FEBRUARY 2019

HFW TURKEY PACK

CONTENTS

INTRODUCTION

With a population of some 80 million, abundant natural resources, well placed ports and historically high rates of growth, Turkey is an attractive market full of opportunities. Even so, it is not without its challenges: the lira has demonstrated extreme volatility over the past year, having lost almost half of its value against the dollar; the US has imposed significant tariffs on steel and aluminium (against which Turkey has retaliated with tariffs of its own); and countries such as Lebanon and Iran have introduced import bans, affecting Turkish products directly and indirectly respectively.

This pack is designed to help you, from both a legal and commercial perspective to successfully navigate these challenges, mitigate risk, and ultimately find success trading in Turkish markets.

The first section of this pack takes a sector focussed approach to the legal consequences of currency fluctuations, tariffs and import bans on commercial contracts. In particular we draw on HFW's sector expertise, and consider commodities, voyage charters, derivatives, construction, aviation, and ports and terminal investments.

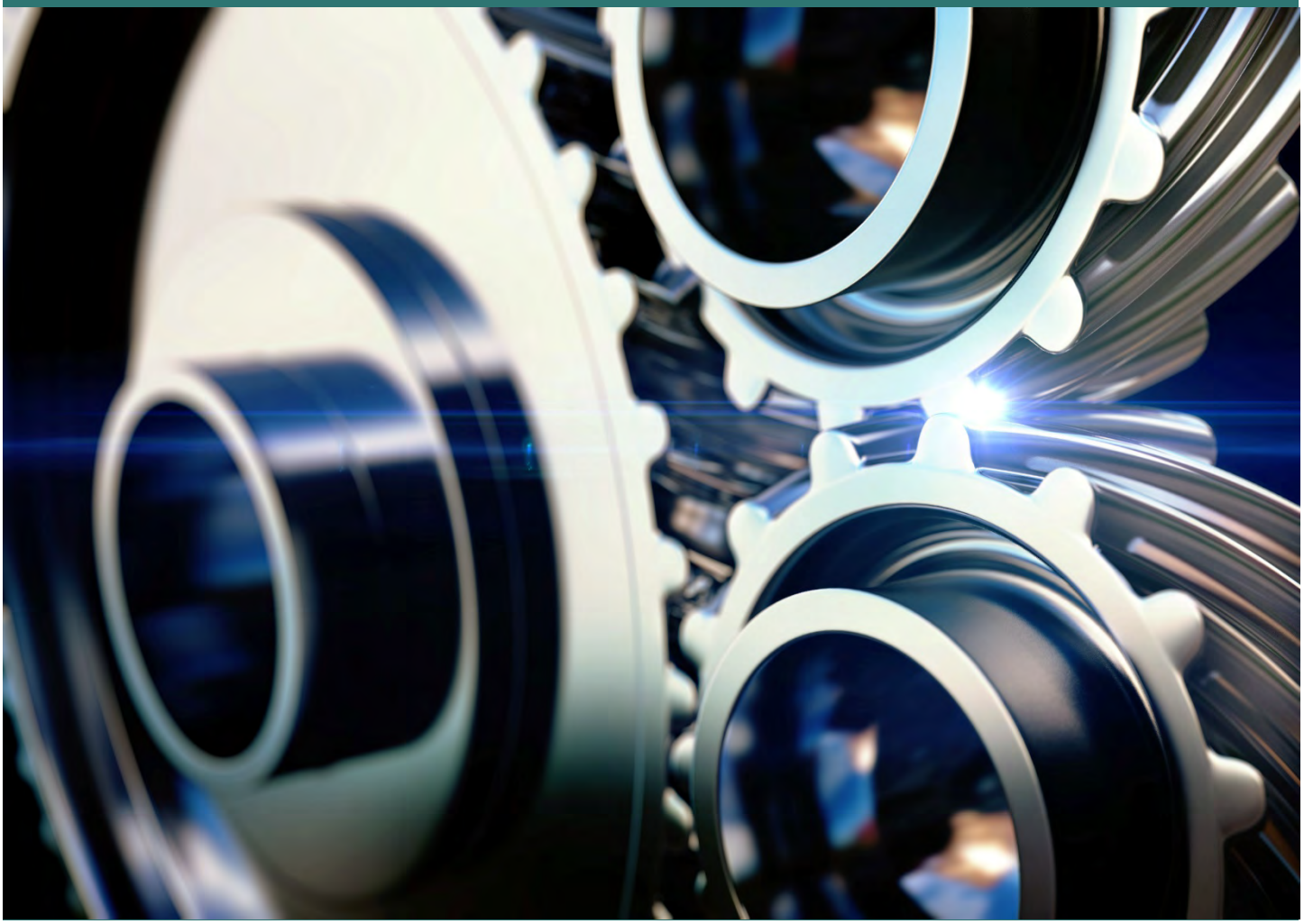
The second section provides detail on ways you can mitigate risk in Turkey. We consider the available means of security in Turkey, and how you can ensure any security obtained is legally effective. A number of commercial considerations are also considered in respect of obtaining guarantees from Turkish counterparties.

Finally, we turn to your options in case something does go wrong. We provide a detailed overview of the mechanisms for enforcing English court judgments and arbitral awards in Turkey, and Turkish judgments and awards in England.

