

10 May 2007

Screening report

Turkey

Chapter 6 – Company Law

Date of screening meetings:

Explanatory meeting: 21 June 2006

Bilateral meeting: 20 July 2006

I. CHAPTER CONTENT

The chapter includes harmonised rules in the field of company law, including financial reporting requirements, intended to facilitate the exercise of the right of establishment.

In the field of **company law**, the first company law directive includes safeguards providing for mandatory disclosure requirements, limiting the grounds for invalidity of the obligations entered into by companies, as well as limiting the grounds for nullity of public and private limited liability companies. The eleventh company law directive similarly provides for disclosure requirements in respect of branches. The second company law directive contains rules on the formation of public limited liability companies and the maintenance and alteration of their capital.

The third and sixth company law directives harmonise national rules for the protection of shareholders and of creditors in the context of domestic mergers and divisions of public limited liability companies. The tenth company law directive provides for rules and procedures to facilitate cross-border mergers of public and private limited liability companies. The thirteenth company law directive on takeover bids lays down harmonised rules to facilitate cross-border takeovers within the EU, as well as improving transparency and protecting minority shareholders in the context of such takeovers.

The *acquis* also provides for certain European legal forms, in particular the European Economic Interest Group (EEIG) and the European Company (*Societas Europaea* or SE), while leaving several aspects of their internal structure and operation to be regulated through the domestic law of Member States. The twelfth company law directive requires Member States to ensure that their domestic law recognises single-member limited liability companies.

Two Commission recommendations address corporate governance principles about the remuneration of directors and about the independence of directors and committees of the supervisory board.

In the field of **accounting and auditing**, the *acquis* includes valuation rules and layouts for balance sheets and profit & loss accounts for annual (fourth company law directive) and consolidated (seventh company law directive) accounts of public and private limited liability companies. These directives also set-out audit requirements, as well as disclosure and publication obligations. In addition, a Regulation requires Community companies listed on a regulated market to draw-up their consolidated accounts in accordance with international accounting standards endorsed by the European Commission. Member States may extend the application of such international accounting standards to the consolidated accounts of non-listed companies and to annual accounts. Finally, the recently adopted eighth company law directive harmonises rules including *inter alia* the approval and registration of statutory auditors, external quality assurance, public oversight, auditor independence and the possible application of international standards of audit. Two Commission recommendations set out minimum standards for audit quality assurance and auditor independence.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the information provided by Turkey and the discussion at the screening meeting. Turkey indicated that it can accept the *acquis* regarding company law. Turkey indicated that it does not expect any difficulties to implement the *acquis* by accession.

II.a. Company law

Company Law in Turkey is governed primarily by the Turkish Commercial Code (TCC) of 29.6.1956, as last amended by Law No. 5274 of 9.12.2004. A new Turkish Commercial Code has been drafted (draft TCC) and is currently under review in the Turkish Grand National Assembly.

Turkish company law recognises the following main types of business entities:

- companies of persons: general partnerships, limited partnerships and co-operative societies;
- companies of capital: public and private limited liability companies

Private limited liability companies are known as *Limited Sirket* and do not have a board structure. Public limited liability companies are known as *Anonim Sirket* and have a unitary board structure. In addition, the Capital Markets Law (CML) foresees the concept of a publicly-held joint-stock company, i.e. those that are listed or that have more than 250 shareholders. These companies are subject to specific or additional requirements which are described below. However, certain provisions of the CML, notably those concerning financial reporting, do not apply to banks and insurance companies (they are regulated by the relevant sectoral acts).

There are no comprehensive statistics about the overall number of companies that exist in Turkey. The CMB reports that there are 604 publicly-held companies, of which 316 are traded on the Istanbul Stock Exchange.

Regarding **disclosure requirements, validity of obligations and grounds for nullity**, three pieces of related legislation are in place: the Turkish Commercial Code (TCC) No.6762, the Law on Foreign Companies with Limited Shares and Foreign Insurance Companies No.974 and the Regulation on the Commercial Registry.

The scope of these regulations is to ensure the protection of third party's interests by requiring the registration and disclosure of basic company documents and information. The procedure for company establishment requires registration in commercial registries located in the Chambers of Commerce and Industry. There are 238 local commercial registries throughout Turkey. Each company has a special file with a unique number in each register.

