

Executive Compensation under Turkish Law

Introduction

In January 2024, the Delaware Court of Chancery held that Tesla, Inc.'s Board of Directors breached their fiduciary duties by granting a multi-billion-dollar compensation plan to Elon Musk and declared such plan void. Even though the compensation committee had diligently formulated the quite ambitious compensation plan (that required Musk to increase the market capitalization of the world's leading EV producer to 650 billion USD and satisfy other targets in revenue and EBITDA) which was approved by a majority of the disinterested stockholders, the Delaware court found that the plan was unfair based on Musk's role in the process as well as its potential value.

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This case attracts attention to the ongoing global debate surrounding executive compensation and the ever-present balancing act between rewarding performance and ensuring fairness. In this article, we will examine to what extent Turkish law addresses these concerns and regulates executive compensation within its own legal framework.

Introduction to Executive Compensation under Turkish Law

Pursuant to Article 375 of the Turkish Commercial Code No. 6102 ("TCC"), the senior level management of the company, giving instructions in relation thereto and determination of the company's management organization are among the non-transferable powers of the board of directors ("BoD"). Therefore, Turkish law explicitly recognizes that the BoD (rather than the CEO) is in charge of the senior management of a joint stock company. However, in accordance with Article 367, provided that it is expressly permitted in the articles of association, the BoD may be authorized to delegate

management, in whole or in part, to one or more of its members or to a third party in accordance with an internal directive to be issued by the BoD.

In accordance with Article 394 of the TCC, the members of the BoD may be paid meeting fees, wages, bonuses, success fees and a portion from the annual profit (*tantième*), provided that the amount is determined by the articles of association (“AoA”) or by a resolution of the general assembly (“GA”).

Under Article 408/2(b) of the TCC, the decision to determine the amount of ‘remuneration, meeting fees, bonuses and premiums’ to be paid to the members of the BoD are amongst the non-transferable duties and powers of the general assembly.

Even though Article 394 of the TCC only refers to the “members of the BoD”, it must be interpreted more broadly to include the management team of the company as well. Furthermore, while the wording of Article 394 sounds to provide a restricted list (*numerus clausus*) for permitted remuneration types, it is generally accepted in the Turkish legal doctrine that other types not mentioned in the provision may also be granted to the BoD members or executives, as is the case under German law which has heavily influenced the Turkish Commercial Code. In this parallel, Article 87/1 of the German Stock Corporation Act (*Aktiengesetz*) includes ‘incentive-based compensation promises such as subscription rights and additional benefits of any kind’.

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I. Types of Remuneration

Article 394 of the TCC refers to “meeting fees, wages, bonuses, success fees and a portion from the annual profit (i.e. *tantième* payments)”. However, even though some types of remuneration which are in use in developed economies are neither expressly recognized by law nor are offered to the management teams in practice, it does not necessarily mean that such remuneration types are not permitted under Turkish law.

In this article, we will only explain the types of remuneration that are expressly stated in Article 394.

Meeting Fees

Meeting fees (or meeting attendance fees) are paid to the members of the BoD for each meeting they attend. The amount of the fee to

be paid for attending each meeting is determined either by the AoA or the resolution of the GA. The rationale behind the idea of paying meeting fees to the members of the BoD is to incentivize them to attend the board meetings and be an active member of the company management.

Other than the meeting fees, the members of the BoD may also claim the expenses (such as travel, accommodation, etc.) they incur in order to attend the board meetings.

Wages

In practice, the professional executives of the Turkish companies are usually offered wages and bonuses in order to incentivize them to increase the performance of their companies. Other options are rarely used for this purpose in the current practice.

As mentioned above, Article 394 of the TCC refers to wages as well as meeting fees, bonuses and *tantième* payments separately. However, under Turkish tax law, all benefits with a monetary value, i.e. *tantième* payments, bonuses, and all other kinds of monies and financial benefits, received from the company are included within the scope of wages.

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The wages for the members of the BoD and the executives are determined either by the AoA or a resolution of the GA. Wages can be disbursed on a weekly, monthly, yearly or per accounting period basis.

Bonuses

Bonuses are paid to the members of the BoD and executives as a financial benefit for fulfilling their management roles and achievements and further to stimulate their interest in the company's business. A GA resolution is required for the payment of bonuses.