HFW has extensive experience in advising both Turkish commercial operators trading globally, and global operators trading in Turkey. Should you require further advice or detail on any of the contents of this pack, then do not hesitate to contact any of the contributors listed at the end of the pack. We are grateful to our longstanding partners, Inal Law for their contributions at pages 16-22, and 29-31 on Turkish law in this pack.

01

KEY LEGAL ISSUES: SECTOR FOCUS



COMMODITY CONTRACTS: FRUSTRATION

English Law

Under English law, a contract may be discharged by frustration when circumstances arise after the conclusion of the contract that render the agreement impossible, illegal or commercially pointless. Given the recent economic volatility in Turkey, and the shifting landscape of tariffs and bans on Turkish imports, it is important to consider the extent to which commodities trading contracts may be frustrated.

In assessing whether there has been a frustrating event the courts generally take into account whether:

- Performance of the contract has become impossible, illegal or radically different from that initially contemplated (not merely more expensive or onerous)
- The supervening event is due to the default of either party
- The contract makes provision for the event (e.g. by means of a force majeure clause)
- (In sale of goods contracts) property has passed to the buyer, in which case the contract will not generally be frustrated

Following frustration the contract is brought to an end automatically and both parties are generally released from further performance.

A key requirement for the doctrine of frustration to apply is that performance should have been rendered impossible, and not merely more expensive or onerous. Therefore, it is highly unlikely that either the lira's recent volatility, or tariffs placed on Turkish goods could be successfully pleaded as a ground for frustration. Depreciation in the value of the contract price as a result of inflation has been held to be a risk to be borne by the seller, and not a valid basis for frustration. Further, in *British Movietonews Ltd v London and District Cinema* [1952] AC 166 at 185, Viscount Simon indicated that "*a wholly abnormal rise or fall in prices*" or "*a sudden depreciation of currency*" would not frustrate a contract.

Conversely, illegality is a well-established basis for frustration. Any subsequent change in the law that would render performance of the contract unlawful could constitute an event of frustration. Therefore, where some countries have prohibited the import of goods originating from Turkey, then affected contracts may become frustrated.

Generally, a contract subject to English law will not be frustrated by a change in a foreign law. However, there is an exception where the contract would be rendered unlawful by a change in the law of the place of performance of the contract. Where an import/export ban is introduced after the date of the contract prohibiting the contractual trade then the contract may be frustrated. However, specific considerations apply when considering supervening prohibitions on imports. For example:

- The prohibition must prevent performance of the contract itself. The contract will only be frustrated if it is a term of the contract that the goods shall be exported from Turkey and imported to the country which has imposed the prohibition.

- The prohibition must not be temporary. The contract will only be frustrated if performance is impossible. If the import/export ban is lifted prior to the end of the period for performance, the contract will not be frustrated.

An FOB contract is only likely to be frustrated by a prohibition on export of goods where that prohibition prohibits export of the relevant goods completely, regardless of their destination. Unless, exceptionally, the FOB contract specifies the intended country of import, it will not be frustrated by a prohibition that is specific to the country into which the buyer intends to import the goods.

Similarly, a CIF contract will not necessarily be frustrated by an import ban at the buyer's intended place of import. CIF contracts are not contracts for delivery of goods in a specified place, but are contracts to ship the goods under a contract of carriage specifying that destination. The contract is unlikely to be frustrated because the seller can fulfil their obligation in arranging for shipment, and it remains open to the buyer to redirect the goods to another country. It is possible that a ban on import of the relevant goods by the country of discharge would amount to frustration of a CIF contract if it applies to the entire period allowed for performance.

COMMODITY CONTRACTS: FORCE MAJEURE

English Law

Tariffs/Fall in lira

Typically, commodity contracts do not contain force majeure clauses expressly covering economic difficulties like a collapse in the market or a drastic change in exchange rates.

In most cases, parties seeking to rely on economic difficulties as force majeure events would need to demonstrate that those economic difficulties came within the general meaning of "force majeure". Typical wording, as in GAFTA Contract No 41, makes provision for "any other event comprehended" in or by "the term 'force majeure'".

However, an argument that a significant fall in the value of the lira comes within the scope of this general force majeure wording is likely to prove extremely difficult as it is well-accepted that the general meaning of "force majeure" does not include economic difficulties (e.g. *Thames Valley Power Ltd v Total Gas & Power Ltd* [2005] EWHC 2208 (Comm)).

Force majeure clauses generally release parties from their obligations only when it has become impossible to perform them in part or in whole. The court will not relieve a party from the consequences of entering into a bad bargain or one which has become difficult to perform.

Tariffs which make performance more costly are unlikely to amount to force majeure events in the absence of clear and express contractual wording to that effect or an actual impossibility of performance. Tariffs are likely to be treated in the same manner as other economic factors which affect price and profitability. It is possible that a tariff might be so exceptionally high that it makes trading practically impossible, although this would require exceptional circumstances beyond the existing tariff levels currently imposed by the US.

Import bans on Turkish products

Whether import bans on Turkish goods imposed by other countries amount to a force majeure event depends largely on the terms of the contract.

Under a CIF contract, which requires the seller to arrange carriage to a particular destination, there may be scope for arguing force majeure, although the contract terms are key.

GAFTA CIF Contract No. 41 includes "prohibition of export" in its list of relevant events so a ban on export of the goods to be delivered under the contract should be covered by the force majeure clause. However, prohibition on imports is not specifically mentioned and it is unlikely that a ban on the goods by the country of discharge specified in the contract would fall within the general wording "any other event comprehended in the term force majeure", the meaning of which is likely to be influenced by the preceding events listed.