The commercial registry is open to the public. All persons may examine the contents of the commercial register and all documents and certificates kept in the registry office, and demand certified copies. Although some registries have electronic files, most of the registries in Turkey keep the records in paper form. Online registration and online public access to the documents and information in the registries are not available. There is currently no general requirement for Turkish companies to disclose their financial reports.

The Turkish Commercial Code (TCC) does not regulate grounds for nullity of companies. Regarding the rules for the validity of obligations, the TCC distinguishes two cases. In the first instance, persons who took part in the formation of the company are liable against third parties, if the company does not accept the obligations arising from the action carried out in the name of the company, within 3 months after the establishment. In the second instance, after the establishment of the company, authorised representatives have the right to conduct transactions on behalf of the company and to use the name of the company. Violation of the Articles of Association and the decisions of general assembly by the authorised

representative does not affect the responsibilities of the company to third parties.

Regarding **disclosure requirements in respect of branches**, registration and disclosure requirements for the first branch of a foreign company are similar to those for the establishment of a national company: the appointment of a fully authorised representative residing in Turkey is compulsory. The requirements for the second and following branches are similar to those foreseen for the branch of a national company.

In order to open the first branch, foreign companies must apply to the Directorate-General for Domestic Trade in the Ministry of Industry and Trade to get permission. If the application is accepted, the foreign branch representative in Turkey is authorised to make transactions as stated in the Articles of Association of the company, represent the company before the courts, delegate powers to a third person when he/she temporarily leaves Turkey and appoint a representative for secondary branches. When all the requirements are met, the Ministry of Industry and Trade issues a permit for the establishment of the branch. The authorisation of the representative and the permit is published in the Commercial Registry Gazette.

Regarding the area of **single-member private limited liability company**, there is no separate regulation for this concept but the Turkish Commercial Code (TCC) No. 6762 of 29.6.1956, as last amended by Law No. 5274 of 9.12.2004, may allow *de facto* the presence of a single member private liability company. Therefore, it is defined as having less than five “real” shareholders is a ground for demanding the dissolution of the company (for both public and private limited liability companies). However, if the shareholders, creditors or the Ministry of Industry and Trade do not raise such a claim, the company may continue to exist. (Arts. 435, 504 TCC)

Regarding **capital formation, maintenance and alteration of public limited liability companies**, Turkey states that it is governed by the Turkish Commercial Code (TCC) No. 6762 of 29.6.1956, as last amended by Law No. 5274 of 9.12.2004, the Capital Market Law (CML) No. 2499 of 28.7.1981, as last amended by Law No. 4629 of 2001, the Commercial Registry Regulation (CRR) of 2.2.1957, as amended by Decision no 98/11548 of 1998, and the Communiqués of the Ministry of Industry and Trade. All companies limited by shares (public and private) are covered by these laws.

Turkey states that in terms of alignment with Articles 2, 3 of the 2nd Company law directive regarding formation of companies, Articles. 279, 300, 401 and 416 of the Turkish Commercial Code (TCC) provide for the minimum content of the company’s articles of association. These requirements are supplemented by Articles 12 of the Capital Market Law (CML) and Articles 60 and 61 of the Commercial Registry Regulation. Regarding the requirement of the 2nd Directive that liabilities incurred before formation must be regulated by the Member States, Turkey states that this has already been regulated by Art. 301 of the TCC: the company becomes a legal entity upon registration in the Commercial Registry, persons acting on behalf of the company before registration are liable for these acts, unless such liabilities are assumed by the company within a period of three months after registration, then the liabilities become the company's sole responsibility.

The TCC regulates minimum capital requirements as companies must have a minimum share capital which has to be subscribed before a company may be incorporated. For private companies and for public companies with a basic capital system, the minimum is YTL 5,000 for limited liability companies and YTL 50,000 for companies limited by shares (appr. Euro 2,500-25,000). For public companies with an authorised capital system, the amount of the

initial capital or issued capital should be the minimum amount that is determined by the Capital Market Board (CMB). Currently this amount is approximately 3 million YTL (appr. Euro 1,5 million). The cap of authorised capital can be determined by the company and must be approved by the CMB. Shares may be issued above their nominal value (at a premium), but no shares may be issued below the nominal value.

