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### GROUP COMPANIES CONCEPT UNDER THE NEW CODE

**R**egardless of the jurisdiction, there could be always tight, sometimes complicated and fictitious relationships between parent companies, their affiliates and subsidiaries. Needless to say, transparency between these companies plays a significant role for their shareholders and third parties who have business relations with such companies and in some cases even for subject company's directors. Unlike many EU members and certain developing countries such as Brazil and Thailand, the Turkish Commercial Code No: 6762 (the "Code"), which is currently in effect, does not regulate these relations in detail which causes various problems and misunderstandings in commercial life.

The New Turkish Commercial Code numbered 6102 (the "New Code") which is to become effective as of 1 July 2012 aims to fill this gap and provide harmonization with corporate governance and transparency principles set forth under the New Code and EU legislation. General approach preferred in the New Code is the creation of a deep transparency. Accordingly, a totally new and

remarkable section namely "Group Companies" has been included in the New Code between articles numbered 195 and 209. The concept of Group Companies, in other words, the relations between parent companies and their affiliates which are under the roof of the same management, has been introduced to Turkish legal market for the first time.



This article has been prepared in an effort to present the main concepts along with the principles and procedures that will be applied to Group Companies under the New Code.

### Key Elements of Group Companies

**T**he New Code sets forth the main elements of the Group Companies and enumerates fundamental instruments of control. As new key expressions of Group Companies, the concepts of "Dominant Company", which sustains control, and "Dependent Company", which is under the control of the Dominant Company, have been clearly regulated and the legal status of these companies and their relationships have been explained in detail

Under the New Code, the domination concept is explicitly detailed so as to enable the determination of whether Group Companies is established and being subject to the principles envisaged for the members of the Group. Domination over a Dependent Company by a Dominant Company may arise either by using the power *de facto* over the bodies of the Dependent Company or by affecting such bodies and management indirectly. As emphasized, the New Code regulates the principles and domination statuses related to Group Companies by taking into account the "control" criteria.

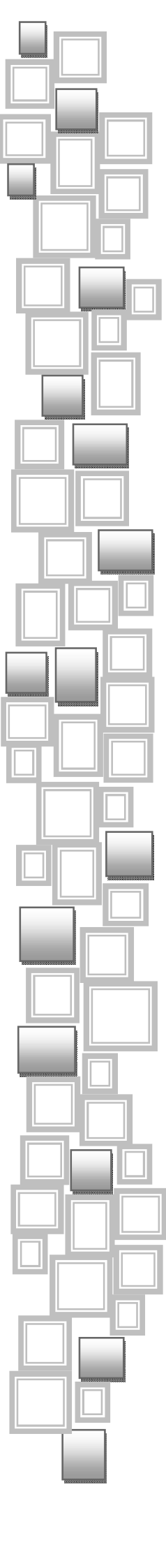
As per the New Code, domination may be established either by way of shareholding, domination agreements or other means. Accordingly, if a commercial company

(*ticaret şirketi*) has (i) the majority of voting rights of a commercial company either through ownership of shares or an agreement; or (ii) the right to appoint the majority of a commercial company's board of directors; or (iii) the majority of the share capital of the commercial company, then it is accepted that there is a dominant relationship;

whereby the first company is defined as the Dominant Company and the latter as the Dependent Company. However, it is worth underlining that in case it is revealed that the company under item (iii) above does not hold the control of the other company, in that case the criteria of domination is not valid

The New Code also emphasizes that, in terms of Group Companies' provisions, dominant position may be

created by domination agreements that must be registered with the trade registry and published in the trade registry gazette or shareholders agreements executed between the shareholders of dominant and dependent companies. Finally, in order to prevent any possible misunderstanding, it is indicated that domination may be provided apart from the events indicated above by other means such as mergers, acquisitions or spin-offs.



The New Code states that in addition to the above mentioned requirements, in order to apply the provisions of Group Companies under the New Code, at least one of the companies' headquarters under the umbrella of Group Companies should be in Turkey. In such case, it will not be considered whether the headquarters of the enterprise dominating the group is located abroad or in Turkey. The lawmaker has used the phrase "enterprise" on purpose by aiming to prevent the escape routes from Group Companies concept. Hence, on the top of a Group Companies there could be a non-legal entity, real person or a commercial enterprise as well.