VOYAGE CHARTERS: FRUSTRATION & FORCE MAJEURE

English Law

Single voyage charters

Where discharge of cargo at the port of delivery specified in the contract is prevented and the charterparty does not provide for this event, the charter may be frustrated.

It is therefore possible that voyage charters could be frustrated by a prohibition, after the charterparty has been entered into, on discharge of Turkish cargo at the designated discharge port. This will depend on the wording of the charterparty. For example, if the charterparty provides that discharge must be undertaken at a particular discharge port or as near as the vessel can get to that port, there is unlikely to be a frustration as a consequence of the prohibition.

It is also possible that a prohibition on the import of Turkish cargo could amount to a force majeure event, although this would depend on the wording of any relevant force majeure provisions in the charterparty.

Consecutive voyage charters

Whether a voyage charterparty covering multiple voyages would be frustrated by a prohibition on discharge depends on whether the voyages are classified as a single enterprise or separate adventures. Where the voyages are performed consecutively, generally the voyages will be considered as one adventure, but if there is an interruption between voyages and the vessel is otherwise employed, it is more likely that they are separate adventures.

If voyages are separate, frustration of one voyage is irrelevant to the frustration of the others. Therefore frustration of certain voyages due to an existing ban on Turkish cargo does not mean that voyages to be performed some time in the future will also be frustrated. If multiple voyages form part of a single adventure, whether the entire charterparty is frustrated depends on whether the proportion of the voyages affected by the event is such that performance of the remainder of the contract is radically different from what the parties had originally agreed.

A party would therefore face difficulties in arguing that an inability to discharge Turkish cargo based on an existing prohibition, would lead to a frustration of the entire charterparty if many voyages were intended to take place some time in the future.

As with single voyage charters, it is possible that prohibition on the import of Turkish cargo could amount to a force majeure event for a multiple voyage charterparty, depending on its provisions.

DERIVATIVE CONTRACTS ISDA

English Law

It is unlikely that a party would be able to rely on any general provisions in the 2002 ISDA Master Agreement ("the Master Agreement") to terminate a transaction on the basis of a fall in the lira.

Under the Master Agreement "*Each payment…will be made in the relevant currency specified in [the]…Agreement for that payment*". This is the case even if the nominated currency has significantly fluctuated or if a party holds its primary funds in a different currency.

Force Majeure

The Master Agreement contains a force majeure provision which describes any "force majeure or act of state" which renders performance "impossible or impracticable . . . so long as the force majeure or act of state is beyond the control of such Office, such party or such Credit Support Provider, as appropriate, and such Office, party or Credit Support Provider could not, after using all reasonable efforts (which will not require such party or Credit Support Provider to incur a loss, other than immaterial, incidental expenses), overcome such prevention, impossibility or impracticability".

Although the scope of this type of clause is yet to be determined by the English courts, and no specific examples of force majeure are given in the Master Agreement, it is understood to cover events such as a change in law, natural forces such as earthquake or hurricane, armed conflict, terrorism, labour disputes or any other circumstances beyond the control of the parties or their Credit Support Provider.

However, the fact that a transaction has become dramatically more expensive for a party is very unlikely to be sufficient to trigger the force majeure provision under the Master Agreement and therefore a fall in the price of the lira is unlikely to allow a party to terminate a transaction on the basis of force majeure.

Event of default

Nevertheless there are a number of mechanisms under the Master Agreement that may offer protection against falls in the lira. For example, where a fluctuation in the value of the lira is such that one of the parties becomes insolvent, is unable to pay its debts as they become due, or defaults under a Credit Support Document, this may amount to an Event of Default under the Master Agreement.

On the occurrence of an Event of Default the non-defaulting party generally has the option close out all outstanding transactions by written notice. However, where the Automatic Early Termination provision has been specified in the Schedule to apply, then the occurrence of an Event of Default will automatically trigger the closing out of all outstanding transactions.

It is also possible for the parties to specify termination events in the Master Agreement, which would allow close out of certain transactions in particular circumstances. This could include the right to close out transactions for significant devaluations of a particular currency.

CONTRUCTION: MANAGING RISK

English Law

Currency fluctuation and international construction and engineering projects

On international projects, the effect of currency fluctuations are felt in two principal ways: directly on the price payable for the works and indirectly in contractors' input costs.

Works are often valued in one currency and paid, at least in part, in another. This arrangement is usually driven by the source of funding (e.g. domestically or internationally such as from an international funding agency) and not the location of the project. Similarly, the currencies of these payments often do not match the currencies of the contractors' input costs. Such payments are naturally vulnerable to changes in currency exchange rates and can affect funders.

Currency fluctuations can also have a more indirect effect – on the cost of a project. Where the supply chain itself is dependent on the international market for resources, inflation on the market price is necessarily partly driven by changes to currency exchange rates.

Given the scale of international construction and engineering projects, the sums and the risks involved can be extremely significant.

Who bears the risk of currency fluctuation?

The starting point is that the contractor will be entitled to payment for the works in the currency named in the contract. If a contractor agrees to complete the works for a price in one currency that is also payable in that currency, it is typical for the contractor to bear the risk of any fluctuations to currency exchange rates which may affect the contractor's costs. However, beyond this, it becomes less straightforward and dependent on the terms of the specific contract, including whether the currency of valuation is the same as the currency of payment, whether any exchange rate is fixed and whether there is any mechanism for the adjustment in prices. Ultimately, this is a commercial matter for negotiation and agreement between the parties.

