COMMERCIAL LAWS OF TURKEY
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AN ASSESSMENT BY THE EBRD

Office of the General Counsel

European Bank
for Reconstruction and Development

CONTENTS

Basis of Assessment: *This document draws on legal assessment work conducted by the Bank (see www.ebrd.com/law) and was last updated during the preparation of the 2012 EBRD Strategy for Turkey, reflecting the situation at that time. The assessment is also grounded on the experience of the Office of the General Counsel in working on legal reform and EBRD investment activities in Turkey and does not constitute legal advice. For further information please contact ltt@ebrd.com .*

1. Overall Assessment

Turkey has had a long-standing, un-interrupted commercial law tradition, going back to the 1920s when the new Republic adopted Swiss-based models for its legislation. In the last few years the commercial legislative norms have been amended on several occasions and are gradually being aligned with those of the European Union (EU). In particular, the securities markets legal and regulatory framework has been refined, due to the EU adaptation process, and become more effective. At the same time, while the Turkish electronic communications framework is based upon EU rules, the European Commission (EC) has expressed the view that both the primary law and implementing regulations could be better aligned with the EU *aquis*.

According to the EBRD assessments, Turkish laws are advanced in a number of areas, including corporate governance and public procurement. In other areas, the system still requires upgrading and modernising in order to fully support market activities. This is particularly true of the secured transactions regime, which lacks flexibility. The judiciary is reported to be generally reliable, but there are many reports of lengthy proceedings.

According to the latest EBRD Concessions Sector Assessment, the concessions legislation is in medium compliance with international standards. In particular, one of the biggest issues is the lack of clarity in the division of power and institutional responsibilities on the part of the state.

The 2009 EBRD Insolvency Sector Assessment found that the insolvency laws are in medium compliance with recognised international standards of best practice. In particular, provisions for treatment of estate assets and creditors are compliant with international standards but there is room for improvement in legislation governing liquidation and the reorganisation process.

The new Commercial Code, which will become effective on 1 July 2012, is expected to introduce a number of positive legislative changes and improve the overall business environment in the country. The Code was amended in order to comply with EU norms and the requirements of the World Trade Organisation. Among other positive developments, the provisions of the new Code are deemed to boost auditing standards and transparency.

2. The Legal System

2.1 Constitution and courts

The current Constitution of Turkey was adopted by a national referendum in 1980 and has been amended several times since. According to the constitution, the Republic of Turkey is a democratic, secular and social state governed by the rule of law. The constitution establishes three fundamental organs: the legislative, the executive and the judiciary and recognises the principle of the separation of powers.

The legislative branch in Turkey is the Turkish Grand National Assembly ('the Assembly') (*Turkiye Buyuk Millet Meclisi-TBMM*). It has a membership of 550 deputies, each elected for a four-year term. Elections are single stage and use proportional representation. A political party must have at least 10 percent of the votes to enter parliament. The Assembly is responsible for the enactment, amendment and repeal of laws. The laws adopted by the Assembly shall be either promulgated by the President within 15 days or referred back to the Assembly for further consideration.

The executive branch of the government is represented by the President and the Council of Ministers. The President is the head of state and elected by the public for a period of 5 years as amended on May 2007. The Constitution bans the re-election of the President for more than two terms.

The Council of Ministers consists of the Prime Minister, who is elected in national elections, and the ministers, who are nominated by the Prime Minister. The ministers may be dismissed by the President upon the proposal of the Prime Minister.

According to the Constitution, the judicial power in Turkey is exercised by independent courts in accordance with the security of tenure of the judges.

Constitutional jurisdiction is overseen by the Constitutional Court consisting of 11 regular and 4 substitute members appointed by the President.

Civil and penal matters are ruled by the Courts of Justice. The lowest Courts of Justice are the Civil or Criminal Courts of the Peace (*Sulh Hukuk/Ceza Mahkemeleri*). All matters that are not specifically assigned to the Courts of the Peace are under the jurisdiction of the Civil or Criminal Courts of First Instance (*Asliye Hukuk/Ceza Mahkemeleri*). The Civil Courts of First Instance have also specialised branches such as Commercial Courts (*Ticaret Mahkemeleri*) and Labor Courts (*Is Mahkemeleri*). The last instance for reviewing the decisions made by the Courts of Justice is the High Court of Appeals (*Yargitay*).

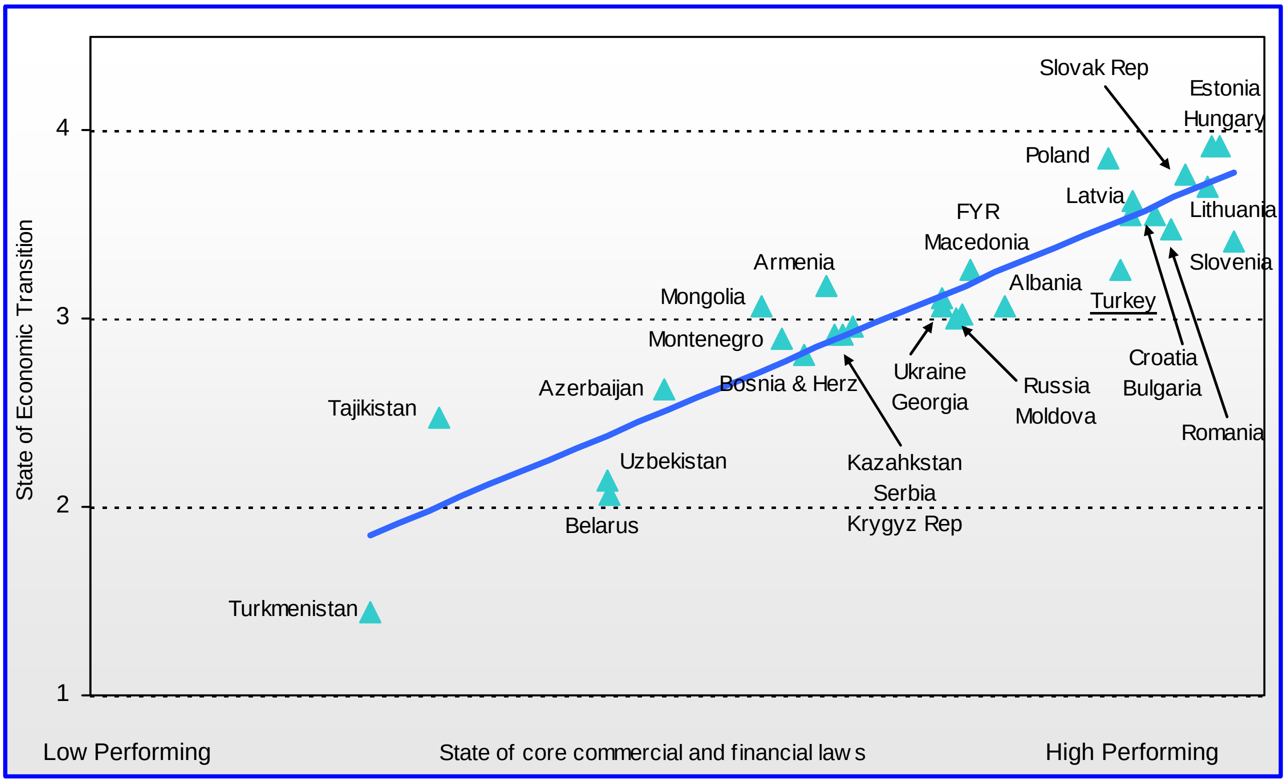
Matters of public law involving an administrative organ are under the jurisdiction of the Administrative Courts (*Idare Mahkemeleri*). Similarly, the Tax Courts (*Vergi Mahkemeleri*) rule on tax disputes. Both the decisions of the Administrative Courts and Tax Courts are examined by the Regional Administrative Courts (*Bolge Idare Mahkemeleri*) upon an appeal raised by one of the parties. The last instance for reviewing the decisions given by administrative courts is the Council of State (*Danistay*). The Turkish judicial system also has military courts for matters involving military personnel or relating to military service.

Finally, the Court of Jurisdictional Disputes (*Uyusmazlik Mahkemesi*) is empowered to deliver final judgements in disputes between civil, administrative and military judiciary branches concerning their jurisdiction and decisions.

2.2 Relationship between legal transition and economic progress

Experience in the transition countries suggests that the degree of respect for the rule of law and progress in economic transition advance or regress hand in hand, as demonstrated in Chart 1. Accordingly, it is fair to say that Turkey's future economic prosperity is dependent in part on further development of the legislative framework and sound implementation of the laws.

Chart 1 – Rule of law and progress in transition in the EBRD countries of operations



***Source**: EBRD Transition Report 2010 Table 1.1; EBRD Composite Country Law Index, July 2011*

***Note**: The **horizontal axis** measures the performance of commercial and financial laws. The **vertical axis** displays the EBRD transition index as an average of transition indicators between 1997 and 2010 with 1 referring to very early transition stages, and 4 referring to an advanced transition level.*

2.3 Recent developments in the investment climate

The Turkish government is keen to attract foreign direct investment. The Government's Annual Programme, announced in July 2011 by the Prime Minister focuses on the development of an enterprise-friendly system, in which efficiency is increased and bureaucracy reduced. To achieve these goals the National Competition Authority continues to strengthen its anti-trust regulation and competition advocacy activities. Recently, effort has been made to further coordinate competition policies with public procurement practices and sector regulators in the network industries.

Furthermore, Turkey has adopted liberal principles with respect to foreign capital under its direct foreign capital regulations.

The purpose of such regulations is the encouragement of foreign capital. According to Turkish Law:

- Enterprises with foreign capital benefit from the same rights, exemptions and other conveniences granted to domestic capital and enterprises operating within the same activity fields and under the same conditions;
- Incorporation of a company, participation in a partnership, opening a branch office and establishing a liaison office with respect to foreign capital are regulated for foreigners;
- The principle requiring each real or legal person providing foreign capital to make a minimum capital contribution of USD 50,000 has been abolished;
- Enterprises with foreign capital shall be subject to the same procedures as domestic companies on capital increase, amendments to articles of association, representation of shareholders in the general assembly etc.

Moreover, the provisions of the new foreign direct investment law facilitate and streamline the process of setting up a company in the country. According to the law, companies can now be set up within 24 hours, although in practice, it may take up to 6 days.

One of the persistent issues that appears to be holding back the development of the investment climate is a heavily bureaucratic, overburdened and slow judiciary. The parliament has passed amendments restructuring the Court of Appeal and provided it with greater resources; however the results of the amendments are yet to be seen.

The World Bank's Doing Business Report for 2012 has ranked Turkey 71st on the ease of doing Business and 61st on starting a business out of 183 countries assessed. Although, Turkey has moved up 2 places since 2011 in the ease of doing business rankings, the report highlights that the country remains in the lower tiers for closing a business, employing workers, and dealing with construction permits.

