

client alert

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REDESIGNING THE PLEDGE OF MOVABLE PROPERTIES IN COMMERCIAL TRANSACTIONS

Small and Medium-Sized Enterprises ("**SME**") mainly resort to bank loans to finance their commercial activities. Due to the limited number of securities granted in consideration of the extended loans, the Turkish Civil Code's physical delivery requirement for movable properties and time-consuming procedures in the foreclosure of pledged properties awarded a secondary place to the pledge of movables in terms of the securities granted to the banks.

The Law on Pledge of Movable Properties in Commercial Transactions No. 6750 ("**Law No. 6750**") and its secondary legislation, which is composed of the Regulation on the Establishment of Pledges in Commercial Transactions and Use of Rights Upon Default ("**Regulation on the Establishment**"), the Regulation on the Registry of the Pledged Movables ("**Regulation on the Registry**") and the Regulation on Valuation of the Movable Properties in Commercial Transactions ("**Regulation on the Valuation**"), came into force on 1 January 2017. By way of abolishing the Commercial Enterprise Pledge Law No. 1447, Law No. 6750 introduced a number of major reforms in terms of the pledge of movable properties in order to boost the access of SMEs to financing. Salient information pertaining to Law No. 6750 and its secondary legislation is briefly summarised below:

SCOPE

Unlike the pledges established under the Commercial Enterprise Pledge Law, which covers the trade name, enterprise name, intellectual property rights and machinery, tools, equipment and motor vehicles allocated to the commercial activities of the enterprise, Law No. 6750 allows enterprises to pledge:

- receivables,
- perennial trees bearing fruit,
- stock,
- livestock,
- revenue and income,
- licenses (other than administrative authorisations) and permits that are not required to be registered with other registries,
- rental income,
- tenancy rights,
- consumable materials,

- raw materials,
- agricultural products,
- wagons, and
- those movable assets, rights and jointly owned properties in possession of third parties,

without a requirement for physical delivery, which enables the relevant enterprise to continue its business without interruption.

It should be noted that the provisions of the Regulation on the Establishment and the Law No. 6750 will not be applied to pledge agreements related to:

- financial agreements on capital market instruments, derivatives and account pledges,
- pledges of movable properties established under the Turkish Civil Code,
- pledges of vehicles established under the Highway Traffic Law,
- pledges over aircrafts established under the Turkish Civil Aviation Law,
- ship mortgages established under the Turkish Commercial Code, and
- pledges over mining rights and ore established under the Mining Law.

ESTABLISHMENT

The pledge agreement shall be prepared either in written form and signed before the Pledged Movable Property Registry's official, or notarised before the notary public; or in electronic form and signed via secured electronic signature. The Regulation on the Establishment lists the minimum mandatory content of the pledge agreements as follows:

- the trade name, registry number and other I.D. details and signatures of the pledger, pledgee and their representatives;
- the subject of the underlying agreement;
- where the amount of secured obligation is determined, the amount of the obligation and security amount;
- where the amount of secured obligation is not determined; the limit of the security amount;
- currency of the pledge;
- the pledged asset and distinguishing features of the relevant asset;
- the pledge system determined at the establishment of the pledge, and where the fixed degree system is implemented in the pledge, the value and ranking of each pledgee;
- where any valuation is made under the Regulation on Valuation, the value of the pledged movable asset;
- the clause on exercising the transfer of ownership rights in the event of default; and
- the statement regarding who will bear the costs of the pledge registration before the Pledged Movable Property Registry

PLEDGE WITHOUT PHYSICAL DELIVERY AND MOVABLE PROPERTY REGISTRY SYSTEM

Unlike the fundamental rule of the Turkish Civil Code, which requires the delivery of pledged assets for the establishment of the pledge, Law No. 6750 enables commercial enterprises to pledge their movable property without such physical delivery requirement. Law No. 6750 provides that the establishment of the Pledged Movable Property Registry be supervised by the Ministry of Customs and Trade ("**Ministry**") for the perfection, monitoring and public disclosure of the pledged assets, determining priority among the pledgees and registering disposals on the pledged movable assets.

DEGREE PRINCIPLE IN THE RANKING OF PLEDGES

Law No. 6750 introduces the degree principle in the ranking of pledges to determine the priority among the pledgees in a manner similar to the mortgage provisions applicable to immovable property in the Turkish Civil Code. Law No. 6750 also allows parties to create an escalation right and creates a system where a pledge escalates to the next degree upon release of the prior-ranking pledge.

REMEDIES IN THE EVENT OF DEFAULT AND EXECUTION

According to Law No. 6750, the pledgee may request:

- the transfer of the ownership of pledged movable property from the execution office to itself, provided that the pledgee is a first-degree pledgee;
- the transfer of its receivables to an asset management company that operates in accordance with the Banking Law; or
- the exercise of lease and license rights for the assets that are not subject to the transfer of possession.

If the secured debt cannot be recovered via the above-mentioned procedures, the pledgee will still have the right to resort to proceedings within the framework of the general provisions of the Execution and Bankruptcy Law.

VALUATION

Prior to establishing the pledge, the value of the pledged asset can be freely determined between the pledgor and the pledgee without receiving any valuation assistance or, where both parties fail to agree on the value, they will request the determination of the value of the pledged movable property from the civil court of peace of the place of residence of the pledgor. In the event the debtor defaults, the pledgee will further request the determination of the value of the pledged movable property according to the Regulation on the Valuation.

MONETARY FINES

In the event of failure by the pledgee to release the pledge within three business days following the fulfilment of the secured obligations, the Ministry shall impose on the pledgee an administrative monetary fine equal to one-tenth of the amount of the secured debt.

The pledgor or the persons who acquire the pledged movable property shall be subject to a judicial monetary fine not exceeding half of the secured debt amount upon request of the pledgee that is unable to partially or fully collect its receivables, where:

- the pledged property is used against the provisions of Law No. 6750;
- the transfer of ownership of the pledged asset is omitted in the event of non-payment of debt;
- the pledged property is destroyed or damaged with the purpose of harming the pledgee;
- the transfer of ownership of the pledged property or the pledged receivables is not registered;
or
- fraudulent actions are carried out specifically to deceive the Pledged Movable Property Registry.

TAX EXEMPTIONS

Execution of the pledge agreement and the transactions performed before the Pledged Movable Property Registry shall be exempt from taxes, duties and charges

In compliance with Turkish bar regulations, information relating to Turkish law matters which are included in this client alert are given by Özdirekcan Dündar Şenocak Avukatlık Ortaklığı, a Turkish law firm acting as correspondent firm of Gide Loyrette Nouel in Turkey.

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