The industry is alive to the risks of currency fluctuations. Often in long term contracts, the currency exchange rate is fixed at the outset and the contractor will take the risk of the increase in costs for items such as labour, equipment and materials for the first 12-18 months of the project and thereafter is entitled to an adjustment to the contract price in the event of fluctuations in the price of labour, materials and equipment. This entitlement to an adjustment to the contract price based on changes in *cost* can provide a degree of protection to contractors where a currency exchange rate is fixed if drafted and operated properly. The 1st editions of the FIDIC Red and Yellow Books published in 1999 follow this approach (see Sub-Clauses 13.8 and 14.15).

The contract will usually include formulae to calculate the appropriate adjustment, for example by reference to consumer, retail or specific construction indices. A number of national and international organisations publish indices that could be used including TUIK or Eurostat.

With this said, the proper interpretation and application of price fluctuation clauses is a fertile source of disputes on construction projects owing to:

- Their complexity
- That they are simplified mechanisms, not reflecting actual cost changes
- The significant sums involved.

Managing the risk of currency fluctuation

Employers and contractors are powerless to control currency exchange rates. However, they can take certain measures to manage and mitigate the associated risks.

When considering the allocation of risk of currency fluctuation in the contract, the most important time is during tender negotiations. If the contract is to contain currency fluctuation provisions, it is important that the specific details, such as payments in different currencies and price fluctuation formula, reflect both the agreed risk allocation and also the reality as to where the costs are likely to be incurred, with appropriate cost indices or reference prices chosen. Other mitigation measures, particularly on large projects to be implemented over a number of years, might include taking steps to insure against currency fluctuations, such as through hedging products.

Conclusion

Fluctuations in currency exchange rates may undermine the financial viability of an international construction project, almost overnight. This will only increase in light of the current procurement trend towards larger, single-package contracts.

For the Turkish contracting market, the recent depreciation of the Turkish lira highlights the risks involved, affecting both 'domestic' projects within Turkey as well as projects with an international element, for example, projects within Turkey involving financing from international funding agencies or the import of materials and services and projects outside of Turkey.

When engaging in a long term international construction or engineering projects in a country with a history of real fluctuations in currency exchange rates, it is essential to consider the financial risks associated with currency fluctuations. As briefly outlined above, the risk faced by a contractor is amplified if the project is:

1. Long term i.e. more than 12 months
2. Based in a country or to be paid in a currency that presents a high risk of fluctuations in currency exchange rates
3. Where materials and/or labour and/or equipment is being obtained from a different country and/or is being paid for in a different currency

4. Third party financing is in place and to be repaid in a different currency to the contract price.

If any, or a combination of the above factors exist, it is important to ensure that the risk of currency fluctuations is properly and clearly addressed in the contract, for example, through a price fluctuations clause.

AVIATION

Turkish Law

Contractual uncertainty/lack of finality

Under Turkish law, where, after a contract has been signed, should the circumstances change so drastically that the contract becomes unfairly burdensome for one party, the Judge has the authority to amend the terms of the contract accordingly[1]. The devaluation of the lira has led to a significant increase in companies seeking advice on how to deal with these contractual aspects and requesting advice and guidance on renegotiating the terms of those contracts to avoid Court intervention.

Settlements, judgments and reserves

Due to the devaluation of the lira over time, this has led to more favourable judgments for reinsurers when converted into US dollars. This has also tended to compensate for, and negate, the additional interest charges on the judgment sum, that Turkish courts apply over a lengthy period of time, which can be up to 20% (commercial rate) on damages.

Currency

From a litigation perspective, claimants are increasingly demanding settlements to be paid in USD, not lira.

From a finance perspective, USD is the preferred currency for aircraft finance transactions in Turkey (if the airline is also long in other currencies such as euro, yen or Swiss franc, any of these currencies could also be selected for certain aircraft finance transactions).

Furthermore, all airlines should enter into fuel hedge transactions to protect themselves against the negative effect of fluctuations in the value of USD.

[1] Whether the Turkish courts will intervene to amend the terms of the contract depends *inter alia* on the fulfilment of the criteria set out in Article 138 of the Code of Obligations.

PORTS & TERMINALS: INVESTORS

English Law

Purchase price

As a result of the depreciation of the lira, Turkish ports and terminals are cheaper for international investors (including international terminal operators, shipping lines, institutional investors or commodity traders). This is particularly the case where the valuation of a target port or terminal is based on metrics denominated in lira.

The purchase price, however, is only one factor which international investors will consider. The short-term, mid-term and long-term 'value' of a target port or terminal will depend on a number of additional commercial and legal factors.

Revenues

Potential investors will want to establish whether all or the majority of a target port or terminal's revenues are in lira and, if so, whether any specific foreign exchange controls are imposed on a target operator, port or terminal. If such target charges, or has the flexibility to charge, its customers in another currency (such as United States dollars or euros) this could provide a hedge against further fluctuations of the lira as well as increase a particular port or terminal's returns on investment should the lira depreciate further (assuming that the majority of its operating costs and other expenses are denominated in lira).