Shares can be issued for cash or non-cash considerations. A quarter of the cash consideration must be paid within three months and the rest must be paid in three years (Communiqué of the Ministry of Industry and Trade No. 2003/3). There is no time limit for the transfer of non-cash consideration. Publicly-held companies are subject to the same system, except that shares offered to the public may only be issued for cash consideration, which must be fully paid upon purchase (Art. 7 CML). In any case, capital may be formed only of assets capable of economic assessment and may not include an undertaking to perform work or supply services. Non-cash consideration must be valued by court appointed experts. (Art. 303 TCC)

Regarding distribution to shareholders, the TCC allows dividends to be distributed from the net profit and distributable reserves. Net profit is the amount remaining after the allocation of statutory reserves and other amounts to be reserved according to the articles of association. (Arts. 469, 470 TCC). Distribution from “net profit” also means that no profit may be distributed unless previous years’ losses are covered. Moreover, no interest may be paid on capital (Art. 470 TCC). Interim interest may be paid at a fixed rate for the period of foundation of the company until the start-up date of the full operation of the business (Art. 471 TCC). The capital may not be reimbursed to the shareholders (Art.405 TCC).

The TCC does not contain an explicit prohibition of subscription of a company's own shares. However, it is generally accepted that a company may not subscribe its own shares. The acquisition by a company of its own shares is also not allowed: (Art. 329 TCC) a company may not acquire its own shares or receive them as pledge.

Turkey states that the TCC allows for increases and reductions of capital, for private and public companies but that capital may only be increased with a resolution of the general assembly. For public companies with authorised capital system, the cap of authorised capital may only be raised by a resolution of the general assembly. However, the general assembly may authorise the board of directors to increase the issued capital up to the cap of authorised capital (CML Art. 7).

For both private and public companies, reduction of the capital is only possible with a resolution of the general assembly and respecting the amount of minimum capital. Shareholders have a pre-emption right to subscribe for new capital in proportion to the capital represented by their shares. Shares issued by a capital increase through the company’s own means such as free reserves, revaluation funds, proceeds received through the sale of subsidiaries, are distributed free of charge to all shareholders in proportion to their shares. (TCC Arts. 385, 389, 394, 396)

Turkey declares that relevant legislation for the authorised capital system, is the Capital Market Law and the Capital Markets Board Communiqué Serial:IV No:7. Publicly held companies (joint stock companies whose shares have been offered to the public and/or that has more than 250 shareholders) may adopt authorised capital system, provided that they obtain the permission of the Capital Markets Board. In this system, the board of directors may increase the capital of the company by issuing new shares up to the amount of authorised capital stated in the Articles of Association without complying with the provisions of the Turkish Commercial Code concerning capital increases.

The decision on limiting the pre-emptive rights of shareholders must be announced by the companies who are subject to the authorised capital system. In case of limiting pre-emptive rights, the members of board of directors, auditors and shareholders may bring an action for annulment before the commercial court against the decisions of the board of directors in 30 days following the publication of decision. The CMB has also power to file a case for annulment against the decisions taken by the board of directors, in accordance with the principles of the Capital Market Law on authorised capital system, within 30 days.

Domestic mergers of public limited liability companies are regulated by the Turkish Commercial Code (TCC) No. 6762 of 29.6.1956 as last amended by Law No. 5274 of 9.12.2004, and the Commercial Registry Regulation of 2.2.1957 as amended by Decision No. 98/11548 of 1998, TCC. The scope of the laws include general provisions for all commercial companies (Arts. 146-151 TCC) and special provisions for companies limited by shares (Arts. 451-452 TCC)

Mergers by acquisition or mergers by formation of a new company are allowed only between commercial companies of the “same kind”. For this purpose, general and limited partnership on the one hand and the companies limited by shares and partnership limited by shares on the other hand, are considered to be the same kind. (Arts. 147, 151 TCC)

All companies limited by shares, both public and private follow special rules for annual balance sheets according to a jointly determined model which must be prepared (Art. 149 TCC) including a "Merger Balance Sheet". Share exchange ratio are determined by an independent expert appointed by the court. There are no rules on the method of valuation and determination of the share exchange ratio.

