

Discharge of Board of Directors from Liability in Joint Stock Companies

Introduction

There are two compulsory organs that must exist in a Joint Stock Company (“JSC”) according to the Turkish Commercial Code (“TCC”, Law No. 6102): The General Assembly (“GA”) and the Board of Directors (“BoD”). Since BoD is the authorized executive body with the administration and representation of the company, it has a responsibility towards the Company. Discharge of the board members from liability is a legal procedure that enables GA to release board members’ liability towards the company. In this article, the procedure and the functions of the discharge and time bar for lawsuits arising from the board members’ liability will be examined briefly.

Types and the Procedure of Discharge from Liability

Board members can be discharged from liability with an explicit GA resolution or by the approval of the balance sheet.

A. Explicit Discharge: Discharge Resolution in GA

According to Article 408 of TCC, taking a resolution concerning the discharge of board members from liability is one of the non-assignable duty and power of GA. The ordinary meetings of GA must be held at least once a year and within three months following the end

of the fiscal year. The discharge resolution can be taken both at the ordinary or extraordinary GA meetings. Pursuant to Article 409, taking a resolution to discharge from liability shall be one of the items of the agenda in GA meeting. Approval by the board members is not required for the validity of the discharge.

The discharge resolution leads to the release from liability of the members of the BoD as individuals but not BoD as an organ. Although GA agendas contain "discharge of BoD from liability" as an item, it actually means the release from liability of each board member individually. GA may release some of the board members' liability while excluding the others. Also, GA may decide to discharge the board member from liability on certain matters while considering them liable on others.

There has not been a special quorum stipulated regarding the discharge under the law. However, unless otherwise stipulated in the Articles of Association as for the special quorum, the majority of the votes present at the GA meeting shall be adequate for the resolution to be taken in respect to the discharge.

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B. Implicit Discharge: Discharge by Approval of the Balance Sheet

Implicit discharge occurs in cases where the GA resolutions are regarded as a discharge of board members from liability even though there is no item on the agenda that specifically refers to the discharge.

Pursuant to Article 424, as a general rule, along with the GA resolution regarding the approval of the balance sheet, board members are deemed to have been discharged from liabilities for the relevant fiscal year.

In fact, the resolution on the approval of the balance sheet and the resolution on the discharge are substantially different from each other. Despite the balance sheet approval by the GA, board members may not be discharged from liability if there is an annotation added to the resolution which states that the resolution does not stand for discharge of BoD. Furthermore, if essential matters are not stated properly or not stated at all, or if the balance sheet contains records that will not reflect the real situation of the company, the approval of the balance sheet does not result in discharge.

Since the approval of the balance sheet is considered as discharge from liability, there is a voting prohibition for the board members and the authorized signatories in such a decision-making process.

Voting Right of the Board Members as Shareholders

Board members cannot use voting rights arising from their shares in GA resolutions on discharge since it is considered as a conflict of interest.

Hence the approval of the balance sheet is considered as discharge from liability, there is likewise a voting prohibition for the board members in such a case.

Withdrawal of a Discharge Resolution

As a general principle, GA is entitled to alter or withdraw a resolution that has been adopted. However, the disposition power of GA should not violate the acquired rights of third parties. Since the discharge resolution grants certain rights to the board members, it is not possible to alter or withdraw the respective resolution. On the other hand, the shareholders who did not vote affirmatively have the right to file a lawsuit within six months after the resolution.

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Single Shareholder JSC

In cases where there is a JSC with a sole shareholder who also has the management authority, it is legally not possible to adopt a discharge resolution. Indeed, it would be meaningless for a sole shareholder to file a lawsuit against him/herself.

Establishment and Capital Increase in JSCs

The liability of the board members regarding the establishment and capital increase cannot be discharged unless four years have passed from the date of incorporation of the company. Upon expiration of this period, the discharge becomes valid only by the approval of GA. Furthermore, GA cannot approve the discharge if the shareholders representing one-tenth of the basic capital (and one-twentieth in public JSCs) oppose the discharge and vote against it.

Time Bar for Lawsuits Arising from Board Member's Liability

As is mentioned before, if there is a valid discharge resolution, the shareholders who approved the discharge cannot file a lawsuit against the board members. It is, nevertheless, possible for the shareholders who did not vote affirmatively to claim compensation within the six months after the resolution has been adopted.

Apart from this, in accordance with the general rule stipulated in TCC, the right to claim compensation against those responsible board members becomes time-barred after two years from the date when the plaintiff shareholder becomes aware of the damage and the liable board member causing the damage; and in any case, after five years from the date of the act that caused the damage occurred.

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