### **Cross Shareholding in Group Companies**

Under the Code, cross shareholding between companies and consequences of such shareholding has been unclear; thus it results in the dilution of companies' share capitals and also creates doubts regarding the accuracy of their balance sheets. Through the New Code, an attempt is made to clarify this shareholding relationship and apply the provisions of Group Companies to the companies having cross shareholding under certain circumstances. As per the related provision of the New Code, companies which hold at least one fourth of each other's shares are deemed as having a cross shareholding relationship. In case one of these companies is in a dominant position over the other company, then the other shall be called as a dependent company in terms of Group Companies provisions.

On the other hand, if both of these companies are in dominant positions over each other, both of them shall be accepted as both dominant and dependent companies. With respect to such cross shareholding position, the New Code aims to restrict certain rights attached to shares of companies being subject to this type of shareholding relation. Accordingly, a company that acquired the shares of another company on purpose and so created a cross shareholding is solely allowed to exercise one fourth of the total voting and other rights attached to the acquired shares except for pre-emption rights and bonus shares. Shares subject to such limitation shall be disregarded in meeting and decision quorums. The New Code clearly underlines that in case a dependent company acquires the shares of a dominant company, regardless of the acquired shares' ratio, all rights attached to the acquired shares with the exception rights mentioned above shall freeze. Finally, if the cross shareholding enables domination over each other, there will be no such limitation.

### **Notification, Registration and Reporting Obligations**

Due to the principle of "transparency" foreseen especially for capital markets, with respect to share acquisitions and dispositions, unlike the Code, new requirements are brought by the New Code. An enterprise's direct or indirect acquisition or disposition of shares of any company's share capital shall require notification if the total number of shares held by such enterprise increases above or falls below 5%, 10%, 20%, 25%, 33%, 50%, 67% or 100% of the share capital of the target company. Required notification shall be made to the related company and other governmental entities indicated in the New Code or other codes, such as the Capital Markets Board, the Banking Regulation and Supervision Agency, the Competition Board and the Undersecretariat of Treasury within 10 days after the completion of the transaction. Additionally, directors and executives of the

above mentioned company and enterprise shall release a declaration with respect to the shareholding status of themselves, their spouses, children, children under their custody, and subsidiaries which have a 20% stake in the subject company. It is required that these declarations / notifications shall be made in writing, registered with the trade registry and published in the trade registry gazette. In case required parties fail to make the notification or registration, all rights attached to the related shares, including voting rights, cannot be exercised.

The New Code also introduces new reporting obligations for both the Dependent Company and the Dominant Company. Accordingly, the board of directors of the Dependent Company shall prepare a report within the first quarter of each fiscal year indicating all legal transactions conducted with the Dominant Company and precautions taken or should have been taken in the previous fiscal year. Also, directors of the Dominant Company may require from the chairman a report regarding the financial status, assets and other relevant information of Dependent Companies.

### **Liabilities Arisen From Domination**

It is obvious that domination does not give the right to abuse this power against Dependent Companies unlawfully. As a totally new concept under Turkish law, the New Code holds the Dominant Company liable for (i) its management; (ii) major resolutions taken by the company; and (iii) trust created among the public.

According to the New Code, a Dominant Company cannot use its dominant position in a way to that causes a loss which is defined as a decrease in and jeopardy of assets of the Dependent Company and which is caused due to the failure to comply with duty of care of Dominant Company. Certain transactions that may cause loss for the Dependent Company are listed not as *numerus clauses* under the New Code. In case the Dominant Company does not compensate the Dependent Company or give an equivalent undertaking regarding the loss within the relevant fiscal year, shareholders and creditors of Dependent Company may claim the compensation from the Dominant Company and its directors. A Judge, upon a claim or at his own discretion, may require the Dominant Company to purchase the plaintiff shareholders' shares or decide on another fair solution.

Shareholders of the Dominant Company who are against the major resolutions listed in the New Code resulting in a loss for the Dependent Company have the right to claim either the compensation of such loss or the purchase of their shares by the Dominant Company.

### **Conclusion**

A specific company, that is under the full control of another company, must be able to act independently and in line with its own free will, so that it can protect the rights and interests of its directors, minority shareholders and creditors. The regulations that have been introduced under the New Code are clearly for this purpose. Whether these new regulations will be able to fulfill their purpose will be seen with time.