CHAMBERS

Global Practice Guides

Securitisation

Turkey – Law and Practice

Contributed by

Paksoy

2018

CHAMBERS® AND PARTNERS

TURKEY

The 'Law & Practice' sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.

Law and Practice

Contributed by Paksoy

CONTENTS

Contributed by Paksoy ***Authors:*** Ömer Çollak, Şansal Erbacıoğlu

Paksoy is an independent full-service law firm in Istanbul, Turkey, focused on helping clients in a wide range of legal areas, including cross-border investments, international business transactions, acquisitions, finance transactions, investigations, compliance and disputes. Established in 1997, Paksoy stands today as one of the strongest independent legal brands in Turkey, focusing on numerous practice groups and sectors. Paksoy has lawyers and specialists from a background of varied sectors and industries, including international accounting and consultancy firms, industry regulators and private practice. The authors would like to thank one of the associates in the capital markets practice group of the firm Ms Merve Kurdak Kurtdarcan for her contribution to this article.

Authors

Ömer Çollak is a partner and head of capital markets. Mr Çollak is one of the few lawyers in Turkey active in securitisation projects. He acts for arrangers in future flow financing (eg, DPRs) of Turkish banks, provides true-sale opinions to Turkish originators and purchasers in sale transactions, such as factorings; gives opinions in multi-jurisdictional trade receivables securitisation transactions, and acts for purchasers and banks in onshore or offshore securitisation of auto loan receivables originated from Turkish financial institutions. Additional expertise includes banking and finance and project finance. He has published a number of articles in industry publications.

Şansal Erbacıoğlu is counsel, head of tax and fiscal services. Mr Erbacıoğlu is very much involved in banking and structured finance transactions. He paves the way for securitisation transactions involving Turkish financial institutions by providing constructive fiscal and tax advice to the clients in their conventional, innovative or first-of-its-kind products such as issuance of exchangeable bonds, offshore ABS issuance, and exchange offers to existing noteholders.

1. Structurally Embedded Laws of General Application

1.1 Insolvency Laws

Securitisation methods constitute one of the favourable ways to create a financial instrument raising funds for financial entities as an off-balance sheet alternative to liquidate their receivables. Securitisation transactions involve either an offshore or an onshore special-purpose entity ("SPE"). Although there is not a specific regulation and an approval requirement for the transactions where an offshore SPE is used, the domestic transactions (where an onshore SPE is utilised) are governed by the regulations issued by the Capital Markets Board of Turkey ("CMB"). In both scenarios, the assets subject to the securitisation cannot be subject to insolvency proceedings of the originator, provided that the legal ownership of assets passes to the SPE with the "transfers of receivables" as regulated under the Turkish Code of Obligations Law.

Receivables under Turkish law are generally transferred by way of a written assignment so that it constitutes a true sale. If the underlying contract contains a prohibition on assignment then the debtor's consent must be obtained. Generally, receivables are freely transferable as a matter of law (outside of certain healthcare/social security-related receivables), but it would be necessary to check the underlying contract to ensure that no public policy considerations were implicated. Ancillary rights, such as security, pass automatically with an assignment under Turkish law, with the exception of certain security, such as security over real property, where the assignor's name would need to be registered at the land registry office.

Under a true sale, receivables are legally isolated from the assets of an originator, provided that the parties intend the assignment to be a sale and act on an arm's-length basis. The transaction may only be set aside following the insolvency of the originator in certain limited cases, for example if there is a transfer at an undervalue, security is granted for an existing debt or if there is an intention to damage the rights of creditors. The purchase of the receivables at a discount; the application of an advance rate; the payment of a portion of the purchase price by way of deferred purchase price; and the maintenance of reserves funded via the receivables can be done without this being problematic for a true-sale analysis, provided there is some consideration and the parties act in good faith in relation to the sale and on commercial terms.

It is standard practice to give notice of an assignment to underlying debtors, in order to prevent the debtors from being able to discharge their obligations by payment to the originator. This is generally done on or before the closing date of a transaction.

As mentioned above, a true sale is a sale of receivables by the originator, as the owner of the receivables which are then transferred to SPE; however, if the parties' intention is sale of the receivables with recourse to the originator, then this transaction is very likely to constitute a secured loan.

In a secured loan, the sale of receivables transaction is executed between the parties in order to secure a loan with the intention to recourse to the originator. Under this transaction, it is important to know whether the parties really intend to transfer the receivables to the SPE or not. If the parties are not really intending to transfer the receivables to the SPE, the transfer of receivables transaction will be invalid accordingly.

As per the Turkish Execution and Bankruptcy Law, if there is an invalid transfer, the receivables will remain in the assets of the originator which will be subject to insolvency.

There is no legal requirement to obtain an opinion of counsel to support the bankruptcy remoteness of a transfer. However, it can be obtained depending on the practice for the purposes of minimising challenging or re-qualification risks of a true sale.

1.2 Special-Purpose Entity

Either offshore or onshore SPEs may be used in securitisation transactions in Turkey.