The Turkish Commercial Code does not cover rules on draft terms of a merger. According to established practice, the draft terms include the rights and obligations of the merging companies, as well as the approval of the general assembly, registration and publication of the merger decision in the commercial registry.

Turkey states that the protection of creditors system in place is one-sided protection: only the creditors of the acquired company are protected. Claims due and payable will be paid, guarantees are supplied for claims which have not become due and for disputed claims. Creditors may also accept the transferee company as the debtor and may give up their right to a guarantee. Another creditor protection is realised through the principle regarding the equities of the merged companies as separate. Equities will be managed separately until the time when it is assumed that it is possible to distribute the assets of the company limited by shares among the shareholders (Art. 451 TCC)

Domestic mergers of publicly held companies are covered by the Capital Market Law (CML) and the Capital Markets Board (CMB) Communiqué Serial:I No:31 on Principles regarding Mergers. It covers publicly held companies and mergers by acquisition of one or more companies and merger by formation of a new company. The procedure includes:

- a preliminary assessment of companies authorised bodies;
- independent auditing report;
- experts report;
- board of director’s report;
- CMB approval;

- publication of an announcement;
- general assembly approval;
- registration of securities with the CMB;
- registration of Articles of Association.

A Board of Director's Report which explains the merger contract, the conditions that affect the valuation and an independent Audit Report on the financial statements have to be prepared. A first expert report must be prepared by the experts appointed by the court. It indicates the methods used to arrive at the share exchange ratio and indicate the amount of capital after the merger. The second expert report must be prepared by independent auditing companies, consultancy firms or intermediary institutions. It indicates the method used to calculate the share exchange ratio, the opinion concerning merger ratio, the efficiency of the methods, and any special valuation difficulties.

Turkey informs that in terms of rights of shareholders of publicly held companies, access to documents is required, at least one month before the general assembly, including: the merger contract, the last three annual financial statements of the merging parties, independent auditing reports and annual reports, expert reports, the board of directors' report, announcement form as well as the last quarterly financial statements. The right to obtain copies of these documents is free of charge.

Regarding the **domestic division of public limited liability companies**, Turkey states that this area is not covered by current law as there are no provisions in the Turkish Commercial Code (TCC) No. 6762 on this. This area is governed by the Joint Communiqué of the Ministry of Finance and Ministry of Industry and Trade On the Partial Division of Companies Limited by Share and Companies with Limited Liability (Division Communiqué).

In the Division Communiqué only partial division is regulated. Division may include assets such as immovables, participations, production facilities, intellectual property. Assets may be transferred to companies as capital in kind based on their book value. The transferring company or its shareholders must be given shares in the acquiring company, cash consideration is not permitted. If shares are given to shareholders rather than the transferring company itself, the transferring company must reduce its capital. The procedure for division under the Division Communiqué requires the preparation of draft terms of division including the following information:

- interim balance sheet (maximum six months interval is allowed between the date of the balance sheet and the date of the general assembly);
- review of the balance sheet and the division, by an expert appointed by the court;
- increase and/or decrease of capital;
- approval of the division by the concerned companies;
- registration of the division in the commercial registry;
- the assets to be transferred upon registration.

In terms of protection of creditors, the Division Communiqué provides for creditors to make their claims. They can demand payment of their matured claims and a guarantee to be given for other claims. If debts are not paid, guarantees not given or approval of the creditors not obtained, the division may not be registered in the commercial registry.

The division of publicly held companies is regulated by the Capital Market Law and the

Capital Markets Board (CMB) Communiqué Serial:I No:26 on Principles regarding Registration with the Capital Markets Board and Sale of Shares. It applies to publicly held companies. Divisions covered include division by formation of a new company. In the case of the establishment of a new company (or companies) by allocating the minimum 15% of the total assets in the latest balance sheet or by terminating the legal personality of publicly held company, the shares of the new company should be registered with the CMB.

Turkey states that the division procedure is similar to the procedure for mergers, requiring independent auditing for financial statements forming the basis of the division, publication of an announcement to shareholders, registration of securities with the CMB. The CMB permits only partial division by the formation of new companies.

Regarding **cross-border mergers** of public limited liability companies, Turkey states that Directive 2005/56/EC applies to mergers of limited liability companies formed in accordance with the laws of a Member State and having their registered office, central administration or principal place of business within the Community. Therefore, the conditions for regulating cross-border mergers within the meaning of this Directive do not exist for non-member states such as Turkey.