The adoption of the new Commercial Code is deemed to have a positive impact on the further development of the investment climate in the country. The amended provisions of the new Code are expected to bring the legislation in line with European Union norms and improve standards of financial disclosure, particularly for large corporate groups, as well as the rights of shareholders.

2.4 *Freedom of Information*

There is no specific right of access to information in the 1982 Turkish Constitution. Article 26 gives right of free expression including the right to receive information. The Turkish Law on the Right to Information, Law No: 4982 was enacted in 2003 and came into force in April 2004. Following the enforcement of the act, all public institutions have established their freedom of information units and started to accept access to information requests including those through the Internet.

Since that time there have been a number of other progressive developments. Following the enactment of the Right to Information Act in Turkey, a Right to Information Assessment (Review) Council was established to deal with appeals on rejected right to information requests. The Council's activities are regulated by article 14 of the Right to Information Act 2003.
In November 2005, the Right to Information Act was amended in order to enable citizens to dispute denials of requests for information. Initially the Council had provided very limited information about its activities and decisions. The Council also did not have a properly functioning website until March 2008. However, the development of the website has no doubt influenced the Council to change its policy in terms of the publications of its decisions and started to publish all of its decisions.

3. Evaluation of selected commercial laws

The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: concessions, corporate governance, insolvency, judicial capacity, public procurement, secured transactions, securities markets and telecommunications. The existing tools assess both the quality of the laws "on the books" (also referred to as "extensiveness") and the actual implementation of such laws (also referred to as "effectiveness"). This section presents a summary of the results accompanied by critical comments of the Bank's legal experts who have conducted the assessments.

All available results of these assessments can be found at www.ebrd.com/law.

3.1 *Concessions*

There is no general framework for PPP/Concessions in Turkey but Concessions have been commonly used for a long time. Policy framework for PPPs is the domain of the State Planning Organisation per the following policy documents: the 9th 2007-2013 Development Plan and the 2010-2012 Medium-Term Implementation Programme.

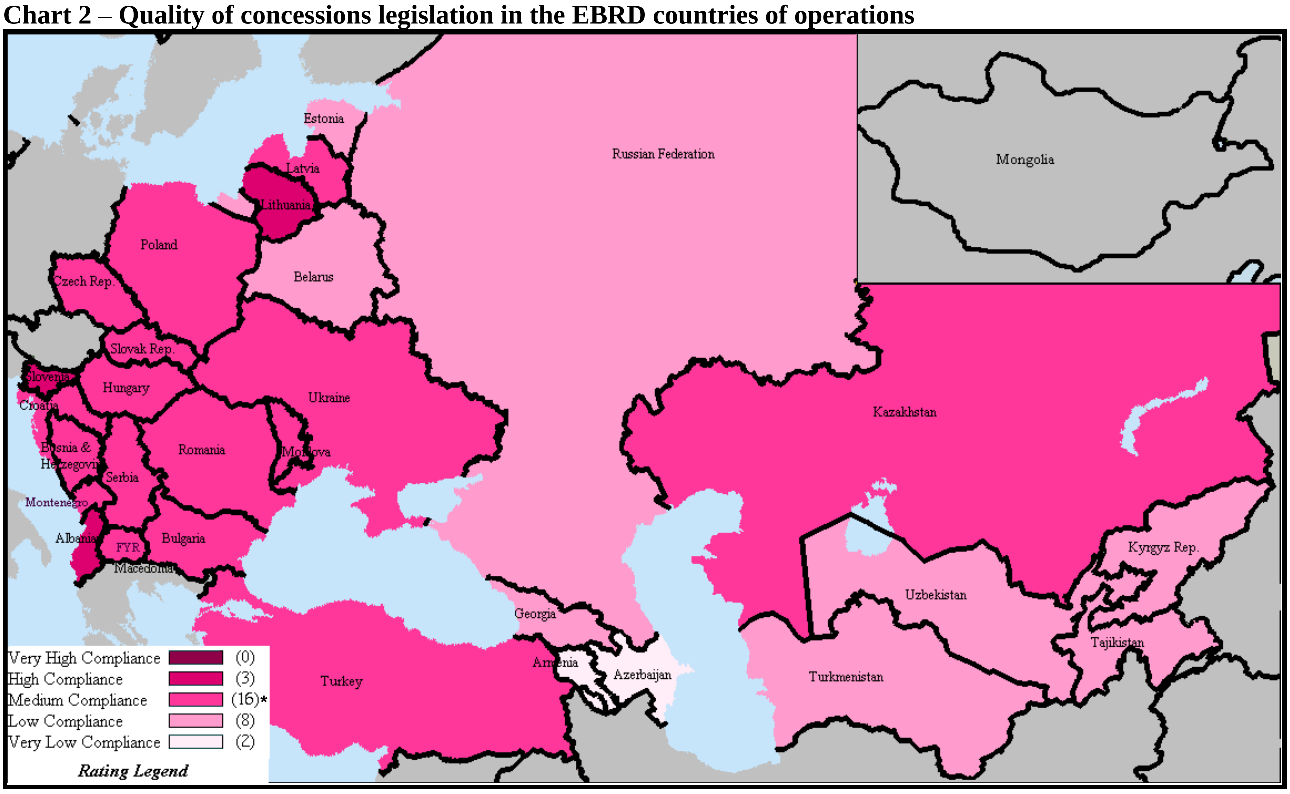
Relevant legislative provisions are contained in sector-specific laws, such as Law No. 3996 on certain infrastructure and public services; Law No. 3096 for the generation, transmission, distribution and sale of electricity by private undertakings; Law No. 3465 on building, maintenance and operation of highways; Law No. 5335 on airports and privatization (and operation) of rail and ports' assets; The Privatization Law No. 4046; or in general laws, such as Municipality Laws No. 5216 and No. 5393; Special Provincial Administration Law No. 5302; State Procurement Law No. 2886; Public Procurement Law No. 4734; Law No. 4501 on International Arbitration Relating to Concessions; International Arbitration Law No. 4686; State Council Law No. 2575; and Administrative Procedural Law No. 2577.

Based on the results of the EBRD Concessions Sector Assessment, the Turkish concessions legislation was found to be in medium compliance with international standards. (See Chart 2 below). Turkey seems to be one of very few EBRD countries of operations (if not the only) where there is a ‘legislation gap’ in the sense that PPP practice so far has been more positive than the proximity of Turkish laws with international best standards. This may be explained by the relatively well developed administrative and judicial system along with a long history of private sector involvement.

The following legal gaps are worth mentioning: current decentralisation of PPP rules presents certain difficulties for market participants and financiers and current legislation does not cover all the common sectors with concession potential (those not covered include justice, education and culture). There is a lack of clarity in the division of powers and institutional responsibilities on the part of the public sector. There is no unified definition of “concession” and no rules on the creation of security interests, these have resulted in ambiguity about the concepts such as “concession”, “public order”, “public policy”, “public interest”, “step-in-rights”. Some positive features include the Law No. 4501 on International Arbitration Relating to Concessions allowing the parties to choose arbitration for the settlement of disputes (e.g. 3G concession in the telecoms sector) (see Chart 3 below).

The Draft PPP law initiated by the State Planning Organisation has been around for a few years and still waits to be formally considered by the Parliament. It aims at defining the PPP concept, principles, sectors, procedures, models, while allowing a sufficient degree of flexibility and establishing an administrative agency managing PPP projects and the institutional infrastructure generally.

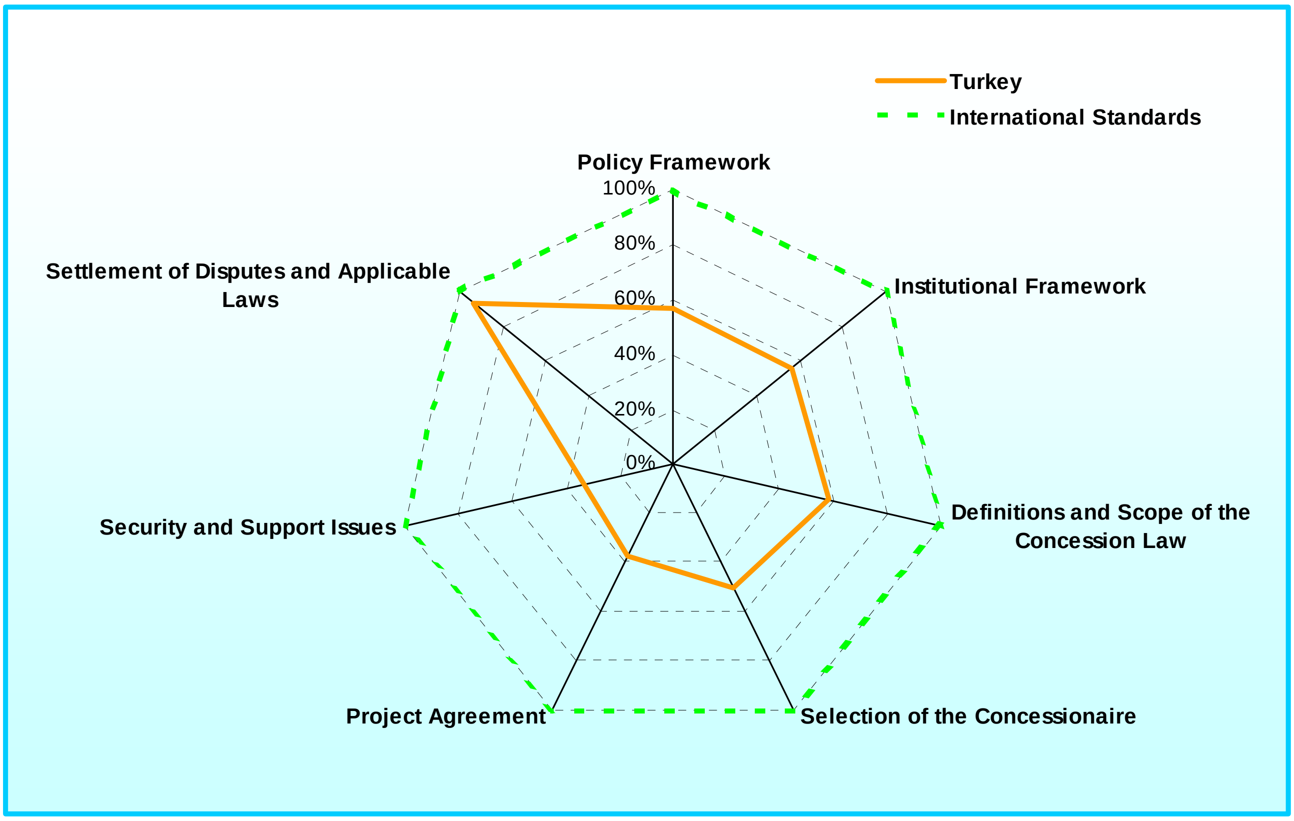
Chart 2 – Quality of concessions legislation in the EBRD countries of operations



***Source**: EBRD Concessions Sector Assessment 2007/08*

***Note**: The various categories represent the level of compliance of a given country’s legislation (“the laws on the books”) with international standards such as the UNCITRAL Model Legislative Provisions on Privately Financed Infrastructure Projects. The asterisk indicates in which category Turkey ranks.*

Chart 3 – Quality of concessions legislation – Turkey (2007/8)



***Source**: EBRD Concessions Sector Assessment 2007/8*

***Note**: The extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the 'web', the more closely concessions laws of the country approximate these standards.*

3.2 Corporate governance

The main law regulating companies and corporate governance in Turkey is the Commercial Code, which has been amended several times since its enactment in 1956. The Code provides the regulatory framework for corporate governance and directors' duties in Turkey. The Code will be abolished by the new Commercial Code (Law N. 6102, dated 13 January 2011), which will become effective on 1 July 2012.