Onshore Securitisations

While the securitisations where an offshore SPE is used are not subject to the CMB approval or a registration requirement, domestic securitisations are mainly governed by the Communiqué on Asset-Backed and Mortgage-Backed Securities (Serial: III, No: 58.1) ("Communiqué"). The Communiqué requires the asset-backed or mortgage-backed securities ("AMBS") to be issued by a CMB-licensed SPE. Such an SPE can either be established as a fund or a mortgage finance institution ("MFI") regulated under the Communiqué on Principles of Mortgage Finance Institutions (Serial: III, No: 60.1).

MFIs are the CMB-licensed joint-stock companies which are allowed to take over assets permitted by the CMB legislation, manage such assets or transfer them within the scope of housing and asset financing. Under the Communiqué, the MFIs are entitled to issue either asset-backed or mortgage-backed securities.

The Communiqué provides for two types of funds: in the case of the issuance of asset-backed securities, asset finance funds, and in the case of issuance of mortgage-backed securities, housing finance funds. Both can be established by financial leasing companies, financing companies, banks, MFIs and broadly authorised intermediary institutions. The funds established by financial leasing or financing companies are entitled to issue AMBS collateralised only by a pool of assets of their founders.

Certain important principles regarding the formation and management of these funds are stated under the Communiqué. They are defined as a separate asset pool formed by the proceeds of the AMBS sold. They do not have a legal personality and must be managed according to fiduciary ownership principles. Therefore, there is no legally recognised shareholding right in a fund, but there is an ownership right over the issued asset-backed securities.

Funds operate under the rules stated in the internal by-laws of a fund, which include:

- general terms about management of the fund;
- custody of the assets;
- valuation principles; and
- conditions of investing in the fund.

The fund must have a board with at least three members, internal controllers, and must enter into agreements with a service-provider and custodian entity for the fund's assets.

Asset-backed securities can be sold through a public offering or private placement or to the qualified investors in Turkey once the CMB approval is granted, but the unit nominal value needs to be a minimum TRY100,000 for sales through private placement. While it is mandatory to prepare disclosure documents (such as an offering circular prospectus) for public offerings, it is also mandatory to prepare an issue document for private placements or for sales to qualified investors.

Security-holders are the beneficial owners of an asset portfolio managed by a service-provider. Since there is no trust concept under Turkish law, the relationship between the fund and its investors can be defined as a sort of agency relationship (fiduciary ownership).

There is no risk of some form of consolidation in any insolvency proceeding of an originator or parent or an affiliate that endangers the bankruptcy remoteness of an SPE. Legal ownership of assets pass to the fund and those assets cannot be subject to insolvency proceedings of the originator or parent or an affiliate.

A guarantee can be used as a tool to ensure payment of obligations which cannot be paid by the fund itself. However, if the originator cannot fulfil its obligation for the guaranteed part of the payments, the investors can attend the liquidation process of the originator for this part pari passu along with the other creditors of the guarantor.

A CMB-governed issuance in Turkey requires the incorporation of an onshore fund, which is subject to strict restrictions as a matter of law. For tax reasons, most recent securitisations have been done through offshore SPEs incorporated in the Cayman Islands or similar jurisdictions, and are not subject to Turkish legislation, except for transfer of receivables to the offshore SPE within the scope of relevant mandatory provisions of Turkish law.

It should be also noted that, from the limited number of securitisations that have taken place in Turkey, securities are usually issued privately to qualified investors.

Offshore Securitisations
Turkish capital markets legislation does not regulate the securitisations where an offshore SPE is used. This type of securitisation is not subject to the CMB approval or another registration requirement.

Assignment of receivables by a Turkish entity, an originator, to an offshore SPE is valid under Turkish law, thus, there is no risk that a transfer of title to the receivables (ie, a true sale) will be re-characterised as a secured loan as long as the parties' intention is the sale of the receivables without recourse to the seller in an offshore securitisation.

For more, see **1.1 Insolvency Laws**.

1.3 Transfer of Financial Assets

The types of financial assets which can be transferred by originators to funds for AMBS issuance are restricted. In other words, there are restrictions on the quality and qualifications of assets that can be included in the fund's portfolio. For ordinary asset-backed securities, in line with the provisions of the Communiqué, the portfolio of the fund can consist only of the following:

- receivables of banks and financing corporations arising from consumer loans and commercial loans;
- receivables arising from financial leasing agreements entered into pursuant to the Law on Financial Leasing, Factoring and Financing Companies;
- receivables arising from the sale of real estate property by the Housing Development Administration of Turkey, based on instalments and contracts;
- commercial receivables attached to deeds or collateral, arising from invoiced sales by joint-stock companies engaged in the production of goods and provision of services to their customers, excluding financial institutions;
- short-term deposits with a maturity of less than three months, participation accounts, reverse repo transactions, money market funds, funds for short-term debt securities and Settlement and Custody (Takasbank) Bank Money Market transactions, destined to invest the cash originating from the assets available in the fund portfolio;
- assets in the reserve accounts; and
- assets, other than the capital market instruments, as may be approved by the CMB.