Outgoings

Another factor is whether the target operator, port or terminal has any commitments or outgoings in currencies other than lira. These could now be relatively more expensive for a target to meet if the majority of its revenues are denominated in lira. Such commitments include the payment of concession fees as well as the servicing of any loans in currencies other than lira. These commitments could reduce a port or terminal's returns as the lira depreciates.

Inflation

In addition, as inflation has increased in Turkey, a potential investor will need to consider any provisions in concession agreements for the adjustment of concession fees in line with inflation (in Turkey, concession fees can be increased annually based on the Producer Price Index). Any such increases could have an adverse impact on a port or terminal's bottom line, although their impact may be mitigated by the inclusion of a cap on annual concession fee increases, linking any such increases to another country's price index or similar clause in a relevant concession agreement. Such a clause may include a mechanism for adjusting the economic balance of a concession agreement if, as a result of a qualifying event (which may

include depreciation of the lira or inflation above a certain threshold), a party's economic or financial position is materially adversely affected.

A potential investor should also consider the termination provisions of any concession agreements to which a target port or terminal operator is a party. In particular, any investor should assess the level of any termination compensation payable to the concessionaire and whether any such compensation is payable or denominated in lira.

Wider economic circumstances

The reported slowdown to the growth of the Turkish economy is also a factor which any investor will need to consider carefully. Consumer demand has weakened as a result of the depreciation of the lira and inflation. This could result in less import handling charges being levied by Turkish port or terminal operators where imports are cancelled. This should be balanced against opportunities for Turkish exporters to produce products relatively more cheaply and increase their profits for exports charged in US dollars or euros. In any event, investors should ensure that any performance standards or requirements in underlying concession agreements allow sufficient flexibility to cater for significant drops in the level of cargo throughput at a port or terminal.

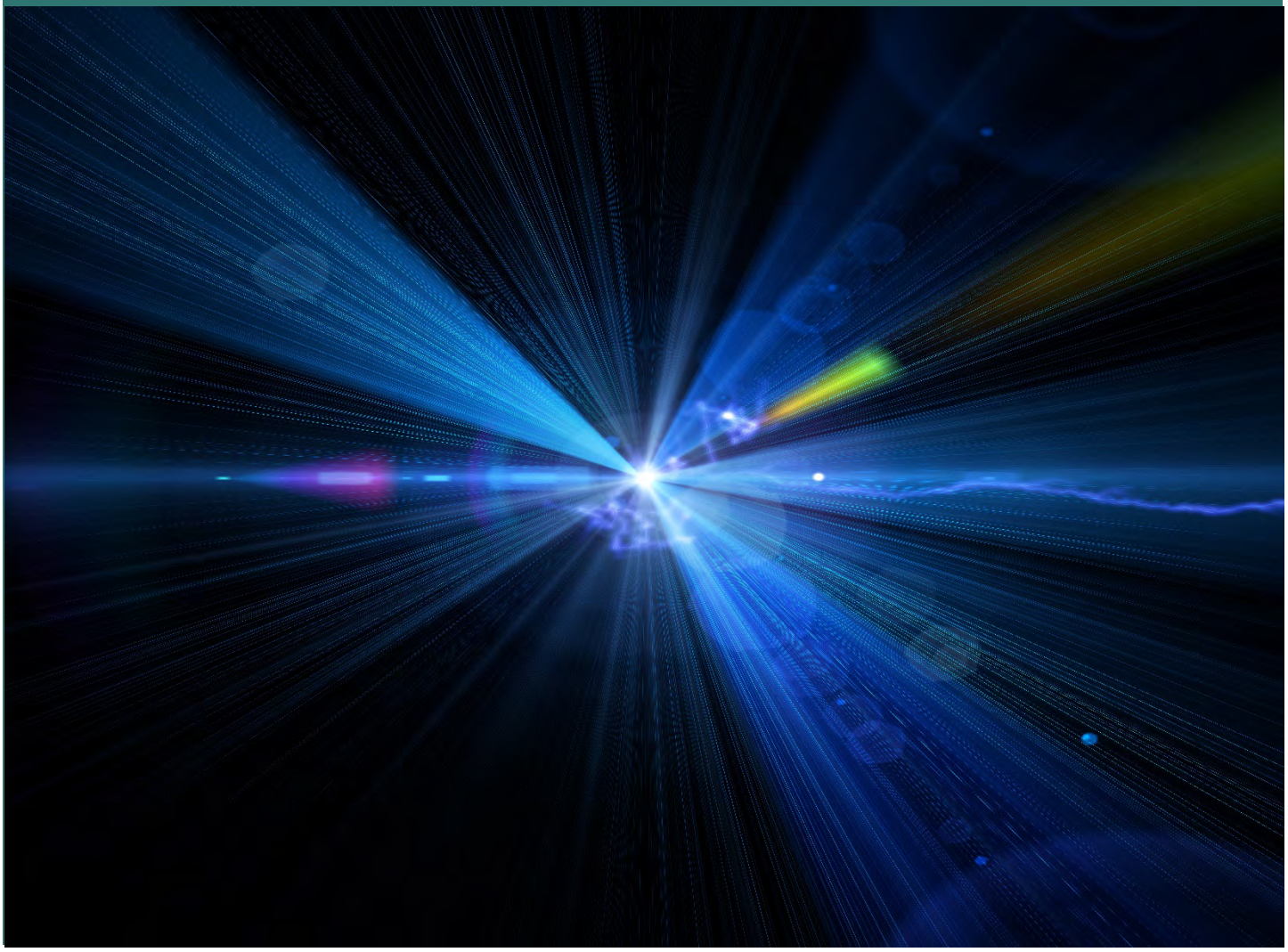
Tourism

The industry within which the target operator, port or terminal operates is another factor. It has been reported that the depreciated lira may prove an opportunity for ports or terminal operators operating cruise terminals as holidays are likely to be cheaper for foreign tourists.

