

CLIENT ALERT

CORPORATE LAW | TURKEY |

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REMEDIES AVAILABLE IN THE CASE OF CAPITAL LOSS OR OVER-INDEBTEDNESS

On 15 September 2018, a Communiqué on the procedures and principles relating to the implementation of Article 376 of the Turkish Commercial Code (the "**Communiqué**") was published in Official Gazette No. 30536.

The purpose of the Communiqué, issued by the Ministry of Trade, is to set forth the procedures and principles to be implemented in the event of a capital loss or the over-indebtedness of joint-stock companies (*anonim şirket*, in Turkish), limited liability companies (*limited şirket*, in Turkish) and partnerships limited by shares (*sermayesi paylara bölünmüş komandit şirket*, in Turkish).

While the Communiqué mainly reiterates the provisions of Article 376 of the Turkish Commercial Code, it also introduces new and important remedies in addition to those already existing under Article 376.

LOSS OF HALF OF THE SHARE CAPITAL AND STATUTORY RESERVES

Pursuant to Article 376/1 of the Turkish Commercial Code, if it is understood from the latest annual balance sheet that half of the sum of the share capital and statutory reserves has been lost, the board of directors will immediately inform the general assembly and propose the remedial measures it considers appropriate.

Examples of remedial measures brought by the Communiqué are as follows: Completion of the share capital (see below), a share capital increase, closing or decreasing the capacity of certain production units / sections, the sale of subsidiaries, modification of the marketing system, etc.

LOSS OF 2/3 OF THE SHARE CAPITAL AND STATUTORY RESERVES

Pursuant to Article 376/2 of the Turkish Commercial Code, if it is understood from the latest annual balance sheet that two-thirds of the sum of the share capital and statutory reserves have been lost, and the general assembly does not decide to complete the share capital or to decrease the share capital to the remaining third, the company will automatically dissolve.

The remedial measures listed in the Communiqué are a closed list in this case:

- **Completion of the share capital**

Completing the share capital requires the shareholders to make a cash injection to the company (*pro rata* to their shareholding) with a view to covering the lost part of the share capital.

The cash injection must be gratuitous, meaning that the contributed amount cannot be withdrawn, and cannot be considered as debt or a share capital advance.

The completion of the share capital requires the adoption of a general assembly resolution with a unanimous vote. However, if the resolution is not finally adopted, shareholders wishing to proceed with completion of the share capital may still individually make a cash injection.

- **Decreasing the share capital**

This measure requires the adoption of a general assembly resolution on decreasing the share capital to one-third of the original level.

- **Increasing the share capital**

- *Simultaneous decrease and increase of the share capital*

While this measure is stated as a form of completion of the share capital under the Parliamentary explanations of Article 376 of the Turkish Commercial Code, the Communiqué deals with it under the share capital increase option.

This measure requires the adoption of a general assembly resolution deciding on the simultaneous decrease and increase of the share capital. The decrease should be equal to the amount of the loss. One-quarter of the amount determined for the capital increase must be paid before the registration of the operation with the competent trade registry.

- *Direct increase of the share capital*

While a share capital increase is not expressly stated under Article 376 of the Turkish Commercial Code or its Parliamentary explanations, this remedy has already been frequently implemented under the practice. The Communiqué, therefore, brings clarity to an existing practice while codifying it.

This measure requires the adoption of a general assembly resolution deciding to increase the share capital.

The Communiqué provides that, in this case, funds covering one-half of the share capital must be paid before the registration of the operation with the competent trade registry. Accordingly, after the completion of the operation, the new net equity must be equal to or higher than one-half of the new share capital.

OVER-INDEBTEDNESS

Pursuant to Article 376/1 of the Turkish Commercial Code, if there are indications causing suspicions that a company's liabilities exceed its assets, the board of directors will have an interim balance sheet prepared in accordance with both (i) the going concern concept and (ii) the liquidation value of the assets. If it is understood from that balance sheet that the assets are not sufficient to cover the receivables of creditors of the company, the board of directors must notify the commercial court of this situation and declare the bankruptcy of the company.

Article 376 of the Turkish Commercial Code provides for just one option in case the assets are not sufficient to cover the receivables of creditors of the company: the board of directors must notify the commercial court of this situation and declare the bankruptcy of the company.

This being said, the Communiqué now entitles the board of directors to convoke a general assembly to take measures foreseen with respect to the loss of two-thirds of the sum of the share capital and statutory reserves.

As the company would have negative equity in this case, the only remedial measures applicable would actually be (i) the completion of the share capital and/or (ii) a direct increase of the share capital.

FLEXIBILITY REGARDING F/X LOSSES

Last but not least, the Communiqué provides that, until 1 January 2023, foreign exchange losses arising from non-performed obligations will not be taken into account when calculating a capital loss or over-indebtedness within the scope of Article 376 of the Turkish Commercial Code. This provision arises from the general action plan put in place by the Turkish government with a view to protecting Turkish companies against recent fluctuations affecting the Turkish currency.

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

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