The above-listed financial assets need to be transferred by originators to SPEs through a written assignment agreement. Pursuant to the Communiqué, all ownership rights will be transferred to SPEs.

For more, see **1.1 Insolvency Laws**.

1.4 Construction of Bankruptcy Remote Transactions

For more, see **1.1 Insolvency Laws**.

2. Tax Law and Issues

2.1 Taxes and Tax Avoidance

For local income tax purposes, offshore securitisation structures are treated as lending arrangements and the SPEs are defined as financing institutions. Therefore the following tax treatment applies:

- 1% withholding tax applies under a special regime, based on interest payments made to the investors;
- VAT is not applicable for the transfer of assets (ie, receivables); however, servicing-related charges are subject to VAT at a general rate of 18%. The servicing agreement is subject to stamp tax at a general rate of 0.948% (almost 1%) over the highest monetary amount (ie, the gross amount of servicing fee) referred to in such a document;
- stamp tax is exempt on documents executed for the transfer of the assets (ie, loans) of banks and financing companies in Turkey; and
- The application of the Resource Utilisations Support Fund Levy depends on the denomination currency and the maturity. The highest rate is 3% and the monetary base is interest on Turkish lira or the principal amount for foreign currency-denominated financing. Turkish intermediary banks act as tax agents and usually it is a borrower's liability. Financial institutions enjoy exemptions for the Resource Utilisations Support Fund Levy in securitisations. The Resource Utilisations Support Fund Levy being calculated over the assets (ie, loans) will continue to be payable, if any.

Onshore securitisations are generally made through funds which are technically considered taxable fiscal units (ie, taxable funds) in Turkey. However, this particular income item of the concerned funds is exempt from corporate income taxation at the level of such a fund in Turkey.

Onshore securitisations are generally subject to tax (ie, transactional taxes such as Banking and Insurance Transactions Tax and stamp tax). However, exemptions apply for some types of securitisations such as sukuk issuances under sale and lease-back models and mortgage-backed securities. Further, as in the case of offshore securitisations, stamp tax is exempt on documents executed for the transfer of the assets (ie, loans) of banks and financing companies in Turkey.

As in the case of offshore securitisations, servicing between the originator and the fund is taxable based on arm's-length fees, and the execution of agreement regulating the servicing is subject to stamp tax as per general taxation principles.

2.2 Taxes on the SPEs
See **2.1 Taxes and Tax Avoidance**.

2.3 Taxes on Transfers Crossing Borders
See **2.1 Taxes and Tax Avoidance**.

2.4 Other Taxes
See **2.1 Taxes and Tax Avoidance**.

2.5 Obtaining Legal Opinion
There is no legal requirement to obtain a legal opinion for bankruptcy-remote transaction; however, it can be obtained, depending on the practice and parties' preference.

3. Accounting Rules and Issues

3.1 Legal Issues with Securitisation Accounting Rules
Asset-finance funds and housing finance funds are subject to the requirements set forth under the Communiqué on Principles regarding Financial Reporting of Investment Funds (Serial: II, No: 14.2). Pursuant to that Communiqué, they must prepare their financial reports in line with the Turkish accounting standards on an annual basis and announce within 60 days following the end of the accounting period. The annual financial reports are subject to the independent financial audit.

The Turkish Accounting Standards Board published its financial reporting standards in 2005 and they could be considered to be identical to the International Financial Reporting Standards (IFRS). The same as asset-financing funds, Turkish companies listed on Borsa Istanbul must prepare their financials according to these standards. Turkish Commercial Law, which entered into force on 1 July 2012, has also taken a similar approach.

3.2 Dealing with Legal Issues
Legal practitioners can provide legal consultancy for compliance of the reports with the rules and standards specified under the relevant laws.

Under Turkish law, there is no legal requirement to obtain a legal opinion regarding accounting issues; however, it can be obtained depending on the necessity.

4. Laws & Regulations Specifically Relating to Securitisation

4.1 Specific Disclosure Laws or Regulations
Principles on providing information and public disclosure relating to domestic securitisation are specifically regulated under the Communiqué.

Under the Communiqué, investors are informed through the public disclosure platform ("PDP") and a founder's website within six business days of the following:

- the receipt of the CMB approval by the founder, any amendment to the fund statutes should be announced;
- the occurrence of events, which include resignation of the fund board members, fund operations manager, auditor, servicer or independent audit company from their duties, or non-fulfilment of the conditions required under the Communiqué, or cancellation of the operation licence of the servicer; these events should be announced;
- the end of the relevant period, an investors, report, quarterly based on a calendar year, covering the amount of principal payments made; the cumulative principal amount paid and remaining principal balance and if there is no principal, the amount of payments made in relation to the assets, since the date of the previous report, if any, these should also be announced;
- the preparation of the report, the facts presented in the report prepared duly in relation to the activities of the servicer and the fund assets should be announced; and
- the notification to the founder or the fund board, the credit ratings that are given or updated by rating agencies for asset-backed securities/mortgage-backed securities should be announced.