Take-over bids are regulated by the Capital Market Law. Articles 16/A and 22/i authorise the CMB to issue secondary legislation on takeover bids. The Communiqué on Principles regarding Proxy Voting at Shareholders' Meetings of Publicly Held Companies, Proxy Solicitation and Take-over Bids (Serial IV, No 8- published in OG No:21872, 9 March 1994) (ProTo Communiqué) as well as the Communiqué on Principles regarding Public Disclosure of Material events (Serial:VIII, No:39- published OG No:25174, 20 July 2003) (disclosure Communiqué) are also applicable to this area. The scope of these regulations is the protection of minority shareholders (equal treatment of shareholders) and the dissemination of adequate, meaningful information about the offeror and the bid.

Turkey notes that the ProTo Communiqué applies to take-over bids, both voluntary and mandatory take-over bids, where the target company is a publicly held company. The procedure for voluntary take over bids requires the Offeror to submit the "Information Form" to the CMB at least 30 days before the offer. The CMB may request additional information. The information forms shall be published in at least two national journals, and also sent to shareholders to whom written offers have been made. The purchasing period is maximum 30 days. Offerors may withdraw their offer up to the beginning of the purchasing period.

Disclosure is required for the following:

- decisions about making a take-over bid by the company for the shares of another company;
- decisions taken by shareholders or third persons regarding a take-over bid for the shares of the company;
- existence of a mandatory take-over bid in accordance with the regulations of the CMB;
- application to the CMB for the grant of an exemption to make a mandatory take-over bid;
- application to the CMB to make a take-over bid.
- Results of the above applications.

The procedures for mandatory take-over bids require a person (or persons acting in concert) who has acquired, directly or indirectly, whether through take-over bid, block or individual

purchase, 25% or more of the capital of a publicly held company (or without being subject to this percentage, owning shares controlling the management of the company), to make an offer to the remaining shareholders of the target company. If a person or persons acting in concert, owning between 25% and 50% of the capital and voting rights of a publicly held company, increases this stake by 10% or more in any given 12-month period, such person or persons are also required to make an offer to the remaining shareholders of such company.

Regarding the pricing of mandatory take-over bids, the rules applicable include: the bid price offered to shareholders cannot be below the highest price paid to the targeted shares. The price offered in the mandatory bid should be equal for all holders of securities of the same class. Furthermore, when the purchase is made through a block sale, the highest price paid per share must be offered. The CMB may seek a third party appraisal report from authorised appraisal companies, where the bid price cannot be determined according to the provisions of the ProTO Communiqué. If the take-over bid is delayed by the offeror, the CMB may impose a default interest on the bid price. The bid price is only paid in cash.

Turkey states that exemptions are possible if the acquisition of shares and voting rights of the company that triggered mandatory take-over bids is necessary for the strengthening of the financial structure of the company, or is approved at a general assembly of the company in accordance with Article 388 of Turkish Commercial Code (66,6% of all outstanding shares). Additional exemptions include cases where it would not cause any change in the control of the company's management due to capital distribution or is realised as result of a privatisation process.

The CMB may grant exemption from mandatory take-over bids. The CMB may grant exemptions from the mandatory take-over bids only if the applications for exemptions shall be made within 5 days following the mandatory take-over bid requirement.

In terms of sanctions, the CMB is entitled to impose fines on those who fail to comply with rules laid down in the Communiqué. A party, who suffers as a result of violation of the mandatory bid rules, may bring an action for damages or for action against the offeror, under civil law.

There is no provision equivalent to the **Statute for a European Company** (Societas Europaea or SE) in Turkish law. Turkey notes that according to Art. 2 of the Regulation (EC) No. 2157/2001, the SE Regulation shall become directly applicable in Turkish law upon accession. For these reasons, the SE has not been dealt with in the Turkish Commercial Code.

There is no provision equivalent to the **European Economic Interest Group** (EEIG) in Turkish law. Turkey indicates that the EEIG Regulation shall become directly applicable in Turkish law upon accession. For this reason, the EEIG has not been dealt with in the draft Turkish Commercial Code.