Under Turkish law, GA has full discretion for taking a resolution to pay or not to pay bonuses to the members of the BoD and executives of the company. The GA may refrain from adopting a resolution to pay bonuses to the executives even if have they have contributed to the company's profitability.

Tantième Payments

Under both Article 339/2(f) of the TCC and Article 19/5 of the Capital Market Law No. 6362 (“CML”), in order to make *tantième* payments to the members of the BoD (and executives), the AoA must include a provision in that regard.

Under Article 19/2 of the CML, unless allocations are made for contingency reserves and the dividends, no resolution can be taken to make *tantième* payments to the members of the BoD and the employees of the company. In the same parallel, in accordance with Article 511 of the TCC, the *tantième* payments may be made only out of the net profit and after making certain allocations for legal reserves and distributing dividends to the shareholders at the rate of 5% of the paid-in capital or at a higher rate if stipulated so in the AoA.

The amount of *tantième* payments should be determined on the basis of personal contribution and services as well as the economic situation and profitability of the company. *Tantième* payments may be made in cash or in stocks by issuing new shares via increasing the capital of the company.

Under Article 512/1, if *tantième* payments were made in bad faith and without justifiable grounds, the members of the BoD (and executives) are obliged to return them. The time bar for demanding the return of such unjust payments is 5 years (Article 512/2).

Finally, under Article 513 of the TCC, in case the company is declared bankrupt, the members of the BoD (and executives) are obliged to return any monies received in return for their services in the last three years prior to the opening of the bankruptcy as *tantième* payments or under any other name, which exceed the appropriate remuneration and should not have been paid if the balance sheet had been prudently drawn up.

Success Fees

Success fees are, in principle, paid to some of the executives for their extraordinary efforts and achievements and not all the members of BoD or the whole executive team. The rationale behind is to reward the higher performers and motivate the other members to follow them.

Success fees are resolved to be paid only upon specific achievements and not in regular intervals.

II. Corporate Governance Rules on Executive Compensation

Apart from the abovementioned regulations and in parallel to the regulatory developments in the US and the EU Member States, the Turkish regulatory bodies have taken a number of steps in relation to the corporate governance rules. The main aim of these steps is to deal with the agency problem and apply certain principles to ensure that minority stakeholders are informed and represented effectively and fairly in the company management.

The Capital Markets Board of Türkiye, which was empowered by Article 1529 of the TCC to regulate corporate governance rules, issued the Communiqué on Corporate Governance (Series II, No. 17.1) in 2014 (which was amended in 2020). The scope of the Communiqué is, in essence, limited to publicly traded companies.

In summary, it regulates reporting requirements (“comply or explain”), sustainability principles (introduced by the amendment in 2020), related party transactions, mandatory establishment of an internal “Investor Relations Department”, the conditions for granting collateral and guarantees. It also introduces detailed rules related to the right to information and inspection, announcement of and attendance and voting rights in the general assembly, minority rights, dividend rights, transfer of shares, public disclosure and transparency, annual reports, company policy for stakeholders, human resources, code of ethics and social responsibility. It further regulates how the BoD is structured and works, audit committee, corporate governance committee, risk management committee, compensation committee, financial rights granted to the management team, etc.

Article 4.6 of the Principles of Corporate Governance which is annexed to the Communiqué (titled “Financial Benefits granted to Board Members and Executives with Administrative Responsibility”) provides that the BoD is responsible for achieving the company’s operational and financial performance targets that are set and disclosed to the public. A self-performance assessment based on the targets is conducted by the BoD and the BoD members and executives are rewarded or dismissed based on these assessments. Furthermore, the principles of remuneration of the BoD members

and executives have to be documented in writing and submitted to the shareholders as a separate item on the agenda of the general assembly, thereby allowing them to express their opinions. The remuneration policy prepared for this purpose must be made available on the corporate website of the company. Remuneration and all other benefits provided to BoD members and executives must be disclosed to the public through the annual reports. Disclosure on an individual basis is essential.

Conclusion

Under Turkish law, the financial rights granted to the members of the BoD and executives must be regulated in the AoA or resolved by the GA. In this way, exorbitant payments to BoD members and executives and, hence, agency problem are eliminated to the maximum extent possible, while on the other hand, higher performance of the BoD members and executives are aimed to be achieved through AoA provisions or GA resolutions.

The GA resolutions as well as the details for the executive compensation must be carefully and diligently structured in order to be prepared against legal challenges by the minority shareholders who have voted against the payment of such remuneration in the GA meeting.

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