If the AMBS are sold through private placement or to qualified investors, the required announcements shall be announced to such investors by electronic means through the Central Registry Agency, and made available for investors by publishing the same on the website of the founder. This shall then be notified to the CMB within six business days

following the announcement, along with the necessary access details, if any.

A founder is responsible for ensuring that the information and documents to be announced are complete, accurate and up to date.

Information regarding the date and number of the Turkish Trade Registry Gazette in which the fund statutes and amendments to the fund statutes were published should be sent to the CMB within six business days following the publication.

The report issued by the fund auditor should be sent to the CMB within six business days following its completion.

4.2 General Disclosure Laws or Regulations

Material Events disclosure Communiqué (Serial: II, No: 15.1) ("**Material Events Communiqué**") regulates the general disclosure requirements of public companies and all other non-listed issuers which offer the securities other than the shares to the public in Turkey. Therefore, funds which issue and then sell AMBS through public offering in Turkey are subject to those mandatory requirements.

As per the Material Events Communiqué, any information, events and developments which may affect the value or price of capital market instruments or the investment decisions of investors relating to capital market instruments should be disclosed on the PDP.

Apart from the general disclosure requirements, funds must announce the offering documents (ie, prospectus and issue certificate) within fifteen business days following the receipt of the CMB approval under the Communiqué on Prospectus and Issue Certificate (Serial: II, No: 5.1).

Pursuant to relevant CMB legislation and communiqués: persons who have violated disclosure regulations should have an administrative fine of TRY20,000, and up to TRY250,000, imposed upon them by the CMB. However, in cases where a benefit has been gained due to the violation of the obligation, the amount of the administrative fine to be imposed cannot be less than twice this benefit.

In the event that an offshore SPE is used for the securitisation, such securitisation will not be subject to the Turkish disclosure requirements. However, if the Turkish originator is a listed company, it needs to disclose the sale of its receivables to a foreign SPE for that securitisation, in line with the requirements stated under the Material Events Communiqué.

There is no legal requirement to obtain a legal opinion on compliance with these rules; however, it can be obtained, depending on the practice.

4.3 "Credit Risk Retention"

Risk retention is regulated under the Communiqué. As per the Communiqué, an originator or founder is required to repurchase asset/mortgage-backed securities corresponding to 5% of the nominal value of the asset/mortgage-backed securities issued and retain this value until the end of maturity. If the asset/mortgage-backed securities are issued in classes, this requirement shall be applicable:

- when the asset/mortgage-backed securities classes do not have a credit rating, or have the same credit rating, on a pari passu or pro rata basis from each class; or
- from the class or classes having the lowest credit rating, if there are different asset/mortgage-backed securities classes with different credit ratings.

The CMB is authorised to vary the aforementioned ratio depending on the type of assets or to increase on the basis of originators or founders provided that the ratio does not exceed 10%.

Risk-retention liability may be shared between the originator and the founder.

It should be noted that there is no rule allowing for "substitutive compliance" by foreign issuers under the CMB legislation and communiqués and, as far as can be known, there is no such prevailing rule in practice.

Under Turkish law, there is no legal requirement to obtain a legal opinion as to such rules; however, it can be obtained, depending on the practice.

4.4 Periodic Reporting

In addition to the annual report announcement requirement, an investor report, quarterly based on a calendar year, covering the amount of principal payments made, the cumulative principal amount paid and remaining principal balance and if there is no principal, the amount of payments made in relation to the assets, should be announced within six business days following the end of each relevant period.

For more, see **3.1 Legal Issues with Securitisation Accounting Rules**.

4.5 Activities of Rating Agencies (RA)

The Capital Markets Law ("CML") and the Communiqué regulate rating agency (RA) securitisation activities. In accordance with the Communiqué, RA shall mean the rating agencies that are established in Turkey and authorised by the CMB in order to conduct rating activities within the frame-

work of the CMB's regulations on rating activities and rating agencies in capital markets, as well as international rating agencies which have been approved by the CMB to conduct rating activities in Turkey.

RAs are required to provide credit ratings for each tenor of asset/mortgage-backed securities and, if any, for asset/mortgage-backed securities tranches that will be offered to the public. The credit ratings should be reviewed on a regular basis in the event that any updates are required according to the CMB regulations on rating activities in capital markets and RA.

RAs are regulated under CMB laws and the CMB is the principal regulator for RA activities accordingly. Under the CMB legislation, it is generally regulated that an RA shall be liable for damages they have caused due to false, misleading and incomplete information included in reports they have prepared as a result of their activities.

RAs included in the prospectus of public disclosure documents shall also be responsible in the framework of the provisions of CMB laws due to any inaccurate, misleading and incomplete information included in the reports they have prepared.

Based on offshore securitisation issuances so far, credit rating agencies focus on the true sale, bankruptcy-remoteness, recourse or non-recourse characteristic, set-off and status of underlying securities when assessing the rating of the transactions.

4.6 Treatment of Securitisation in Financial Entities

Financial leasing companies, financing companies and banks are the main financial entities which play an important role as funder of funds or originators in an asset/mortgage-backed securitisation transaction.