Turkey states that **remuneration of directors and the independence of directors and the committees of the supervisory board**, are covered by the Turkish Commercial Code and by the Corporate Governance Principles issued by the CMB in 2003. The Turkish Commercial Code requires that the Articles of Association of the company shall contain the following details (Article 279):

- Special advantages to be granted to the founders, directors and other persons out of the profits of the company

- The method of choosing the person to be entrusted with the administration and the control of the business of the company, their rights and duties
- Fees and allocations of the directors are decided in annual general assembly, if not already provided by the Articles of Association (Article 369).

In 2003, the CMB issued Corporate governance principles for publicly held companies covering shareholders, disclosure and transparency, stakeholders and board matters. A Corporate governance compliance report needs to be included in the annual reports of listed companies, as a separate section. It explains the CMB Corporate Governance Principles that are adopted, reasons for not applying the principles, and conflicts of interest resulting from not wholly adopting these principles.

In the “Board of Directors” section of the Compliance Report, the following are disclosed by listed companies: all rights, compensations and wages granted to the members of the board and the criteria used to determine them, whether the remuneration is determined according to the performance of the board of directors and the company, whether the company lends money to any member of the board and to managers and its grounds for the conflicts of interest.

Turkey informs that in terms of the Commission recommendation on non-executive Directors and board committees, the relevant legislation in place includes the CMB Communiqué series X, No:22 on Auditing Standards in Capital Markets as well as the Corporate Governance Principles issued by CMB in 2003.

The Communiqué determines that it is compulsory for listed companies to establish an audit committee, composed of at least 2 board members with the majority as non-executive members.

Regarding the formation and election of the board of directors, it must include independent members. Several committees must be established by the board, the Corporate Governance Committee and Audit Committee. Independent Board Members must have no direct or indirect relationship with the company, its subsidiaries or any other group companies, nor receive any compensation other than the board membership compensation and attendance fee.

In the Corporate governance compliance Report, the following information is disclosed by listed companies:

- structure and composition of board of directors and independent members;
- qualifications of board members;
- mission, vision and strategic targets of the company;
- internal control and risk management mechanism;
- authority and responsibility of the members of the board and executives;
- number, structure and independency of the committees established by the board of directors;
- remuneration of the board of directors.

II.b. Corporate accounting and auditing

The Turkish delegation acknowledged that the current legal framework on accounting and auditing mostly do not reflect internationally-accepted practices and that there are inadequate sanctions for non-compliance. The majority of Turkish companies are currently required to

draw-up their accounts on the basis of the Tax Procedural Law and related implementing regulations. Similarly, most companies – other than publicly-held companies and regulated financial institutions – are only subject to a tax audit which differs in fundamental ways from a statutory audit as defined in the *acquis*.

Turkey states that **annual accounts** are governed by fragmented standards derived from multiple regulations, including the Turkish Commercial Code, the Tax Procedures Law, the Capital Market Law, Banking Law and Insurance Law. Responsible bodies are also fragmented, including the Ministry of Industry and Trade, Ministry of Finance, Capital Markets Board, the Banking Regulation and Supervision Board as well as the Under-secretariat of the Treasury. For annual accounts, the main rules cover content and formats, notes to Financial Statements, layouts and valuation, inflation accounting, publication and audit Requirements

Consolidated accounts of groups of companies are regulated by the Capital Market Law and by the Banking Law (for detailed presentation of these laws, see the screening report for Chapter 9 - Financial Services). . With the exception of companies falling within the scope of these laws, there is currently no requirement for Turkish companies to prepare consolidated accounts. At the time of the screening meeting, banks were not required to include non-financial subsidiaries in their consolidated accounts.¹

In terms of **international accounting standards**, the Turkish Accounting Standards Board (TASB) sets uniform national accounting standards compatible with IFRS. It is a public legal entity with administrative and financial autonomy and an official relationship with the International Accounting Standards Board (IASB). Publicly-held companies are required to prepare their consolidated financial statements in accordance with the Communiqué (Serial XI, No. 25) which Turkey claims is to be in compliance with IFRS, in particular "TMS 27 Consolidated and Separate Financial Statements", which the Turkish Accounting Standards Board published in the Official Gazette on December 2005, is purported to be fully compatible with IAS 27.