Finally, investors should consider the political risk associated with the acquisition of a port or terminal in Turkey in this climate. In the event of a recession, the Government may take mitigating measures which could adversely impact on the profitability of an investment (e.g.: by imposing foreign exchange controls, restricting the repatriation of profits from Turkey or reducing port tariffs). Investors may, however, take some comfort from Turkey's '2023 goals' which include improving and expanding overall port capacity in the country – this could prove a disincentive for the Government taking measures which could deter international investment in the industry.

02

SECURITY



SECURITY UNDER TURKISH LAW

Overview

Under Turkish law, it is not possible to establish blanket security under a single general security agreement and accordingly, different types of securities are collateralised separately under separate security agreements.

Furthermore, pursuant to the Law No. 805, an agreement to be executed by and between Turkish individuals and/or Turkish legal entities should be in Turkish. However, if one of the parties to an agreement is not a Turkish individual or a Turkish legal entity, the parties may freely decide on the language of the agreement. That being said, agreements which are subject to formal registration or execution procedures, such as movable asset pledge agreements and mortgage agreements, must be executed in Turkish (or in a bilingual format provided that the Turkish version shall prevail in case of a discrepancy).

Under Turkish law, any provision which envisages that the title to the pledged assets shall automatically be transferred to the pledgee in case of default is void (due to the *lex commissoria*), save for certain conditions regarding which an exemption is imposed by virtue of applicable laws.

Further requirements in relation to different types of security are set out below.

Pledge

Entering into a written pledge agreement is a customary practice regarding the establishment of a security interest, especially for evidentiary purposes.

Movable Asset Pledge

In order to create a pledge over movables, the physical possession of the pledged asset should generally be transferred to the pledgee as a perfection requirement,[2] although there are exceptions to this rule.

The Law on Movable Asset Pledge in Commercial Transactions (Law No. 6570) (*published in the Official Gazette dated October 28, 2016 with no. 29871*) (the "**Pledge Law**") has introduced a new concept on the establishment of pledges over movables and as per the Pledge Law, a pledge can be established over the following movables without the necessity to deliver possession:

1.	Receivables;
2.	Perennial trees bearing fruit;
3.	Intellectual property rights;
4.	Raw materials;
5.	Animals;

[2] Article 939/(1) of the Turkish Civil Code (Law No. 4721) (published in the Official Gazette dated December 8, 2001 with no. 24607) (the "Civil Code").

6.	Any revenue and income;
7.	Licenses and permits which are not required to be registered with other registries (save for regulatory and administrative permits);
8.	Rental incomes;
9.	Tenancy (lease) rights;
10.	Moveable enterprise assets including machinery, tools, equipment, motor vehicles and any electronic tool such as electronic communication tools;
11.	Consumables;
12.	Supplies (inventory);
13.	Agricultural products;
14.	Trade names and/or enterprise names;
15.	Commercial or tradesman enterprises;
16.	Commercial (vehicle) plates and commercial lines;
17.	Commercial projects;
18.	Wagons;
19.	Other moveable assets, rights and jointly owned properties in possession of third parties; and
20.	Any similar moveable asset and rights.

A written movable pledge agreement to establish a security interest in any of the assets and rights specified above should be executed by and between the pledgor and the pledgee before a notary public in *ex officio* form (i.e. in Turkish or a bilingual format with Turkish version to prevail) and then such agreement shall be registered with the Pledged Movables Registry.

The Pledge Law has introduced another new concept that abolishes the *lex commissoria* principle which prevents the pledgee from the benefit of gaining the title to the pledged assets in case of default. In case of non-payment of a debt secured via a movable asset pledge, the pledgee has the right to request the transfer of the ownership of the movable asset(s). This must be explicitly stated in the agreement.

Finally, the pledge shall be released by the pledgee within 15 days of the payment date of the debt if the pledgee is a Turkish entity. On the other hand, if the pledgee is a foreign entity, the pledgee must apply to the Pledged Movables Registry for the release of the security within 30 days of the payment date of the debt. The pledgor and/or the debtor (if a different entity than the pledgor) may file a complaint with the registry if the pledgee fails to comply with this requirement and as a result of which the pledgee may be fined with an administrative penalty amounting to 10% of the secured debt.

Share Pledge

Establishing a pledge over shares is similar to movable assets, with a few differences. As pledges over shares are not explicitly listed under the Pledge Law, a share pledge cannot benefit from the exemptions that the Pledge Law provides.

A pledge over the shares of a company can only be established by entering into a written pledge agreement and in order to ensure the legal validity and enforceability of the pledge over the shares, physical possession of the pledged shares (bearing blank endorsement or the pledge endorsement of the pledgor) must be delivered to the pledgee or a custodian to be appointed by the pledgee. Unless any additional procedure is envisaged under its articles of association, the company (whose shares are subject to a pledge) should adopt a resolution for the registration of such pledge with the share ledger of the company. Under Turkish law, the voting rights of the shares pledged in favour of the pledgee are required to be exercised by the legal title owner during the term of the pledge, in other words, the pledgor should continue to enjoy its rights as a shareholder until a default occurs.