Furthermore, listed companies are also subject to the Capital Markets Law enacted on 28 July 1981. Also, the "Corporate Governance Principles", issued by the Capital Markets Board in June 2003 and amended in February 2005 are a set of voluntary recommendations to be implemented by listed companies according to the so-called "comply or explain" mechanism.

The Banking Act, the Regulation on the Internal Systems of Banks and the Regulation on Banks' Corporate Management Principles provide provisions with specific reference to corporate governance of banks

The Banking Act (Law No.5411, dated 1 November, 2005, as amended) regulates the principles and procedures for ensuring confidence and stability in financial markets, the efficient functioning of the credit system and the protection of the rights and interests of depositors.
The Regulation on the Internal Systems of Banks (published in November 2006) sets out the procedures and principles concerning the internal control, internal audit and risk management systems to be established by banks and the functioning of these systems.

The Regulation on Banks' Corporate Management Principles (published in November 2006) regulates the structures and processes relating to the corporate management of banks.

The 2007 EBRD assessment on corporate governance showed Turkey being in "High Compliance" with the OECD Principles of Corporate Governance and only minor shortcomings were evidenced (see Chart 4 below). The assessment has revealed that the provisions regarding the role of stakeholders are the least developed in the legislation. In particular, the law does not require employee representation on boards and stakeholders do not have special access to corporate information (See Chart 5 below).

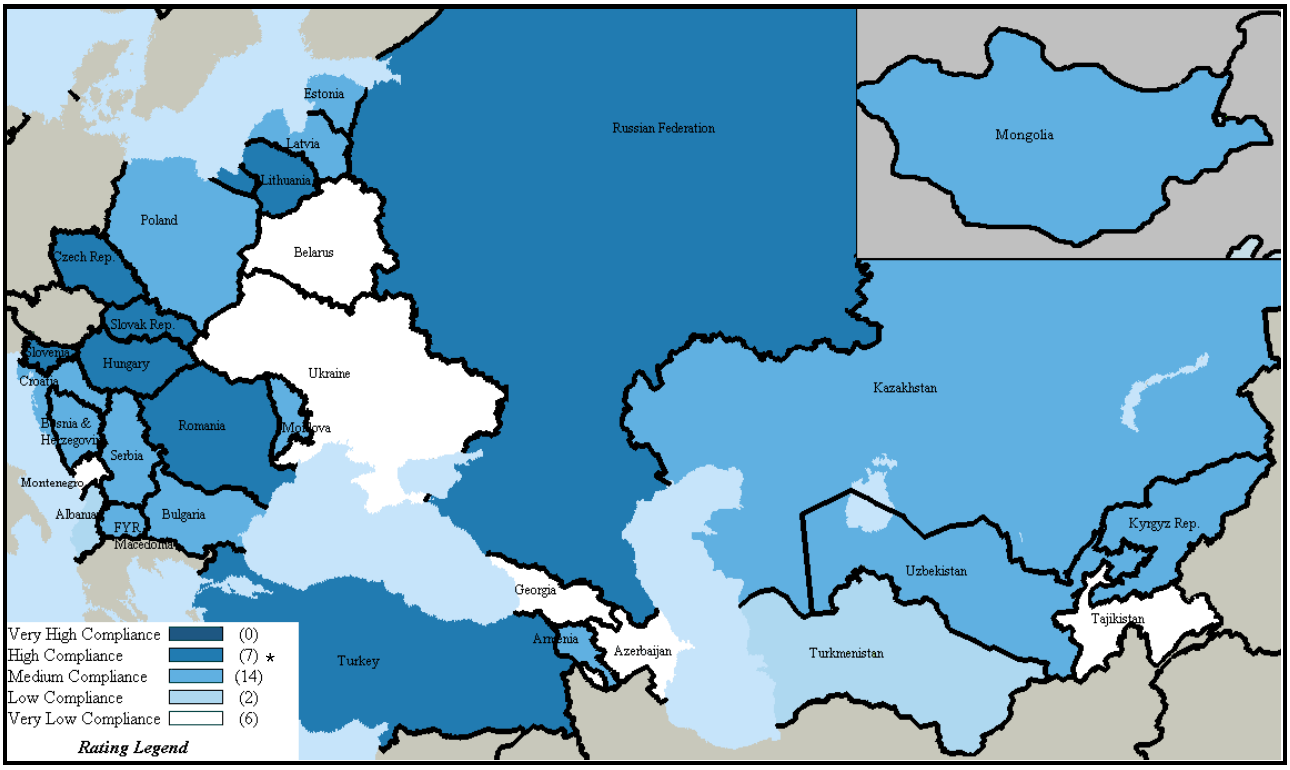
The new Commercial Code will introduce new important rules and concepts to the corporate governance framework. This positive development needs to be coupled with an improvement to the understanding of basic corporate governance issues such as independent directors, the role of board committees and internal control mechanisms.

Moreover, the adequacy of the Corporate Governance Principles, as the main comply-or-explain governance code should be reviewed, as companies generally do not provide detailed explanations of whether they comply with the Principles or not.

In addition, the 2010-2011 assessment on corporate governance of banks highlighted a number of recommendations on how to improve corporate governance of banks. Among those, it is worth mentioning:

- Bank boards should develop a clearer definition of their risk appetite, possibly in co-operation with supervisory authorities;
- Banks boards should review the extent to which they are involved in credit decisions;
- Bank boards should have a more formal role in approving the structure and amount of senior executive remuneration; and
- The banking regulator should have full access to information on the amount and structure of senior executive remuneration, including the remuneration of heads of key control functions.

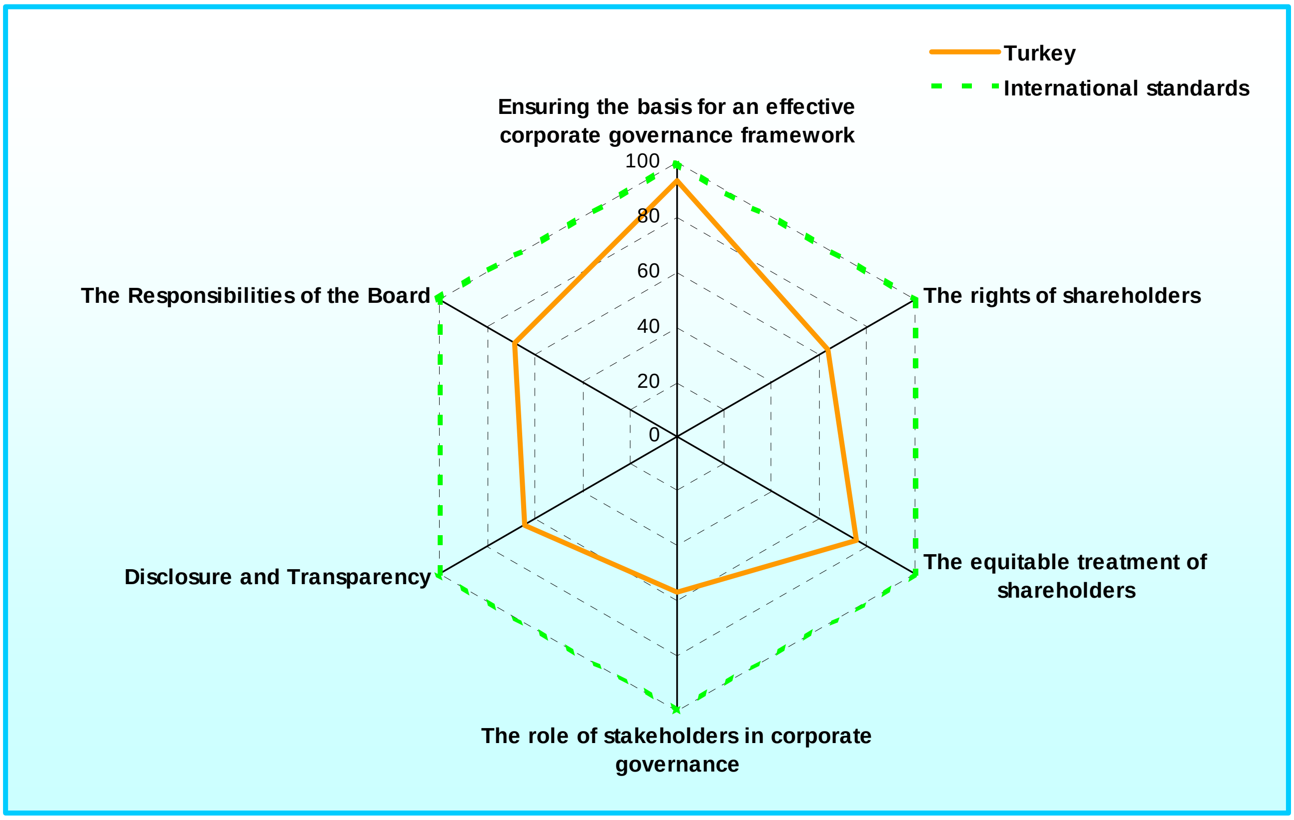
Chart 4 – Quality of corporate governance legislation in the EBRD countries of operations



***Source**: EBRD Corporate Governance Sector Assessment 2007*

***Note**: The various categories represent the level of compliance of a country's legislation (the "laws on the books") with international standards as set out in the OECD Principles of Corporate Governance. The asterisk indicates in which category Turkey ranks.*

Chart 5 – Quality of corporate governance legislation in Turkey (2007)



***Source**: EBRD Corporate Governance Sector Assessment 2007*

***Note**: The extremity of each axis represents an ideal score, i.e., corresponding to OECD Principles of Corporate Governance. The fuller the 'web', the more closely the corporate governance laws of the country approximate these principles.*

3.3 Insolvency

Insolvency in Turkey is primarily governed by the Execution and Bankruptcy Code (EBC), enacted in 1932 and subsequently amended in 2003 and 2004. In addition, the Turkish Commercial Code, Code of Obligations, Code of Civil Procedure and the Banking Act also govern some aspects of the insolvency system.