Pursuant to the Communiqué, all accounts and transactions of funds, founders, originators, fund operations managers and servicers relating to the fund are subject to supervision of the CMB. In addition to this, such financial entities are also regulated by certain specific laws or regulations and subject to equity ratio restrictions or other criteria stated therein.

Financial leasing companies and financing companies are regulated by Financial Leasing Companies, Factoring Companies and Financing Companies Law No 6361. They are subject to supervision of the Banking Regulation and Supervision Agency ("BRSA") (the regulatory and supervisory authority in the banking sector). The BRSA is entitled to take all kinds of measures to detect, analyse, monitor and evaluate the risks exposed and to specify limitations and standard ratios for their activities and equity.

The BRSA has also been regulating capital adequacy rules and principles for banks in accordance with Basel III regulations and monitors their implementation, which have been in effect as of 2013.

BRSA have issued the Regulation on Liquidity Coverage Ratios in 2014 in order to ensure that a bank maintains an adequate level of unencumbered high-quality liquid assets that can be converted into cash to meet its liquidity needs for a 30-calendar-day period. In August 2017, the BRSA amended this Regulation increasing the inclusion ratio of the mandatory reserves held at the Central Bank to 100% from 50% in calculation of liquidity coverage ratios. The BRSA is currently implementing transitional liquidity coverage ratios for deposit banks under Basel III. Development and investment banks will follow a 0% legal liquidity coverage ratio requirement for 2017, though the BRSA may increase the ratio from 2018 onward.

In addition to BRSA's regulations regarding capital and liquidity there are also other regulations on these issues under various laws as follows:

- Turkish Commercial Law provides capital thresholds that companies must sustain to avoid technical bankruptcy, although under Turkish Commercial Law a company has a period of time to remedy any capital inadequacy; and
- There is no authority which regulates and supervises capital adequacy of companies in Turkey. However, the CMB issues capital adequacy regulations for capital market entities such as brokerage houses and asset management companies, and is responsible for the implementation of these rules.

According to the Turkish Banking Law, persons who have violated the regulations will have an administrative fine imposed upon them, which varies according to each case.

4.7 Use of Derivatives

There are specific regulations regarding the use of derivatives in securitisations under the Communiqué. As per the Communiqué, rights and obligations arising from derivative instruments that will hedge interest or currency, or at risk of housing finance fund portfolios may also be included to the fund portfolio to ensure that the liabilities arising from mortgage-backed securities are performed. These derivative instruments are required to meet the following conditions:

- the derivative instruments have to be traded on stock exchanges or the counterparty to the derivative instrument has to be a bank, financial institution, insurance company or central clearing institution authorised by the relevant

authorities of the country where it was incorporated, and it must have a long-term credit rating which corresponds to the top three degrees of the investment grade, as determined by credit rating institutions; and
- the rights originating from derivative instruments may not exceed the nominal value of the outstanding total principal amount of all assets that are exposed to the risk; and the liabilities may not exceed the nominal value of the outstanding total principal amount of the issued mortgage-backed securities that are exposed to the risk.

Additionally, the internal control system of the housing finance fund (which will be party to derivative instrument transactions) is required, in addition to general requirements specified for each internal control system of the funds, also to include: risk-management procedures for the development of a risk-measurement mechanism that will enable defining the basic risks that the fund may encounter; reviewing the risks on a regular basis and updating the risk definitions in compliance with significant developments; and evaluating the exposed risks in a consistent manner. Risk-management procedures shall be set up and followed up by a separate unit personnel holding Capital Market Activities Advanced Level and Derivative Instruments Licences under the organisation of the internal control system or the fund auditor holding the Derivative Instruments Licence.

The CMB enforces these rules. Pursuant to CMB laws, persons who have violated the regulations will have an administrative fine of TRY20,000 up to TRY250,000 imposed upon them by the CMB.

4.8 Investor Protection
According to the Communiqué, there are credit-enhancement mechanisms which may be carried out to protect the rights of investors and prevent the risk of cash-flows obtained from the assets not being sufficient to meet the payments to be made to investors, and to make other expenses by using the fund assets as follows:

- the fund can enter into an insurance, guarantee, letter of guarantee or other similar types of security arrangements with the originator or another third party;
- the fund can diversify the securities with different rights and classes;
- the fund assets in excess of its liabilities can be transferred to reserve accounts (known as creating retained spread); and
- any other mechanism approved by the CMB.

As mentioned above, these transactions may be carried out to protect the rights of investors and prevent the risk of cash -flows obtained from the assets not being sufficient to meet the payments to be made to investors; however, they are not mandatory. There is no penalty for not carrying out these transactions accordingly.

It should also be noted that, due to restrictions on the quality and quantity of fund assets, the operations of the fund and the expenditures to be made, it is unlikely that a fund would become insolvent.

4.9 Banks Securitising Financial Assets
For more, see **1.3 Transfer of Financial Assets**.

4.10 SPEs or Other Entities
Material factors used in choosing entities are tax treatments and bankruptcy remoteness.

For more, see **1.2 Special-Purpose Entity**.