The *lex commissoria* principle prohibits inserting any provision in the pledge agreement enabling the pledgee to become the title owner of the pledged shares in case of default. Upon the occurrence of an event of default, the pledgee has the right to apply to the execution office to initiate foreclosure proceedings in order to encash the pledge and the shares subject to pledge shall be sold via execution proceedings[3] and the pledgee shall be satisfied from the proceeds of such sale. However, this is not a mandatory provision of Turkish law and the pledge over the shares may be foreclosed by the pledgee by means of a private sale without requiring a judicial proceeding provided that such mechanism is envisaged explicitly under the pledge agreement.

Account Pledge

The establishment of a pledge over a bank account is possible through the fulfilment of the following requirements: execution of a written pledge agreement; a notification filed with the relevant account bank(s) following the execution of the agreement by the parties; and an acknowledgement from the account bank(s) in this respect.

There is no statutory requirement to obtain consent from the account bank for the pledge. However, an acknowledgment notice from the account bank is highly recommended and may ascertain whether a prior ranking pledge, assignment or counterclaims regarding the account exist.

[3] Execution and Bankruptcy Law (Law No. 2004) (published in the Official Gazette dated June 19, 1932 with no. 2128) (as amended from time to time, the "Execution and Bankruptcy Law").

Assignment of Receivables

The assignment of receivables is subject to the requirements set forth under the Pledge Law.

In addition, it is recommended to deliver notice of assignments to the debtors of the pledgor and obtain acknowledgement of assignment. By doing so, the debtor acknowledges the assignment and is not released from its payment obligation in case of any payment made by the debtor to the pledgor in good faith.

Mortgage

Under Turkish law and according to Article 881 of the Civil Code, a mortgage can be created as security for any kind of present, future or contingent debt, by registering a mortgage over a real property with the records of the relevant Title Deed Register where the real property subject to mortgage is registered. The perfection of a mortgage requires a mortgage agreement to be entered into between the mortgagor and mortgagee at the Title Deed Register (in the official form and in Turkish) and thereafter, registration of the mortgage with the same.

In principle, the amount of the mortgage is required to be registered in Turkish lira; however, according to Article 851/II of the Civil Code, in the event the mortgage is to be registered as a security for a foreign currency cash loan to be obtained by a borrower resident in Turkey from a credit institution conducting business within Turkey or abroad, the amount of the mortgage can be registered in foreign currency, which should be the same currency as the loan.

In case of default, the mortgagee is entitled to enforce the mortgage and request foreclosure of the mortgage. Upon sale of the property, the mortgagee will be paid from the proceeds and any surplus amount will be returned to the mortgagor.

Ship Mortgage

The Turkish ship mortgage may be defined as a right created to secure a claim, which grants the mortgagee a *right in rem* over the ship. The scope of the ship mortgage includes all the integral parts of the ship such as the engine, hatch covers, navigational instruments, life boats, furniture and anchor chains.

There are three steps to establish a mortgage over a ship: (i) recording the agreement of the parties in the mortgage deed; (ii) the application for the registration of the mortgage; and (iii) the registration procedure itself.

Mortgage agreements should be concluded in writing and the signatures of the parties of this deed should be certified by a notary public[4]. Alternatively, the mortgage agreement may also be concluded before the ship registrar.

[4] Article 1015/2 of the Turkish Commercial Code (Law No. 6102) (published in the Official Gazette dated February 14, 2011 with no. 27846) (as amended from time to time, the "TCC").

If the mortgage agreement is concluded before a notary public abroad, then an Apostille from the relevant authority of such country is required. The mortgage agreement may be concluded in foreign languages, provided that one of the parties is a foreign individual or legal entity, and if so, the notarized Turkish translations of the mortgage agreement should be submitted to the registrar.

Following the conclusion of the mortgage agreement, the mortgage agreement should be registered in person with the relevant ship registry e.g. the Turkish International Ship registry, in order to become enforceable against third parties. If the registration application is filed only by the mortgagee, then the consent of the ship-owner would be required to complete the transaction.

As a general rule, unless otherwise specified in the mortgage agreement, the ship mortgage is not limited by any validity period under Turkish law.

A ship mortgage grants the mortgagee the right to collect its receivables only from the proceeds of the judicial sale of the vessel, over which the mortgage has been established.

The mortgagee has various legal remedies for the collection of its receivables, including:

1. Ship Arrest (Precautionary Attachment)

   Ship mortgage is included in the list of maritime claims, as specified in Article 1352 of the TCC. Article 1353 of the TCC entitles the mortgagee to apply to the courts for the arrest of the ship, over which the mortgage has been established, by way of precautionary attachment decision.

2. Encashment of Mortgage

   The mortgagee shall be entitled to apply to the bailiff's office for the encashment *(foreclosure)* of the mortgage through a public auction in accordance with the provisions stipulated in the Execution and Bankruptcy Law and the TCC.

3. Bankruptcy Request

   According to Article 1378 of the TCC, the mortgagee may also carry out a proceeding by way of requesting the bankruptcy of the owner/mortgagor.

4. Urgent Sale

   In the event that the value of a vessel rapidly falls or the maintenance thereof proves too costly, and in particular, it causes new lien rights to arise or the number thereof to increase, the bailiff's officer or the creditor may apply to the Enforcement Court in order to achieve urgent sale of the vessel.