As Chart 6 indicates, the Turkish insolvency laws "on the books" are in medium compliance with recognised international standards of best practice. Provisions for treatment of estate assets and creditors are compliant with international standards but there is room for improvement in legislation governing liquidation and the reorganisation process (see Chart 7).

At the time of its establishment, the EBC was primarily a debtor friendly regime. However in the wake of the Turkish economic crisis of 2000 to 2001, the Turkish government rigorously reviewed its insolvency procedures. This economic crisis was far reaching and led to various corporate bankruptcy proceedings; thus there was a strong effort to reform and modernise Turkish insolvency regulation and enforcement.

Consequently, the EBC was amended in 2003 and 2004. The 2003 amendments resulted in a number of measures, which objectives were to rejuvenate the national economy by providing regulatory and legal tools to rescue and rehabilitate financially distressed companies. However, the general view on these is that they are disproportionately favourable to debtors at the disadvantage of creditors. Below is a summary of these amendments.

1. <u>Postponement of Bankruptcy</u>

Prior to the 2003 amendment to the EBC, if the debts of the debtor exceeded the value of its assets the officers of the company had to file for bankruptcy with the court. With the 2003 amendment both debtors and their creditors have the opportunity to persuade the court that the debtor can improve its financial situation and thus should not file for bankruptcy. If the court is convinced that the debtor can in fact ameliorate its financial status, the court can postpone the debtor's bankruptcy for one year. The court can extend this postponement period for a maximum of four years (four one year deferrals).

More specifically, the debtor must persuade the court that its development plan, which generally deals with how the debtor will increase revenue and decrease costs, will improve its financial position over the specified period of time. If the court does in fact postpone the bankruptcy, it will also appoint a trustee who will have certain powers specified in the court order (i.e. the right to manage the company, suspend certain transactions, etc.).

2. <u>Reorganisation / Concordat</u>

Pursuant to the 2003 amendments, a debtor can now apply to the court to execute an agreement with its creditors to re-structure its debt payments. The debtor will set aside some or all of its assets to be sold, which will then be distributed to its creditors in accordance with their entitlements. The advantage of this procedure is that it allows debtors to continue business with the remainder of its assets without the burden of its historical debt. However, secured debts remain enforceable notwithstanding reorganisation.

Debtors wishing to reorganise or creditors with the right to institute a bankruptcy proceeding must apply to the court and provide its reorganisation project or "concordat". If the execution court deems that the reorganisation project is likely to succeed, it will order a meeting of the creditors who must decide to accept/reject the project. The required quorum for a reorganisation project's approval is at least one-half of all the creditors and whose debts amount in value to at least two-thirds of the total recorded debts. If this quorum is met, the court must approve the reorganisation project.

The court will approve the execution of the project if the following conditions are met: (1) the debtor undertakes to pay at least 50% of its debts; (2) the suggested payments appear to be payable by the debtor given the total assets of the debtor; (3) the debtor provides sufficient security for the amounts to be paid to its creditors; and (4) the debtor pays for court expenses and charges.

3. <u>Restructuring</u>

The 2004 amendment introduced a third proceeding that allows debtors to apply to the court with a plan to restructure if they: (1) cannot pay their due debts; (2) have liabilities that exceed their assets; or (3) are likely to be subject to the previous conditions in the near future. This plan, however, must have been previously approved by a quorum of creditors affected by it – at least one-half of the creditors affected by the project in number and whose debts amount in value to at least two thirds of the total affected debts. If the court approves the restructuring plan it will not enter a bankruptcy ruling. Additionally, the provisions of the plan are binding and will prevail over any bilateral agreements between the debtor and relevant creditor. However, the amendment includes a safety mechanism for creditors that allows them to apply to the court if the debtor does not fulfil its obligations under the plan. If this occurs, the court has the right to declare the debtor bankrupt.

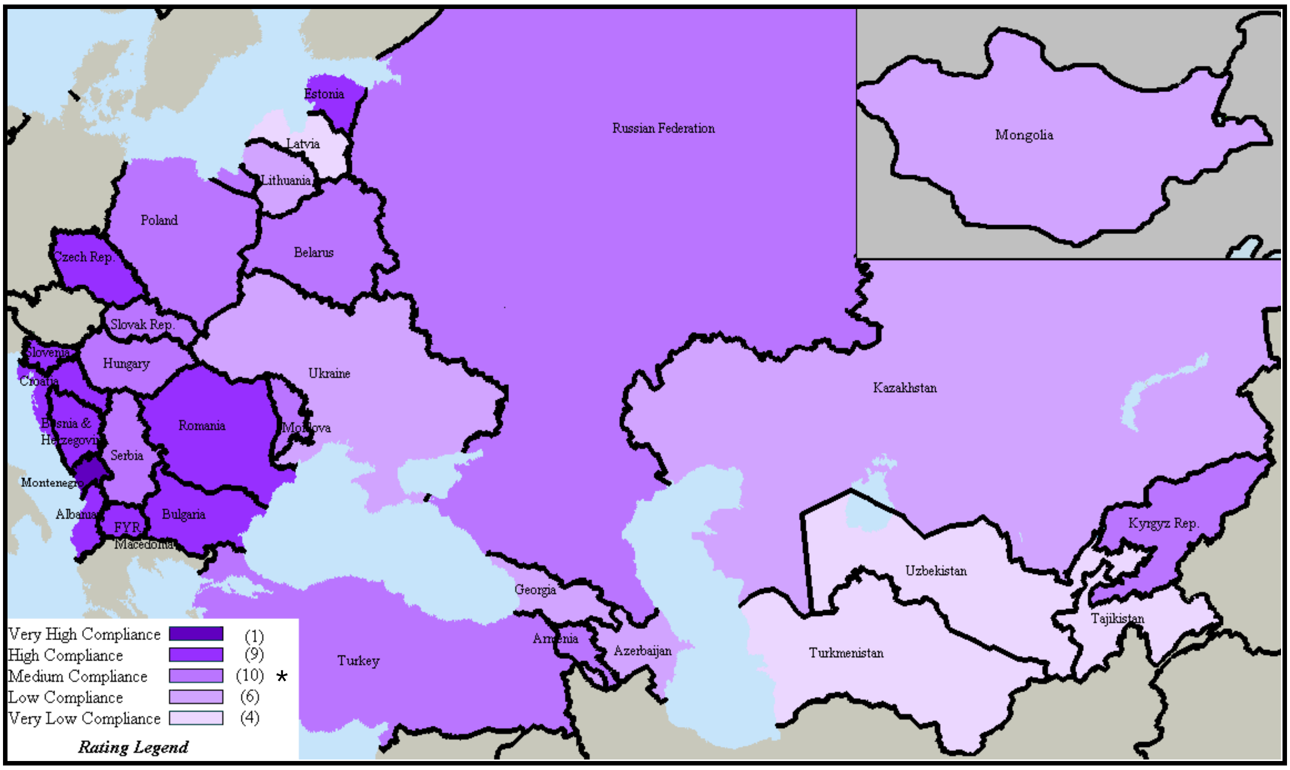
While Turkey's insolvency regime is sound, there remains room for improvement. Regarding reorganisation, the EBC adequately provides for the preparation and approval of a reorganisation plan, but fails to ensure that all creditors receive sufficient information about the plan before voting. A related regulation regarding reorganisation requires plans to certify that creditors have been given all material information necessary to vote, but there is nothing in the insolvency law itself that would guarantee this protection.

Additionally, the EBC would gain from stronger provisions regarding the management of the debtor's finances during the reorganisation and provisions directed at reorganisation financing. Liquidation/termination provisions could also be improved by providing for a complete discharge of the debtor on completion of proceedings and enabling the Turkish courts to assist in respect of foreign proceedings.

In addition to EBC reform, practitioners in Turkey report that there are shortcomings in the system that can hamper its efficiency and effectiveness. The bankruptcy process is seen as relatively slow and it appears both common and easy for debtors to delay the process even further. The courts are also overburdened, resulting in breaks of between two and four months between hearings.

Changes to the insolvency regime in Turkey have aimed at creating new opportunities for debtors and creditors to agree on alternatives to liquidations with the view of salvaging businesses that are, in fact, commercially viable. These changes are complex and require a good deal of fine-tuning. We would recommend the Turkish authorities to closely follow up the effects of the amendments to ensure that they are functioning as intended as well as to address the problems mentioned above.

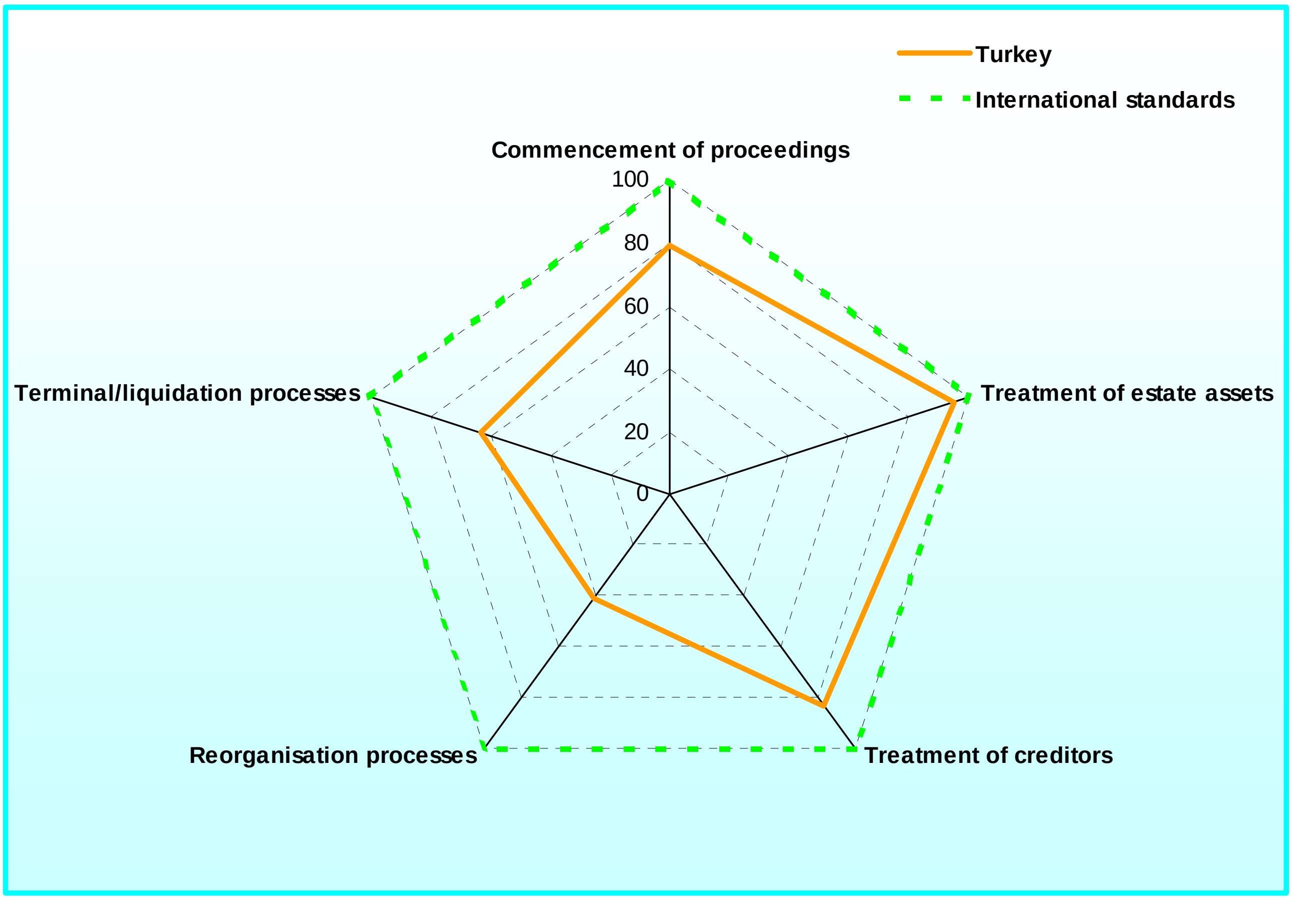
Chart 6 – Quality of insolvency legislation in the EBRD countries of operations