4.11 Activities Avoided by SPEs or Other Securitisation Entities
Funds, as the onshore SPEs of securitisations carried out in Turkey, can be established solely to issue AMBS. Therefore, they cannot conduct any other activity. These funds are mainly responsible for issuance of AMBS, establishment of fund portfolio, its management and increasing its value.

In addition to the activity restriction, the Communiqué restricts the types of the expenditures of funds. All the fund expenditures must be made on an arm's-length basis. The list of allowed expenditures under the Communiqué is as follows:

- Compulsory registration and announcement fees.
- Fees to be paid to the fund employees and to the providers of legal, accounting, custody, settlement and other management services.
- Servicing fees to be paid to the service-provider.
- Fees paid to audit firms.
- Fees paid to rating agencies.
- Fees, commissions and other payments paid to credit-enhancement providers.
- Underwriting and brokerage fees and commissions.
- Accruals to reserve accounts.
- Legal fees for the issuance.
- Tax charges of the fund.
- Expenses associated with cash management loans.
- Other expenses that are approved by the CMB.

4.12 Material Forms of Credit Enhancement
Material forms of credit enhancement provided by originators are secured loans, over-collateralisation, reserve accounts, purchase of subordinated notes while bank guarantees, insurance coverage and swap are some other forms of credit enhancement provided by third parties.

See **4.9 Investor Protection**.

4.13 Participation of Government-Sponsored Entities

No government-sponsored entities participate in the Turkish securitisation market.

4.14 Entities Investing in Securitisation

Generally, there is no limitation for the types of entities that can invest in Turkish securitisations; the specific legislation to which investors are subject shall be applied accordingly.

5. Documentation

5.1 Bankruptcy Remote Transfers

Documentation customarily used to affect bankruptcy remote transfers are: i) transaction documentation (ie, assignment agreement for transfer of receivables, pooling and servicing agreements, trust indentures, credit enhancement, and underlying documents in the transactions); and ii) organisational documentation (ie corporate charter, partnership agreement, trust documents etc); iii) offering documentation (ie, board of directors' resolution of originators, issue certificate, prospectus, offering circular etc).

Provided that the originator and SPEs intend the transfer or assignment to be a sale and they act on an arm's-length basis, in other words, there is a true sale of receivables to either offshore or onshore SPEs as a separate legal entity, legal ownership of assets will pass to those SPEs. Those assets cannot be subject to insolvency proceedings of the originator.

Additionally, due to restrictions on the quality and quantity of fund assets, the operations of the fund and the expenditures to be made, it is unlikely that a fund would become insolvent. To the best of our knowledge, such insolvency remoteness has not been eroded in recent years.

5.2 Principal Warranties

Under Turkish law, unless otherwise agreed, the seller will be deemed to make a representation that the transferred receivables exist and the underlying debtors have the ability to pay their debts. In order to override the deemed representation in relation to ability to pay, the agreement should be drafted in way to make it clear that the transaction is a non-recourse transaction.

There may be certain warranties relating to the irrevocable and unconditional transfer of receivables (also future receivables), the accuracy and validity of relevant agreements, documents, representations and data protection.

5.3 Principal Perfection Provisions

The originator, as the owner of the receivables, creates a pool of the receivables, which is then transferred to the fund through a written assignment agreement. Ancillary rights to these receivables such as a pledge over vehicle and surety pass automatically to SPEs; however, to perfect the transfer of mortgages and pledges on motor vehicles, the transfers must be registered at the land and motor-vehicle registries.

Although notification to the debtors is not required to perfect the assignment, it is recommended that the agreement include a provision obliging the originator to notify its debtor(s) of the assignment and to request an acknowledgment of no prior-ranking assignments or counterclaims from the debtor(s). The debtor cannot then raise a good-faith claim for the payments directly to the originator after they have received the assignment notice. In other words, the debtor, following receipt of such a notice, is legally barred from discharging its payment obligations to the originator. Serving a notification and requesting an acknowledgment of no prior-ranking assignments or counterclaims from the debtor of the relevant receivable should also assure the SPE that the receivables were not previously assigned or subject to counterclaims.

5.4 Principal Covenants

General covenants which might used in securitisation documentation cover the following issues:

- an SPE is the sole legal and beneficial owner of the receivables;
- receivables constitute legal valid, binding and enforceable rights and claims against respective borrowers;
- receivables are transferrable and require the respective borrowers to make payments for a period from the date of origination of the receivables;
- an SPE may dispose of the receivables free from the rights of third parties and free from other encumbrances;
- receivables are free of defences, whether pre-emptory or otherwise for the agreed term of its main contract, as well as free of the rights of third parties and, in particular, respective borrowers have no set-off rights;
- status and enforceability of the receivables are not impaired by set-off rights or due to warranty claims or any other rights of a borrower (even if the issuer knew or could have known of the relevant cut-off date of the existence of such defences or rights);
- no borrower maintains deposits on accounts with an SPE;
- each contract relating to the receivables has been duly authorised, executed and delivered to an SPE and is valid, in full force and effect and enforceable in accordance with its terms;
- according to an SPE's records, no contract relating to receivables has been terminated or is in the process of being terminated;
- contracts relating to receivables have been entered into exclusively with borrowers which, if they are corporate entities, have their registered office in Turkey or, if they are individuals, have their place of residence in Turkey;

- contracts relating to the receivables, which are subject to the provisions of the Consumer Protection Act, comply in all material respects with the requirements of such provisions; and
- according to an SPE's records, no insolvency proceedings are initiated against any of the borrowers.

