

Turkey Adopted a New Commercial Pledge Regime for Movable Assets

Introduction

The Law No. 6750 “Law on Pledge over Movable Assets in Commercial Transactions” which annulled and replaced the Law No. 1447 “Commercial Enterprise Pledge Law” has been entered into force on January 1, 2017 together with a series of secondary regulation. The new law introduces a centralised registry for movable collateral and allows for non-possessory pledge over a wide spectrum of movable properties.

Better Access to Financing

As is the case for most of the developing economies, the capital stock of businesses in Turkey is typically in movable assets. The ability to use movable assets as collateral is therefore highly important for improving access to credit. In line with this rationale, the purpose of the law is to facilitate the access to sources of financing, especially for SMEs which are often the primary generators of new jobs and make a substantial contribution to the economic growth of Turkey, by way of increasing the use of pledge over movable assets.

The new law aims to make pledges over movable assets more flexible and easier to use by:

- i. eliminating the transfer of possession requirement

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- ii. enabling the establishment of a pledge over any piece of movable assets rather than the entire assets of the enterprise, and
- iii. providing alternative ways to foreclosure

Centralised Registry

Commercial pledge agreements used to be registered at local trade registries. However, third parties had no right to view the details of such agreements.

The new law provided for the establishment of the Movable Asset Pledge Registry, abbreviated in Turkish as “*TARES*”, a nationwide electronic platform in which pledge agreements, as well as information about pledged assets, are recorded, kept and are open to public access.

Parties to a Pledge Agreement

A wide range of businesses can pledge their assets if the underlying loan is extended by a financial institution. In addition, a pledge agreement may be executed among merchants and/or craftsmen.

Potential parties to a pledge agreement for all scenarios are shown in the table below:

PLEDGEE	PLEDGOR
❖ Financial Institution	❖ Merchant ❖ Craftsman ❖ Farmer ❖ Producer Organisation ❖ Self-employed person or entity
❖ Merchant	❖ Merchant ❖ Craftsman
❖ Craftsman	❖ Merchant ❖ Craftsman

A pledgor granting a pledge need not to be the debtor of the loan agreement, instead he can be a third party providing the pledge for the debt of another debtor.

Form of Agreement and Perfection

Basically, the pledge agreement can be concluded in two ways:

- i. It can be executed electronically over TARES with secure electronic signatures of the parties, or
- ii. It can be executed before a notary public, who is also the competent authority for registration over TARES.

The pledge will only be deemed perfected once it is registered with TARES. In other words, the pledge will only be effective against third parties as of the date of registration.

Pledgeable Assets

The new law broadens the scope of assets which may be subject to a pledge agreement. Pledgeable assets notably include, intellectual property rights, private licenses, any type of revenue and receivables, rental and other tenancy rights, bearer plants, agricultural products, animals, stocks, raw materials, consumable materials, commercial title and trade names, commercial enterprises, etc.

Unlike the former law, it is now possible to pledge the prospective assets of the enterprise. In such case, the pledgor may only enjoy other disposition rights once he acquires the ownership of such assets.

However, the new law is not applicable to pledges regarding capital markets instruments, derivate products, bank deposits and movable assets registered with a land registry for whatever reason.

Pledge Value

A pledge may be created both for specified and unspecified loans. Where the loan amount is specified, the security may only cover assets worth up to %120 of the loan amount.

In addition, the pledge value can now be denominated in a foreign currency, which was not permitted in the era of the former law.

Multiple Pledges

It is possible to establish more than one pledge over the same movable asset. The new law introduced an optional degree system to determine the priority amongst pledges.

If, in the establishment of the very first pledge, parties do not opt for a degree system, the priority of the pledges is determined according to the date of registration of the pledge. In such case, subsequent pledges automatically move forward to a higher degree when a prior-degree pledge is released.

On the other hand, the degree system creates fixed degrees so that a degree cannot be taken over by a lower-degreed pledge once the concerning pledge is released. In such case, the priority of a pledge is principally determined by its degree. Thus, a subsequently-established pledge may have priority over a previously-established pledge if it is placed in a higher degree.

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Rights and Obligations

The Law requires the possessor of the pledged assets, be it the pledgor or a third person, to take necessary precautions to maintain the value of pledged assets. The pledgee has the right to inspect the condition of the pledged assets.

In case the acts of the possessor impair the value of the pledged assets, the pledgee has the right to apply to the court to request for prohibition of the possessor from conducting such acts which lead to the depreciation of the collateral. Besides, in emergency situations, the pledgee himself is entitled to take the necessary measures without applying to the court. The pledgee may then claim compensation for expenses he incurred to take those precautions as well as the damages arising from the depreciation.

Negative pledge clauses prohibiting the pledgor from creating subsequent pledges over the relevant movable assets as well as provisions restricting the pledgor's disposal rights over the pledged assets are deemed to be null and void as per the law. However in

return, the law requires pledgors to register any transfer of the pledged assets with TARES so that the pledged assets are trackable for the pledgee.

Valuation

Prior to registration of the pledge, the parties may determine the value of the movable asset by mutual agreement or request a valuation from court. In the event of default, the pledgee is required apply to the court for valuation of the pledged asset.

The valuation will be made by experts appointed by the relevant court within three days following the application by the pledgee. In case one of the parties objects to the valuation, the court will request a new valuation and the new valuation will be final and binding for two years.

Remedies in an Event of Default

5 The pledgee is furnished with a variety of remedies to recover the overdue debt when the pledgor is in default.

First, the pledgee may take over the ownership of the pledged assets through an execution order, provided that he is the first-degree pledgee. In such case, if the amount of the satisfied debt is lower than the value of the transferred asset, the first-degree pledgee, along with the pledgor, shall be jointly and severally liable towards lower-degreed pledgees. The scope of such liability is limited to the difference between the value of the transferred asset and the amount of the satisfied debt.

Second, the pledgee may assign its receivable to an asset management company in which case the asset management company will have the same pledge degree over the pledged asset.

Third, the pledgee may use the tenancy or licensing rights over pledged assets which are not subject to the transfer of possession.

If the pledgee cannot recover the debt owed by the pledgor through above methods, he may request the foreclosure of the pledge from the enforcement office within the framework of the general provisions of the Turkish enforcement laws.

Release of the Pledge

The pledgee must apply to the Registry for deregistration of the pledge within three business days upon full discharge of the secured debt. Otherwise, the pledgee will be subject to an administrative fine equal to 10% of the amount of the secured debt.

If the pledgee fails to apply for the release of the pledge, the pledgor may also request release of the pledge by evidencing fulfilment of its obligations.

Sanctions

The pledgor or transferee of the pledged asset may be subject to an administrative fine in an amount not exceeding half of the amount of the secured debt upon complaint by pledgee, in cases where the pledgor/transferee;

- i. uses the pledged asset contrary to the law,
- ii. does not transfer the title of the pledged asset in an event of default,
- iii. damages or harms the pledged asset with the intention to harm the creditor,
- iv. fails to notify the Registry of the transfer of the title of the pledged assets and/or the underlying debt, or
- v. perform acts to mislead the Registry.

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Tax and Charges

Registration of the pledge agreement and other transactions to be made over TARES are exempt from taxes and other charges. However, notary fees should be paid for the notarial services regarding registration, amendment or cancellation of the pledge when such transactions are made before a notary public.

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