***Source**: EBRD Insolvency Sector Assessment 2009*

***Note**: The various categories indicate the level of compliance of each country's legislation (the "laws on the books") with international standards, such as the World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on Legislative Guidelines for Insolvency Law, and others.*

Chart 7 – Quality of insolvency legislation in Turkey (2009)



***Source**: EBRD Insolvency Sector Assessment 2009*

***Note**: The extremity of each axis represents an ideal score, i.e. corresponding to international standards such as the World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group's "Legislative Guidelines for Insolvency Law", and others.*

3.4 Judicial Capacity

The court structure in Turkey provides for a high level of specialisation in the hearing of different types of disputes. Civil disputes are heard initially by the Civil Court of First Instance, which has specialised branches for dealing with commercial, labour and other types of claims. Appeals lie to the Court of Appeal, and then to the High Court of Appeal, which is the final instance. Matters of public law involving an administrative organ are dealt with by specialist administrative courts, and tax disputes by taxation courts. Appeals from decisions of the administrative and tax courts are heard by the Regional Administrative Court. The last instance of appeal for such matters is the Council of State. Finally, the Court of Jurisdictional Disputes is empowered to deliver final judgements in matters relating to the delineation of jurisdiction as between civil and administrative courts.

The High Council of Judges and Prosecutors is the judicial supervisory body. Recent changes to the law regulating the High Council aim to bolster the independence of the judiciary from the executive. Thus, judicial inspectors (responsible for evaluating the performance of judges and prosecutors) now report to the High Council rather than the Ministry of Justice. Permanent membership of the High Council has been increased from seven to twenty two, and there is now greater representation on the Council from the judiciary, academia and the legal profession. Importantly, the dismissal of judges from office is now open to judicial review.

One of the key concerns about the effectiveness of the Turkish judicial system has been the large backlog of cases and the slow speed of proceedings, particularly in relation to appeals. The latest EBRD–World Bank Business Environment and Enterprise Performance Survey (BEEPS) revealed that only 25% of business responents believe the Turkish legal system is sufficiently fast. In order to address this problem, the parliament passed amendments in 2011 restructuring the Court of Appeal and providing it with greater resources. In particular, the number of chambers at the Court of Appeal was increased from 32 to 38. A further reform which could assist the authorities to tackle the backlog problem would be the introduction of a system of mediation of civil disputes.

3.5 *Public procurement*

Public procurement in Turkey is governed by the Public Procurement Law Act No: 4734, published in the Official Journal No: 22.01.2002/24648 ('the PPL') and the Law on Public Contracts. Since 2002 the PPL has been amended several times. The most significant and extensive amendment was adopted in October 2008, in order to align the national law with the EU Public Procurement Directives.

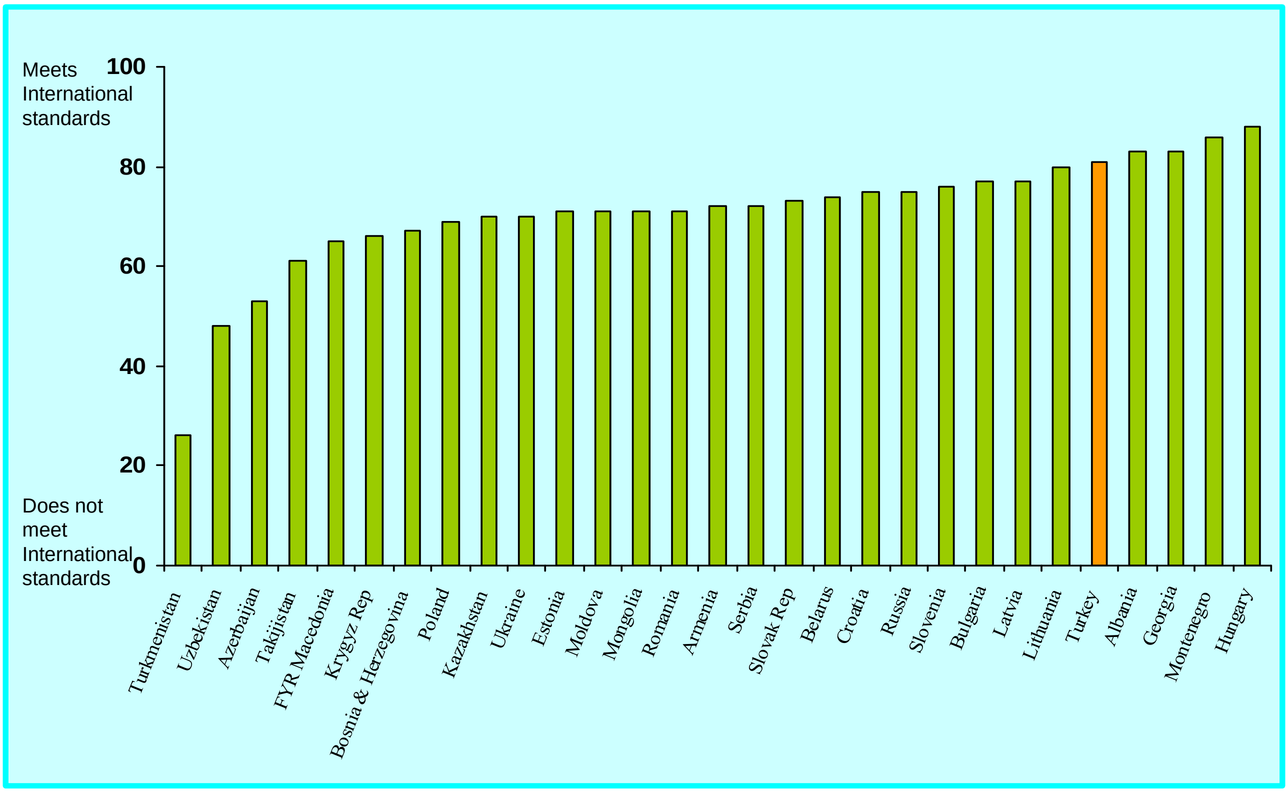
The PPL in principle is in high compliance with international standards (see Chart 8 below); the only major weaknesses are preferential treatment of domestic tenderers, a far-reaching black listing system, and insufficient independence of the public procurement remedy procedures (the review proceedings are conducted by the regulatory authority).

Public procurement legislation in Turkey is based on the principles of the EU Public Procurement Directives, except for the lack of a special regulation for public procurement in the utilities sector. PPL provides for open tender as a default procurement procedure and establishes a comprehensive tendering regulation; still public procurement planning and contract management are not sufficiently regulated (see Chart 9 below). It is evident that all efforts are made to ensure transparency of the procurement process and to combat corruption. At the same time the legal framework embraces most of the efficiency instruments and if eProcurement solutions are fully implemented, Turkish regulation will be very up to date.

Based on the 2010 assessment, local procurement practice in Turkey has increasingly improved and is mostly compliant with international best practice, yet its integrity, transparency and uniformity could still be improved (see Chart 10 below).

The Turkish legal and institutional framework in public procurement is comprehensive and well-managed. Local contracting entities in Turkey are clearly increasing their procurement capacity and learning new procurement techniques (eProcurement). However, some key regulatory matters still need attention, and implementation of the laws could be improved, as some implementation problems were identified by the survey of local practice. Finally, sustainability policies for public procurement are at the initial stage of development in Turkey.

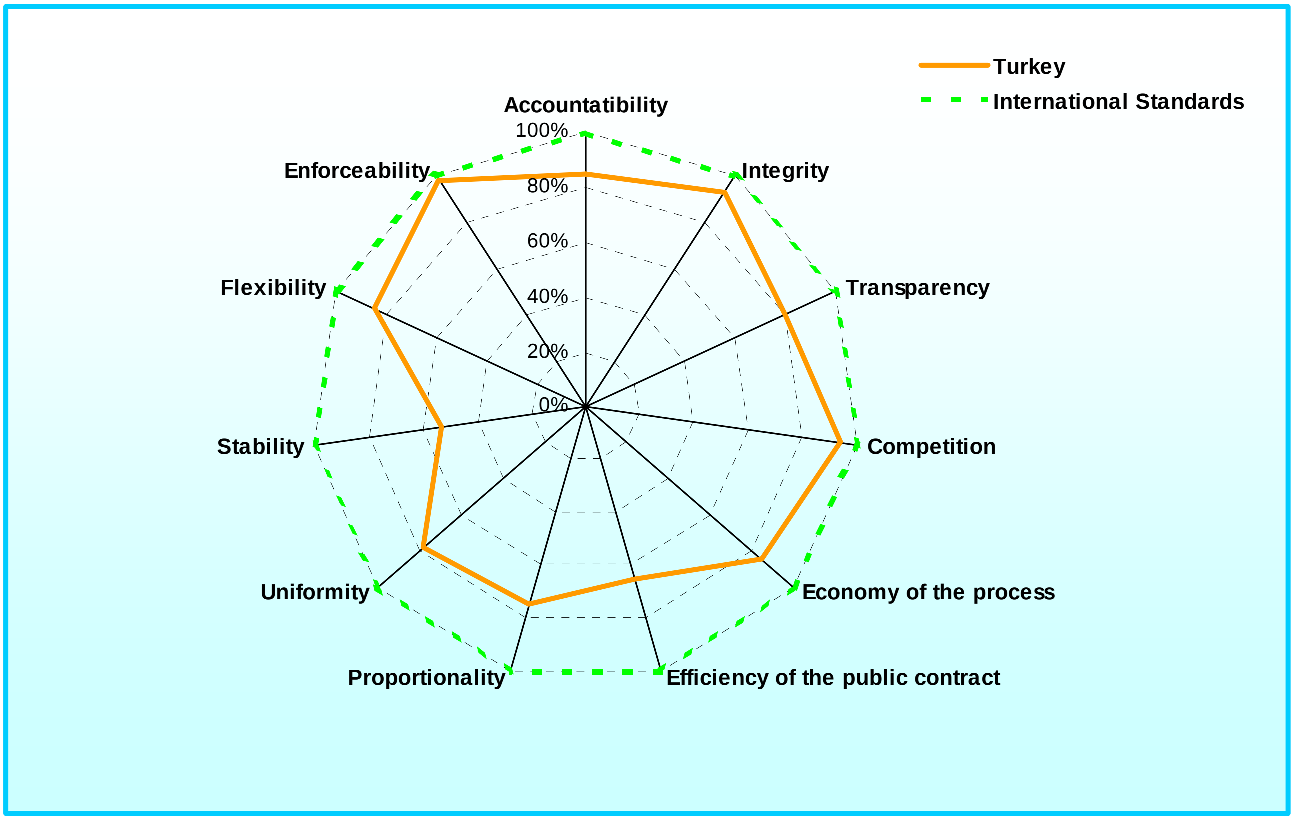
Chart 8 - Quality of Public Procurement legal framework in Turkey as compared to other EBRD countries of operation