The TASB is made up of nine members from various ministries including the Ministry of Finance and representatives from the Capital Markets Board, Banking Regulation and Supervision Board, the Union of Chambers and Commodity Exchanges of Turkey (TOBB) as well as the professional organization of accountants. The TASB established working groups of accountants and auditors which issue opinions on draft standards. So far, 36 IAS/IFRS have been adopted. In July 2006, IAS 32, IAS 39 and IFRS 7 were adopted. The TASB has also created a working group to address the issue of simplified accounting standards for SMEs.

Regarding **statutory audits**, Turkey reports that fragmented standards from multiple authorities are in place, including from the Ministry of Industry and Trade, the Ministry of Finance, the Capital Markets Board, the Banking Regulation and Supervision Board and the Under-secretariat of the Treasury.

The existing Turkish Commercial Code requires that public limited companies appoint an "auditor", while private limited liability companies must appoint an auditor if they have more than 20 shareholders.

1 A new BRSA regulation adopted in November 2006 does not appear to have fundamentally changed this situation.

The Law No. 3568 on Independent Accountancy, Independent Accountant Financial Advisory and Sworn Financial Advisory (1989) defines 3 categories in the audit profession: an Independent Accountant (Bookkeeping), an Independent Accountant and Financial adviser (bookkeeping and tax services) and a sworn Financial advisor (can perform tax audit). The audits performed by Sworn Financial Advisors are based on Tax Regulations.

The Turkish delegation noted that the auditors and the audit as required in the Turkish Commercial Code, do not conform to internationally-accepted audit practices and that there are inadequate sanctions for non-compliance.

Specific auditing requirements exist in relation to publicly-held companies and regulated financial institutions, including banks and insurance companies.

According to Article 39 of the Banking Act No.5411, the annual financial reports/financial statements to be presented by banks have to be approved by independent audit firms authorised by the BRSA Board. Consolidated and non-consolidated financial statements of banks are subject to independent audits on a quarterly and annual basis. There are two by-laws regarding independent audit: the by-law on Independent Audit of Banks and the by-law on Authorisation of Independent Audit Firms². Similarly, the Insurance Audit Law (No. 7397) and related implementing regulations, require that auditors of insurance companies must be approved by the Treasury.

The Capital Markets Board (CMB) regulates auditing activities and audit firms in capital markets (Communiqué Serial:X, No:16). Existing regulations have been revised after the recent accounting scandals and it provides for the separation of audit and consultancy, the establishment of audit committees for listed companies and brokerage firms, an audit firm rotation and the determination of corporate responsibility for the preparation, presentation and accuracy of financial statements and annual reports. The CMB provides oversight over audit firms, performs quality controls, evaluates complaints about audit firms and imposes sanctions. In order to perform audits in capital markets, the following are required: company limited by shares formed with registered share, university degree in related economics sciences, licensed audit professionals, adequate personnel and equipments. All applications are evaluated by the CMB.

Independent audit companies are subject to quality control inspections of the CMB regarding their reports on publicly held joint stock corporations. Inspections are conducted on a random basis or upon concerns on the quality of reports. These inspections are held by the Accounting and Auditing Standards Department of the CMB, which had a total staff of 7 in 2005 (9 in 2004). However, only 614 (2005) of around 2 048 059 (2005) companies are publicly held joint stock corporations.

In June 2006, the CMB issued the Communiqué on Independent Auditing Standards in the capital market, introducing the International Standards of Audit set by the International Federation of Accountants. The BRSA adopted implementing legislation on audit principles. The Capital Market Board (CMB) and the Banking Regulatory and Supervisory Authority (BRSA) require the accounts of, respectively, listed companies and banks to be audited. However, there is no general purpose framework consistent with internationally accepted

² In addition, a by-law on the "Authorisation and Activities of Independent Audit Firms" was adopted in November 2006. It takes into account some principles from Directive 2006/43, such as independence of auditors and audit firms, quality assurance systems, audit fees, auditors liabilities and reporting.

auditing practices and the regulatory framework for the auditing profession remains to be significantly upgraded.