5.5 Principal Servicing Provisions

The Communiqué restricts the entities which are entitled to provide services to funds. Such services can be provided only by founders, originators and entities which are entitled to establish a fund. There is no requirement for the service-provider to have a separate licence.

General servicing provisions under securitisation documentation cover following issues:

- appointment of a servicer pursuant to the servicing agreement; and
- except to the extent otherwise specified, management, administration, service, collections of the receivables and enforcement of the receivables, and performance of or causing to be performed all contractual and customary undertakings to the receivables' obligors on behalf of an SPE in conformity with its Customary Policies and Procedures, and subject to the terms and conditions of relevant agreement and the other transaction documents.

5.6 Principal Defaults

Some defaults used in securitisations are as follows:

- any failure to make any payment, transfer or deposit, or to give instructions or notice to an SPE to make any payment, transfer or deposit pursuant to the relevant agreement;
- any failure to deliver the report pursuant to the relevant agreement;
- any failure to observe or perform duly any other covenants or agreements set forth in the relevant agreement that have a material adverse effect on an SPE; and
- any representation, warranty or certification made in the relevant agreement or in any certificate delivered which is incorrect and has a material adverse effect on an SPE.

5.7 Principal Indemnities

Where funds suffer from repayment difficulties as a consequence of a failure of its board duly to perform its duties under the Communiqué, the CMB is entitled to require the board to be changed.

If repayment difficulties continue even after such a change, the CMB may determine the transfer of the fund to another founder. However, guarantees provided by the first founder, if any, will survive.

With a true sale of receivables, SPEs become the owners of assets that are exclusively to be used to repay the notes, but the investors can always make recourse to those assets in the event that any default occurs on the notes. Security-holders are the beneficial owners.

In the case of a breach of originators under assignment agreement, SPEs are entitled to seek recovery for damages incurred in line with the rules of the Turkish Code of Obligation.

In addition to the foregoing, CML provides another indemnification mechanism for investors. Investor Compensation Centre is a public legal entity executing compensation decisions rendered by the CMB pursuant to the requirements under the CML in the event that investment firms fail to fulfil their cash payment and capital market instrument delivery obligations arising from the investment.

5.8 Other Principal Matters

It is possible for the originator to guarantee to pay the part of obligations which cannot be paid by the fund itself or to provide an insurance coverage within the scope of Insurance Law.

In addition to the requirements outlined under the Communiqué, pursuant to Data Protection Law No 6698, the transfer of the personal data in principle depends on the prior approval of the data subject (owner of the personal data/debtors). Regardless of the existence of prior approvals in relation to the receivables transferred to the SPEs and compliance with law, Data Protection Law No 6698 provides a safe harbour and exemption to obtaining prior approval if transfer of the data is provided for under a specific law. The Turkish Code of Obligations, as a specific law, includes a provision which allows the transfer of personal data in assignments to the extent it is needed to assist collection of debt from the obligors (ie, the enforcement of the assignment). Therefore, there is no need to obtain prior approval of the debtors in the assignment/transfer in this securitisation transaction as long as such data is needed to collect the debt from the obligors.

See **4.13 Material Forms of Credit Enhancement**.

6. Enforcement

6.1 Other Enforcements

There are no other aspects of enforcement of securitisation that are material.

6.2 Effectiveness of Overall Enforcement Regime

Enforceability of transaction documents relating to a securitisation may be limited by bankruptcy, insolvency or

similar laws affecting the enforcement of a creditor's rights generally. Rights of acceleration and recognition of foreign judgments by Turkish courts are subject to conditions such as not being against Turkish public policy rules or necessity of a treaty, etc.

With regard to the enforcement of a choice of law, in principle, the parties to a contract are free to determine the governing law of the contract. Generally, English law is chosen for cross-border security issuances. A choice of English law to govern transaction documents is valid under Turkish law and the courts of Turkey recognise and give effect to the choice of English law as the governing law of transaction documents, except to the extent that to recognise and give effect to such a choice of law would clearly be against Turkish public policy rules.

7. Roles and Responsibilities of the Parties

7.1 Issuers
See **1.2 Special-Purpose Entity**.

7.2 Sponsors
There is no sponsor requirement under Turkish securitisations, except for enhancement mechanisms sought under true sale of receivables in line with the Communiqué.

7.3 Underwriters and Placement Agents
Investment banks mainly perform structuring, underwriting and marketing of a securitisation transaction.

7.4 Servicers
A servicer is the entity collecting principal and interest payments from obligors, and administers the portfolio after a transaction closes. Generally, the originator acts as a servicer.

Servicing contains customer service and payment-processing for the obligors in a securitised pool, and collection actions with regard to the pooling and servicing agreement. Servicing can also cover default management, collateral liquidation and the preparation of monthly reports. The servicer is typically compensated with a fixed servicing fee.