***Source**: EBRD Public Procurement Assessment 2010*

***Note**: The score represents the level of compliance of the country's legal framework with international standards such as the revised UNCITRAL Model Law on Public Procurements. Turkey is highlighted in comparison with other countries.*

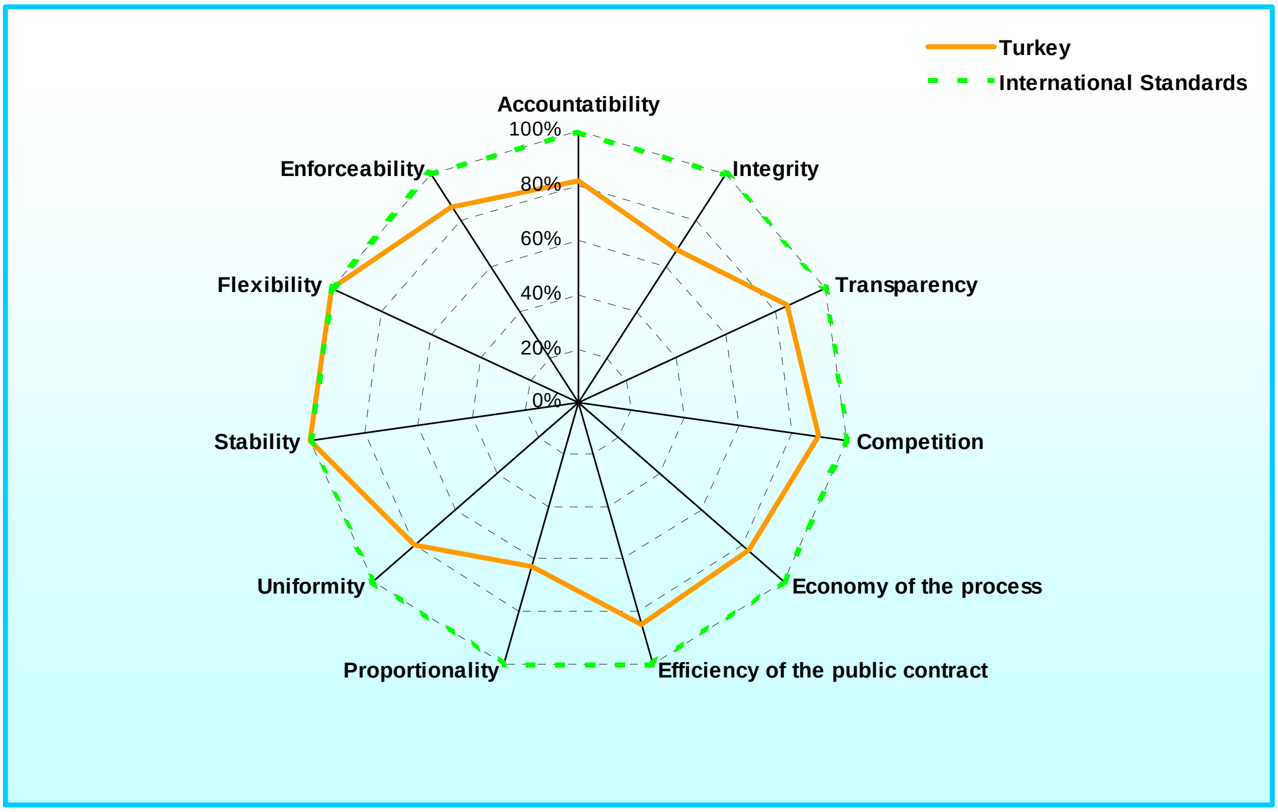
Chart 9 - Quality of Public Procurement legislation – Turkey (2010)



***Source**: EBRD Public Procurement Assessment 2010*

***Note**: The extremity of each axis represents an ideal score in line with international standards such as the revised UNCITRAL Model Law on Public Procurement. The fuller the 'web', the more closely the public procurement laws of the country approximate these standards.*

Chart 10 - Turkey - Quality of local procurement practice (2010)



Source: EBRD Public Procurement Assessment 2010

Note*: The extremity of each axis represents an ideal score in line with international standards such as the revised UNCITRAL Model Law on Public Procurement. The fuller the 'web', the more closely the public procurement practices of the country approximate these standards.*

3.6 Secured transactions

The Civil Code is the main source of law governing secured transactions – both pledges (that is, security rights over movable property) and mortgages (security rights over immovable property). Typically for a civil law regime, the Civil Code comprises a chapter with provisions on property rights, including mortgages (articles 850-938) and pledges (articles 939-972). The Code of Obligations (articles 162-172), the Execution and Bankruptcy Act (articles 145-153) and the 1971 Commercial Enterprise Pledge Act also contain relevant provisions.

Taking security under Turkish law remains a fairly inflexible process, which limits the type of collateral that borrowers may be able to offer and the parties' contractual agreements over the security package. Ways to circumvent legislative limitations have been designed by practitioners but these alternatives are necessarily complex and restricted.

Specific types of pledges have been created by statute to serve a particular segment of the economy, such as, for example, the commercial enterprise pledge. With this instrument, the pledgor can continue to use the pledged assets. The downside of this instrument is that the assets included in the pledge are listed by law on a limited basis (trade and enterprise names, machinery, equipment and vehicles used by the enterprise, and if the parties choose to do so, intellectual property rights) and do not include assets that were not allocated to the activity of the enterprise at the time of the agreement (future equipment), stock in trade or accounts receivable. Moreover, the pledgee's consent will be required for any operation on the collateral (including replacement). Registration of the security is done in the register operated by the Chamber of Commerce. The registers are neither electronic nor centralized and searching is cumbersome.

Pledges over shares are treated as any other pledges – they require the physical delivery of the certificates representing the shares or the annotation into the Central Depository system (for publicly listed companies). The biggest drawback concerns the voting or dividend rights which are not included in the pledge. In practice, the technique used is either to require proxies or to obtain a right of usufruct[1] over the shares from the shareholders.

Taking security over intangible assets such as accounts receivable or bank accounts is a well-established practice; however it is highly formalistic and restrictive. Accounts receivable are usually assigned, as opposed to pledged, and this requires a precise description of the assigned claims. Although the third-party obligor's consent is not needed for the validity of the assignment, the common understanding is that notice should be formally given to the obligor – in fact, many market participants require that this be done by a notary public, to guarantee evidence of the notification's date and contents. An assignment of all future and present claims would not be possible according to the general principles of the Civil Code. Future rights and receivables could be pledged as long as they can be defined in monetary terms at the time of the pledge.

Pledging bank accounts is widely used in practice. Notification to the bank where the account is held is recommended (but not required for the validity of pledge) and the pledged accounts should be specifically identified in the pledge agreement. It seems that there is a consensus among users that the pledgor would not be allowed to close and to draw money from the pledged account without the pledgee's consent.

Mortgages, on the over hand, are the preferred type of security rights over real estate (buildings and land) and the system is well established. The system is fairly similar to that found in other European countries. The Law Amending the Laws Related to Housing Finance, widely know as the Mortgage Law, was enacted in 2007. Specific features include the fact that the mortgaged assets can include "accessories to the immovable property" that are "allocated" to the operation and benefit of the property. In other words, these are movable assets that are attached to a building or land to be mortgaged (e.g.,furniture, equipment). The regime presents a sophisticated system of ranking, which does not entirely depend on the chronological order of registration but also on the parties' contractual arrangement. Escalation rights may be granted, thereby giving a creditor the right to move up a level when the ranking held by another creditor has been released. There are two types of mortgages that can be entered into.

"Definite amount mortgages" secure:

- the principal amount as provided in the mortgage agreement
- up to three years' worth of contractual interest
- default interest
- certain enforcement-related costs and expenses.

If parties confirm a "maximum amount mortgage", they can define the secured debt as they wish, in particular as a credit line or overdraft. It should be noted that the enforcement procedure is considerably easier when the mortgage is a definite amount mortgage as opposed to a maximum amount mortgage.

Modes of enforcement of security rights are in line with the civil law tradition. The *Lex Commissaria* rule applies, which means it would be invalid in the security agreement to provide that in case of default, the creditor is entitled to receive the property's ownership in lieu of payment.

[1] Usufruct is the legal right to use and derive profit or benefit from property that belongs to another person, and provided that the property is not damaged.

The creditor could, however, purchase the collateral during realisation. In theory, out-of-court enforcement and direct sale is legally possible but this requires the consent of all related parties (including that of the pledgor) at the time of default. In practice, such cooperation is unlikely. Enforcement is therefore mostly conducted by the courts' enforcement offices and the property is sold at public auction. The exception to the public auction applies to assets that have a readily established market value (for example stocks, commodities). Enforcement of a commercial enterprise pledge is always led by an executor, who will decide which assets will be realised. Enforcement appears to be slow and inefficient, despite the fact that the law provides that it should happen within one month. Enforcement is also relatively expensive – especially if it is a maximum amount mortgage that is being enforced as the creditor must deposit over 5 per cent of the claim in order to be able to proceed. Appraisal (collateral evaluation) is reported to be problematic. This is significant because on enforcement, the collateral may be sold at auction at 60 per cent of the appraised value (first auction) and 40 per cent at the second auction. Creditors generally do not expect that the property will be sold at market value.