Turkey states that in June 2006, international standards on auditing have been adopted for auditing of the accounts of publicly-held companies and brokerage firms subject to Capital Market Law (CML) (Communiqué Serial:X, No:22). The rotation rule for auditors/audit firms is harmonized with 8th Directive Proposal (within the maximum period of 7 years). Exam requirements are being introduced in order to close the educational knowledge gap of auditors, who are subject to CMB legislation, in international financial reporting standards and international standards on auditing. Regulations related to appointment/dismissal and penalties of auditors are updated, ethical principles are revised and the public oversight role of CMB is emphasized.

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY

Overall, Turkey's legislation has reached only a limited level of alignment to the *acquis* covered by this chapter, both for company law and for corporate financial reporting, in particular for audit. Turkey has not outlined any target dates nor plans for further approximation with the *acquis* in this chapter. A new Turkish Commercial Code is currently pending before the Turkish Grand National Assembly. Adoption of the new Code, as currently drafted, would represent a major step forward and would address many of the shortcomings identified in this report.

III.a. Company law

The existing legislation in the area of company law is aligned with the *acquis* to a limited extent. Important adjustments are required concerning the disclosure and publication of financial reports, certain provisions concerning the registration of branches of foreign companies, establishment of grounds for nullity, procedural aspects relating to domestic mergers and divisions, cross-border mergers, single member private limited liability companies, the recognition of the *Societas Europaea* and of the European Economic Interest Grouping and a number of aspects relating to takeover bids

Turkey has reached a limited level of alignment with the 1st Company Law Directive related to the **disclosure requirements, validity of obligations and grounds for nullity** of public and private limited liability companies. Disclosure requirements will need to be enhanced and a general obligation to disclose financial reports will need to be introduced. The technical infrastructure of company registers operated by the Chambers of Commerce needs strengthening to fulfil *acquis* requirements in this field, e.g. to ensure the access to company registers by electronic means. The TCC will also need amendments to cover grounds for nullity of limited liability companies. Amendments to the Turkish Commercial Code (TCC) will be necessary to reach alignment with the 11th Company Law Directive concerning **disclosure in respect of branches, *inter alia*** to repeal the obligation to appoint an authorised representative residing in Turkey. For alignment in all of the abovementioned areas, approximation plans with target dates are needed.

The Turkish Commercial Code currently does not allow **single-member private limited liability** companies and is therefore not aligned with the *acquis*.

In the area of **capital maintenance**, Turkey has reached a partial level of alignment with the 2nd Company Law directive. However, it is not aligned with the provisions of the Second

Directive regarding the acquisition by a company of its own shares, particularly in terms of disposal of the company's own shares, and will need to be amended.

Turkish legislation has reached a limited level of alignment with the 3rd Company Law Directive on **domestic mergers of public limited liability companies**. Adjustments will be necessary to address the gaps described in section II.a. Amendments to the TCC will be needed to include rules on draft terms of a merger. Further adjustments are also needed to improve the system of protection of creditors which for now only protects the creditors of the acquired company.

Turkish legislation has reached a limited level of alignment with the 6th Company Law Directive on **domestic divisions of public limited liability companies**, as the current law only foresees division by split-off.

Turkey will need to introduce provisions concerning **cross-border mergers**.

In Turkey, the Takeover Act has reached a good level of alignment with the 13th Company Law Directive on **take-over bids**. Several adjustments will be necessary to address the gaps described in section II.a.

Turkey is not expected to have any problems to allow the recognition of the **statute for a European company** in its domestic law, upon accession as well as to allow for the recognition of the **statute for a European economic interest group** in its domestic law, upon accession.

Turkish legislation and the Capital Market Board Communiqués issued in 2003 provide for most of the principles foreseen in the Commission's Recommendations concerning the **remuneration of directors** and the **independence of directors and the committees of the supervisory board**.

III.b. Corporate accounting and auditing

The legislation in the area of accounting and auditing is aligned with the *acquis* to a limited extent. Turkish legislation does not incorporate a general-purpose financial reporting framework corresponding to the *acquis* in this area. The situation is better for listed companies and regulated financial institutions, esp. banks, for which accounting and auditing requirements are to various degrees based on internationally accepted standards (IFRS and ISAs). However, the specific requirements applicable to these entities are not consistent and a number of divergences from international standards remain.

Overall, a major overhaul of the legal framework is required to introduce the concepts of the *acquis* in this area.