholders which we assume will be similar to a trustee and, unlike a fiscal agent, such representative should, to some extent, be able to enforce the terms of the bonds or negotiate with the issuer regarding any necessary amendments to the terms of the bonds, especially in times of financial distress.

As typical in restructurings, in case of a bond restructuring through amendment to the terms and conditions of the bonds after a payment default, all proceedings initiated due to default of the bonds will be suspended as of the date on which terms and conditions of the bonds are considered to be amended, and also preliminary injunctions and precautionary attachments cannot be enforced. As such, any statute of limitation that may be ceased due to an execution proceeding will be suspended.

The terms and conditions in relation to resolutions and invitation to the bondholders meeting by the bondholders or board of the issuer are required to be set forth and disclosed in the prospectus and/or issuance certificate. The Amendment Law, however, stipulates a minimum voting threshold, requiring simple majority (i.e. 50%) of all outstanding bonds to resolve in a bondholders meeting unless qualified majority is required by the CMB or under the prospectus and/or issuance certificate. Same is also applicable if there is a separate bondholders meeting for investors holding certain tranche of bonds. Although the Amendment Law is silent on whether resolution with simple majority will bind rest of the bondholders, it states that the dissenting bondholders are bound by a resolution of the qualified majority to be set forth by the CMB.

Finally, the Amendment Law authorises the CMB to determine principles and conditions for the implementation of rules for bondholders meeting, which are expected to be issued by the CMB in the form of an amendment to the debt securities communique in the coming months.

Exit Rights (Appraisal Rights)

Significant transactions in a public company trigger exit rights for the existing shareholders which oblige the public company to purchase shares of dissenting shareholders voting against such transactions in the shareholders meeting. While significant transactions were listed non-exhaustively in the Turkish Capital Markets Law, the Amendment Law introduces a new criteria making a reference to “transactions relating to corporate structure of the issuer that result in a change in the investment decision of the investors”. Therefore, the scope of significant transactions is now extended.

Another notable change brought in by the Amendment Law is the worldwide use of “fair price” concept, removing the existing “30-day weighted average of stock price”, principles of which will be regulated by secondary legislation of the CMB. A public company will be under the obligation to pay a fair price for the shares of dissenting shareholders. The Amendment Law further authorises the CMB to set rules for offering of such shares to the other shareholders or the investors before they are purchased by the public company.

Finally, exemption to the obligations of the public company due to triggering of exit rights can now be granted by the CMB through an application process and principles to such exemptions will be regulated by a secondary legislation. It is expected that the significant transactions such as, mergers for the purpose of rescuing the financially distressed entities or remedying capital loss of companies, may be among such exemption grounds.

Mandatory Tender Offer

Shareholders will now benefit from the tender offer only if they already owned shares at the time of the public disclosure made regarding the acquisition of control. Therefore, in contrast to previous rules, the Amendment Law does not allow shareholders to tender their shares who acquire them after the first public disclosure

has been made in relation to the acquisition transaction, and this new rule is introduced in order to avoid manipulation possibilities and costs associated for the new buyer.

Crowdfunding

Crowdfunding refers to raising funds for a specific project through crowdfunding platforms established to enable the interaction between fundraisers and potential investors. It is an alternative financing method and a unique route compared to traditional method of business funding where the “crowd” or investors - not the traditional institutions - finance the projects and ventures of fundraisers such as individuals, small and medium enterprises as well as the start-ups who usually face challenges in raising capital and accessing to other conventional financing methods.

Crowdfunding was first introduced with the amendments made to the Turkish Capital Markets Law in 2017, and following that a communique was published by the CMB for more detailed regulation of share-based crowdfunding in October 2019. With the Amendment Law, “debt-based” crowdfunding is now also recognized under Turkish Capital Markets Law, and it is explicitly mentioned not to be within the scope of banking legislation. The CMB is provided with the authority to regulate debt-based crowdfunding, which is expected to be regulated with secondary legislation. All parties signing the information form for the crowdfunding activities will be held jointly and severally liable according to the Amendment Law.

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