The main policy recommendations would be to build a consensus with the private sector over the opportunity there is to simplify and modernise the secured transactions regime. Even the mortgage market would benefit from a reform on the mode of enforcement, which is lengthy and costly.

3.7 Securities markets

The key regulatory institutions in the field of securities markets are the Capital Market Board; the Central Bank of Turkey; the Undersecretariat of Treasury; the Banking Regulation and Supervision Agency of Turkey; the Istanbul Stock Exchange; the Merkezi Kayit Kurukusu A.S. (the authorised Central Registry Agency) and the IMKB Takas ve Saklama Bankasi A.S. (the authorised Settlement and Clearing Agency of the ISE).

The following acts govern securities markets in Turkey:

a. Capital Market Law including Communiqué on the Registration and the Sale of Debt Securities Serial No. II/22 regulating the primary and secondary debt capital markets activities (Official Gazette, 21 January 2009, No. 27117);
b. Communiqué Serial No. III/33 Regarding Mortgage Covered Securities (Official Gazette, 4 August 2007, No. 26603);
c. Communiqué Serial No. III/38 Regarding Asset Covered Securities (Official Gazette, 12 September 2009, No. 27347);
d. Communiqué Serial No. III/34 Regarding Housing Finance Funds and Mortgage Backed Securities (Official Gazette, 4 August 2007, No. 26603);
e. Communiqué Serial No. III/35 Regarding Asset Finance Funds and Asset Backed Securities (Official Gazette, 27 August, 2008, No. 26980);
f. Banking Law (Official Gazette, 1 November 2005, No. 25983);
g. Communiqué Serial No. VII/10 (Official Gazette, 19 December 1996, No. 22852);
h. Insurance Law (Official Gazette, 14 June 2007, No. 26552);
i. Regulation on the Establishment and Activities of Pension Investment Funds (Official Gazette, 28 February, 2002, No. 24681).

The debt capital markets of Turkey are not as developed as in Western Europe due to its size and relatively young age, but the legal and regulatory framework has been refined, due to the EU adaptation process, and became more effective. Banking laws and regulations are mostly in line with EU directives. As opposed to many other countries, Turkey was not significantly affected by the global financial crisis of 2008-2009. No laws impacting the debt capital markets were adopted specifically to address the said financial crisis. Much of Turkey's current success stems from the way its financial system was rebuilt after its collapse of 2001. Turkey strengthened the local banking system and created strong, independent regulators.

While the local debt capital markets of Turkey are rather sophisticated, they could benefit from further development. Regulations could be amended to allow for the creation of a shelf program (i.e. to allow for fast and flexible issuances) for all types of debt securities. In addition, the process for amending issuance documentation could be eased.

Repo transactions are permitted with respect to certain types of debt securities. Uncertainty exists as to whether individual repo transactions will be classified by the Turkish Revenue as a *repurchase* or a *true sale* from the Turkish taxation and accounting point of view. This uncertainty can discourage investment in repo transactions.

Regulations could be implemented to make the credit rating process more efficient. Arbitrary timelines for the review of credit ratings could be replaced with reviews based on specific risk considerations.

While Turkey has already made some regulatory changes to facilitate Islamic finance in its local debt markets, additional changes that would attract more Islamic finance market participants could be considered.

The credit reporting system in Turkey consists of:

(1) a public credit registry, owned and operated since 1951 by the Central Bank of Turkey; and
(2) a private credit bureau, KKB Kredi Kayit Burosu A.Ş., which started operating in 1997.

There is no specific law on the credit reporting system, but the Central Bank serves as regulator and applies banking law, central bank law, and company law to the system. Additionally a data protection law is in development and will be relevant for the regulation of the credit reporting system when it is approved.

Information regarding the private credit bureau is limited. Because the credit bureau has consultancy services that it performs for remuneration, it was unwilling to participate in the EBRD's research. Information available from KKB's website was used in the assessment peocess. The private bureau was founded in 1995, began its work in 1997 and as of December 2009 had 77 members. KKB's website indicates that it now has 98 members.

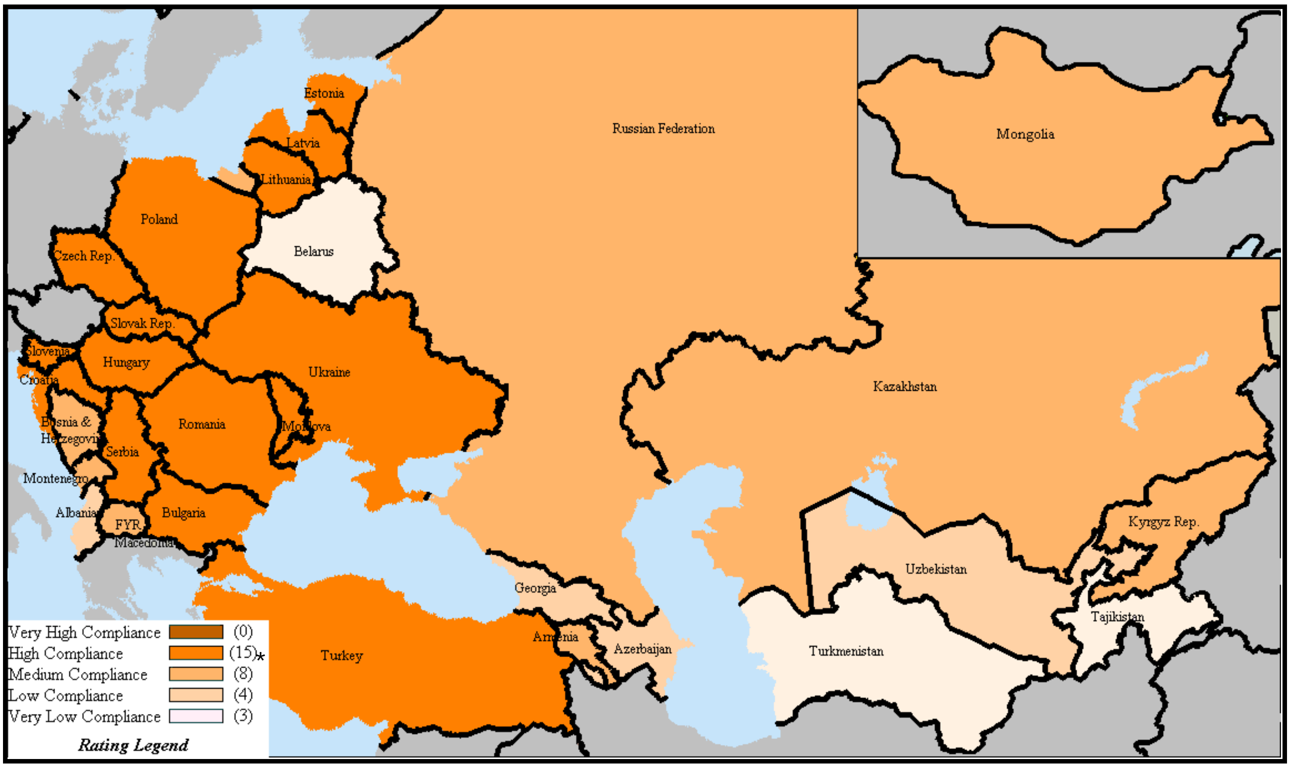
The public credit registry has data on over 8.26 million people and over 476,000 legal entities according to its responses to the EBRD questionnaire. Doing Business 2011 indicates that the public registry has data on 7,799,160 individuals and 2,148,810 firms. These numbers indicate an 18.3 per cent coverage rate in the public registry. No performance data was made available to the EBRD by the private credit bureau, but Doing Business indicated that the coverage includes 20,000,000 individuals and 3,000,000 firms. This represents a 42.2 per cent coverage rate in the private bureau.

Turkey appears to have a reasonably well functioning credit information reporting system. The latest EBRD Securities Markets Legislation Assessment found Turkey to be in "high compliance" with the Objectives and Principles of Securities Regulation published by the International Organisation of Securities Commissions (IOSCO) (See Charts 11 and 12 below).

The legislation nevertheless suffers from important flaws, such as:

- There does not seem to be a system in place to ensure accuracy of the information and it seems that the credit bureau would not be found liable in case of inaccuracy of information or other unlawful wrongdoing. According the Central Bank, there is a possibility of liability for loss to data subjects, but no liability to users;
- It seems that the legal framework does not require consent of the data subject for credit information to be shared, and in practice consent is not obtained; and
- The processes for obtaining credit reports could be simplified and swifter.

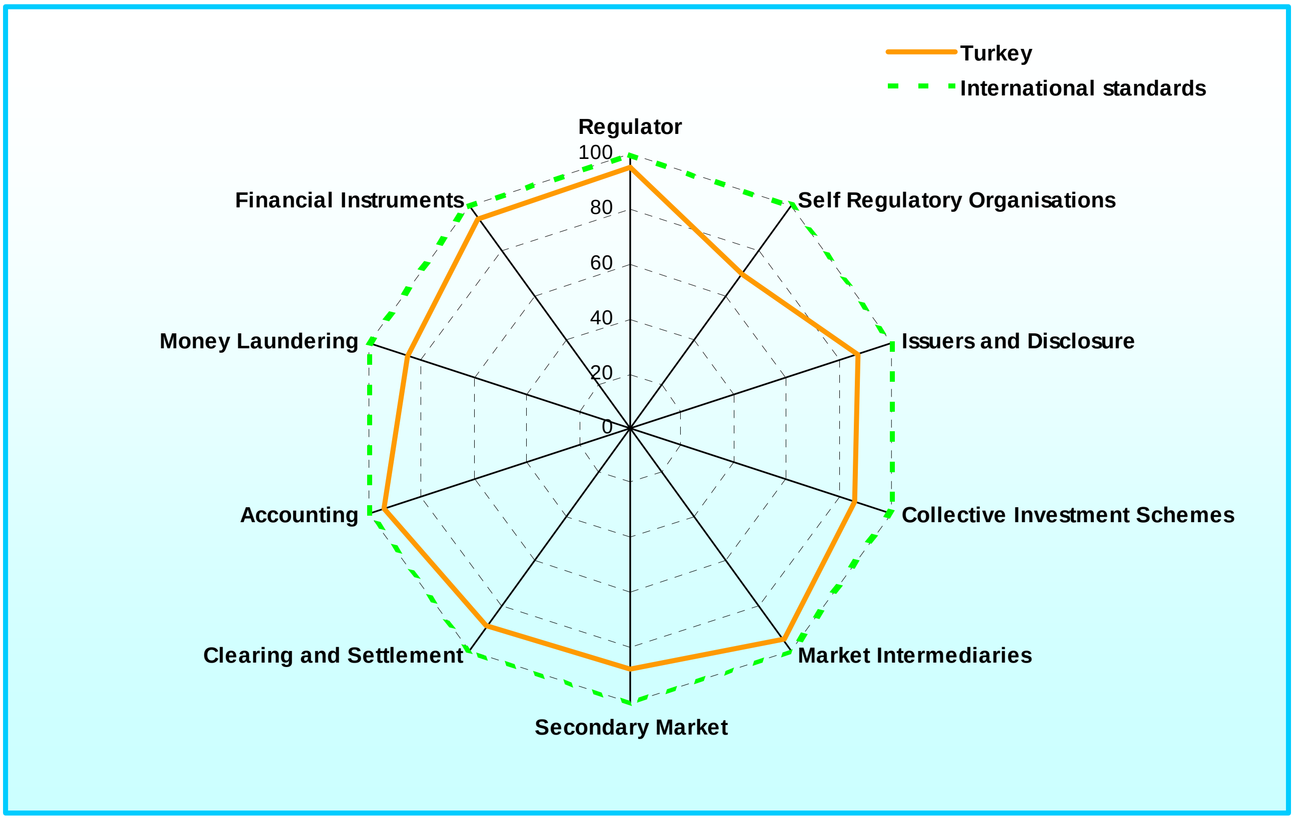
Chart 11 – Quality of securities market legislation in the EBRD countries of operations