7.5 Investors
Investors purchase the securities issued by an SPE and are therefore entitled to receive the repayments and interests based on the cash-flow generated by the underlying assets.

As a result of the development of the Turkish sukuk market, ijara sukuk, for example, has provided an excellent basis for securitising a pool of ijara financings originated by Turkish islamic banks. There have been a couple of onshore securitisation structures in the past where Kuveyt Türk, Bank Asya and Turkiye Finans issued lease certificates (sukuk ijara) which attracted a great amount of attention, but so far these remain the only transactions of their kind. Turkish islamic banks, such as AlBaraka, Turkiye Finans and Kuveyt Turk, have also issued and offered sukuk to RegS investors outside Turkey.

7.6 Trustees
Asset-backed securities issued by funds are held directly by investors. This relationship is governed by the rules of representation.

The trust concept is not legally defined under Turkish law. However, it is widely accepted that trust provisions in agreements are enforceable under the general provisions of law. So far, however, this has not been tested in Turkish courts.

8. Synthetic Securitisations

8.1 Synthetic Securitisation
Synthetic securitisation is not a standard securitisation method that is used in Turkey; an originator does not transfer the assets to an SPE and assets remain in the originator's balance. However, risks are transferred to an SPE by using credit derivatives or other similar securities and the SPE issues the securities under this type of securitisation based on underlying portfolio.

8.2 Engagement of Issuers/Originators
In a synthetic securitisation, originators transfer credit risks by means of credit derivative instruments or financial guarantees. SPEs issues the securities based on underlying portfolio of exposures (eg credit default swap).

See **8.5 Principal Structures**.

8.3 Regulation
Certain principles of synthetic securitisation are regulated under BRSA regulations; however, Turkish capital markets legislation does not standardise the synthetic securitisation method.

8.4 Principal Laws and Regulations
BRSA Regulation on Measurement and Assessment of Capital Adequacy of Banks dated October 2015 ("Regulation") regulates the capital adequacy criteria for Turkish banks. The Communiqué on Calculation of Risk Weighted Exposures Related to Securitisation numbered 29511 (" Risk Weighted Exposures Communiqué ") that is based on the above regulation outlines the calculation methods and principles for risk-weighted exposures related to standard and synthetic securitisations. It states that the synthetic securitisation is a securitisation where a credit risk is transferred in whole or in part by using credit derivatives or guarantees.

8.5 Principal Structures
In synthetic securitisation structures, instead of receivables, risks and benefits related to those receivables are transferred to SPEs. SPEs issues the securities based on those risks and benefits. In this way, the originator transfers the non-payment and pre-payment risk and return on receivables. During the life of the transaction, the originator makes agreed payments to the SPEs. Since this model of securitisation does not remove the underlying portfolio of assets from the originator's balance sheet, the originator needs to collect the receivables and delivers them to SPEs.

8.6 Regulatory Capital Effect
The Regulation sets forth the principles to ensure banks' equity sufficiency to balance the damage related to risks. To this end, the principal amount for credit risks which include risk -weighted exposures related to assets on the balance sheet, non-cash credits, undertakings and derivative financial instruments needs to be calculated in line with BRSA legislation.

Credit risks are deemed to be transferred in a synthetic securitisation, provided that the following criteria stated under the Risk Weighted Exposures Communiqué is met:

- the risk-weighted exposure amounts of the mezzanine securitisation positions held by the originator bank in the synthetic securitisation do not exceed 50% of the risk-weighted exposure amounts of all mezzanine securitisation positions existing in this securitisation;
- in a synthetic securitisation where there are no mezzanine securitisation positions, if the originator bank can demonstrate that the exposure value of the securitisation positions that would be subject to a 1,250% risk weight exceeds a reasoned estimate of the expected loss on the securitised exposures by a substantial margin and does not hold more than 20% of the exposure values of the securitisation positions that would be subject to a 1,250% risk weight.

In addition to the above-listed criteria, the originator bank must have appropriately risk-sensitive policies and methodologies in place to assess the risk transfer and it needs to demonstrate that the transfer of credit risk to third parties for purposes of the bank's internal risk management and its internal capital allocation.

9. Specific Asset Types

9.1 Common Financial Assets
Auto and consumer loans, trade receivables and receivables arising from financial leasing are the most common financial assets securitised. There are also future flow financings that may be deemed as securitisation transactions, such as the sale of diversified payment rights ("DPRs") of Turkish banks issued by offshore SPEs.

9.2 Common Structures
The above-mentioned financial assets to be transferred are subject to transfer of receivables provisions under Article 183 et al of the Turkish Obligations Law, and onshore securitisation relating to such assets shall take effect under the CMB laws.

Paksoy
Orjin Maslak
Eski Büyükdere Caddesi, No:27, K:11
Maslak
34485 Istanbul
Turkey

Tel: +90 212 366 4700
Fax: +90 212 290 2355
Email: contact@paksoy.av.tr
Web: www.paksoy.av.tr