***Source**: EBRD Securities Markets Sector Assessment 2007*

***Note**: The various categories represent the level of compliance of a given country's legislation (the "laws on the books") with international standards such as the IOSCO Principles. The asterisk indicates in which category Turkey ranks.*

Chart 12 – Quality of securities markets legislation in Turkey (2007)



Source*: EBRD Securities Markets Sector Assessment 2007*

Note*: The extremity of each axis represents an ideal score in line with international standards such as the IOSCO Principles. The fuller the 'web,' the more closely the country's securities markets laws approximate these standards.*

3.8 Telecommunications / Electronic Communications

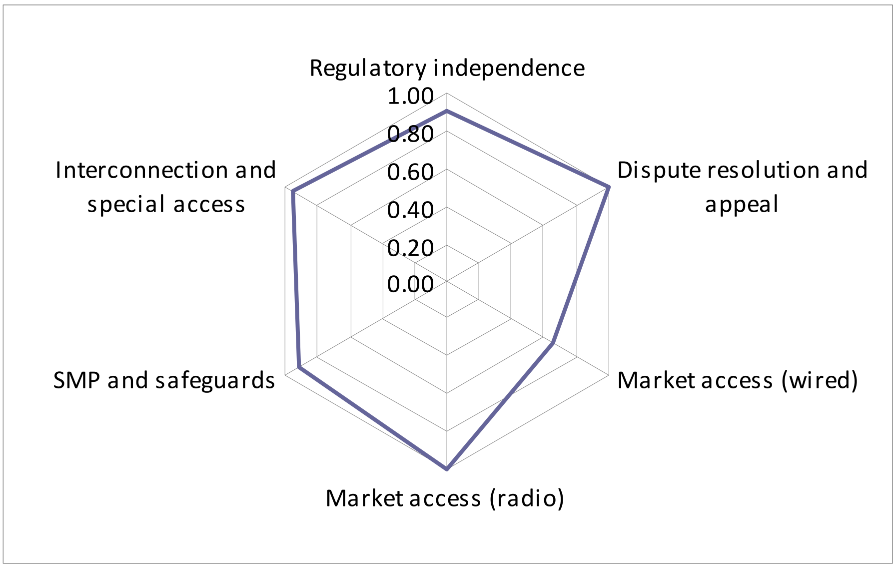
The Ministry of Transport and Communications is responsible for policy making in the electronic communications sector. Government policy is broadly one of private sector-led full liberalisation of all markets. This is a policy which, although it has filtered through into the legislative and regulatory framework, has been slow to fully implement.

The sector is governed by the Law on Electronic Communications (2008) together with supplementary subordinate legislation. The legislative framework is largely based on the 2003 European Union (EU) Electronic Communications Regulatory Framework.

While the Turkish electronic communications framework is based upon EU rules, the European Commission (EC) has expressed the view that both the primary law and implementing regulations could be better aligned with the EU *aquis*.

Comprehensive competition has been slow to take hold in the sector in Turkey, owing mainly to the fact that full voice liberalisation and introduction of 3G mobile did not occur until 2009. Now that those policies are in place the competitive market is advancing. Into the future, however, the authorities should focus on finalising and adopting primary and secondary legislative amendments, fuller alignment of the domestic framework with current EU *acquis*, particularly in the area of institutional independence of the regulatory authority, together with effective implementation of relevant competitive safeguards. The focus of the authorities should be on implementing the policy and regulatory measures which support a more rapid development of broadband infrastructure and services.

Chart 13 – Quality of telecommunications regulatory framework in Turkey (2008)

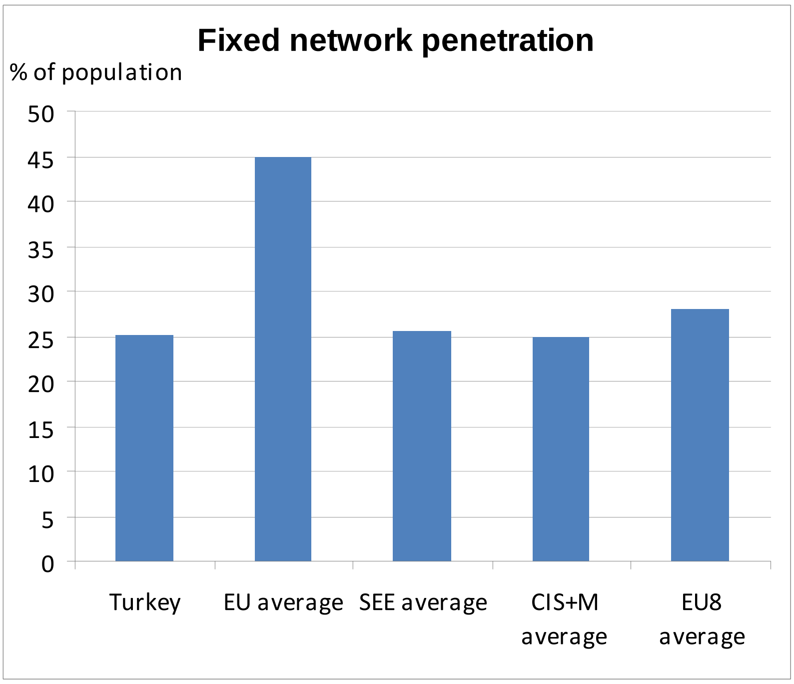


***Source**: EBRD Telecommunications Regulatory Assessment 2008*

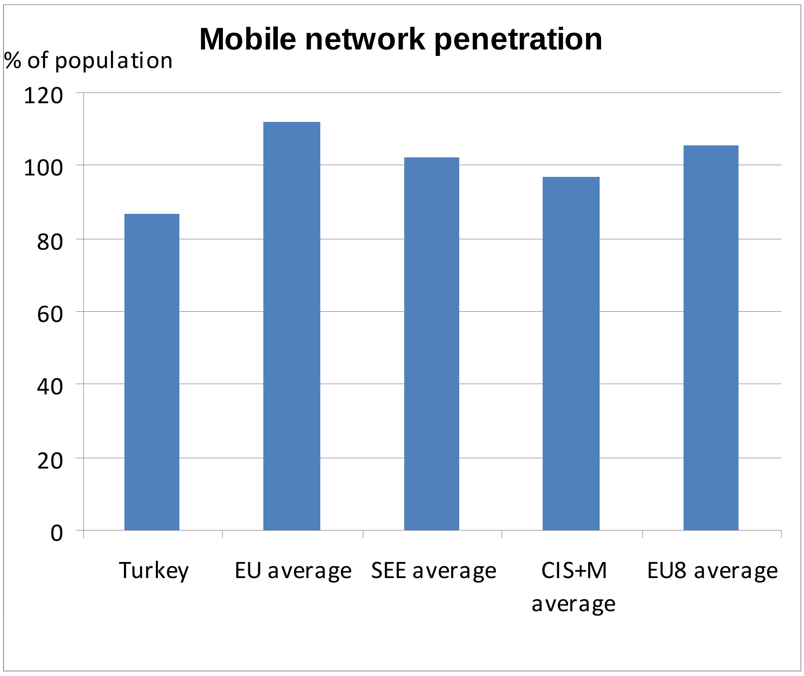
***Note**: The diagram shows the combined quality of institutional framework, market access and operational environment when benchmarked against international standards issued by the WTO and the European Union. The extremity of each axis represents an ideal score of 100 per cent, that is, full compliance with international standards. The fuller the "web", the closer the overall telecommunications regulatory framework of the country approximates these standards.*

Chart 14 – Key indicators for Turkey (2008)

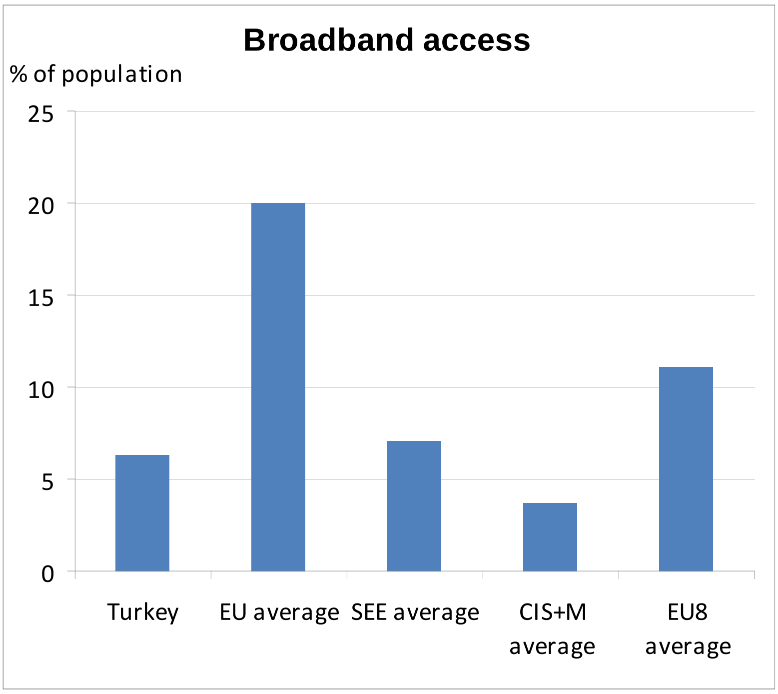
14(a) Fixed Network Penetration



14(b) Mobile Network Penetration



14(c) Broadband Network Penetration



Source: *EBRD Telecommunications Regulatory Assessment 2008*

Note: *Key indicators for Turkey provide the fixed network penetration defined as active subscriber lines as a percentage of population, mobile network penetration defined as active pre- and post-paid subscribers as a percentage of population and the broadband network penetration defined as the number of access subscribers with speeds of 144k/bits or more as a percentage of population (broadband Network Penetration less than 1% is not shown on this chart).*