5. Private

   As stated above, the mortgage does not provide any right to the mortgagee to take possession of the ship. However, private sale is possible under Article 1387 of the TCC, according to which a vessel may be sold by way of negotiations, provided that the urgent sale is requested by all interested parties.

6. Deterioration of the Vessel

As per Article 1030 of the TCC, in the event that the security provided by the mortgage is endangered as a result of the deterioration of the vessel, the mortgagee may grant an appropriate period to the owner to remedy such situation. In the event that the owner does not remedy the deterioration within such period, the mortgagee becomes entitled to immediately encash the mortgage.

Guarantees

General Overview

Guarantees are regulated pursuant to Article 128 of the Turkish Code of Obligations (Law No. 6098) (*published in the Official Gazette dated February 4, 2011 with no. 27836*) (as amended from time to time, the '**TCO**') which states that "*the party which undertakes a third party's obligation in favour of the other party is liable to indemnify the damages arising out of the non-performance of this obligation*".

Comparison with suretyship

The most utilised mechanisms of personal or corporate undertakings under Turkish law are surety agreements and guarantee agreements, which share certain characteristics (especially with respect to validity requirements). However, these two mechanisms have totally different legal implications. The key differences are as follows:

- A surety agreement creates a binding secondary obligation on the surety. There are two main criteria in this respect; (i) the dependency of the surety agreement on the underlying agreement, and (ii) thesecondary nature of the surety's obligation. As such, a suretyship can exist if it is based on a valid and enforceable contractual relation. On the other hand, the guarantee executed by and between the guarantor and the beneficiary is an independent agreement and is not bound by the terms of the agreement between the principal and the beneficiary.
- Article 591 of the TCO provides that the surety is entitled and obliged to plead against the beneficiary all defences available to the principal provided that such defences are not based on the insolvency of the principal. However, the guarantor is not entitled to use such defences the principal may have against the beneficiary pursuant to the underlying agreement and the guarantor may exert only his/her own defences arising under the relationship established between the guarantor and the beneficiary.

Validity Conditions of Guarantees

A guarantee agreement may be drafted either for a specific term or an indefinite term, in which case the guarantee continues to be valid and in effect until all of the obligations and liabilities guaranteed have been fulfilled.

Under Turkish law, a simple written agreement is generally sufficient to prove the existence and validity of a guarantee (provided that such agreement does not violate any mandatory provision of Turkish law); save for the condition stipulated under Article 603 of the TCO wherein it is specified that certain provisions of the TCO regarding validity of suretyship shall also be applicable to any personal security (including guarantees), regardless of the title under which such security has been issued. This includes certain statements which must be provided by a guarantor for the guarantee to be valid.

Notification to the Undersecretariat of Treasury

In addition, in cases where individuals or legal entities resident in Turkey issue guarantees, sureties or other similar undertakings in favour of third parties located outside Turkey, they must file a notification with the Undersecretariat of Treasury within 30 days of execution[5].

If a guarantor fails to file a notification with the Undersecretariat of Treasury within the required time, it will be subject to administrative monetary sanctions[6].

[5] Article 18 of the Decree No. 32 on Protection of the Value of Turkish Currency (published in the Official Gazette dated August 11, 1989 with no. 20249).

[6] Article 3 of the Law No. 1567.

GUARANTEES OFFERED BY TURKISH COMPANIES

Relevant Considerations for Counterparties and Other Corporate Issues

Overview

Guarantees provide one means by which commercial lenders or creditors, especially those with high levels of exposure to the Turkish economy, can protect themselves against problems with the repayment of their loans and/or enforcement of security, such as a corporate guarantee, in the event of a company's default or breach of the underlying contract.

Enforcement of the guarantee

It is important that a lender or creditor is confident that it will be able to enforce a guarantee against a Turkish guarantor in the event of default or breach by a principal or debtor. Foreign companies should ensure that the Turkish guarantor is well-capitalised and able to pay an amount or fulfil the obligations of a third party if the third party fails to do so itself. This means that due diligence on the Turkish guarantor is important before a lender or creditor enters into a guarantee with such a guarantor.

Currency

Recent restrictions on the use of foreign currency denominated or indexed payments for certain types of contracts[7] applies to contracts concluded between Turkish companies only. Contracts involving a foreign party are exempt from the restriction, provided that the foreign party is not a (i) branch of a Turkish resident; (ii) fund operated by a Turkish resident; or (iii) Turkish resident that owns 51% of such foreign entity's share capital.

Therefore, foreign companies still have the freedom to and should thoroughly consider the currency of a payment before a guarantee is entered into with a Turkish counterparty. Foreign investors may seek to secure payments under a guarantee in US dollars or euros to protect against fluctuations in the lira.

English contract law considerations

Guarantees are subject to general contract law principles, including offer and acceptance and consideration. Furthermore, a guarantee is a secondary obligation. This effectively means the guarantor is only liable if the guaranteed party is liable under the underlying contract. Correspondingly, if the

[7] Amended to Decree No. 32 Regarding the Protection of the Value of the Turkish Currency published in the Official Gazette on 13 September 2018 introduced a ban for foreign currency and foreign currency-indexed pricing with regard to certain contracts between Turkish residents.

underlying contract is invalid, there is nothing which can be enforced against the guarantor, although many guarantee documents also incorporate indemnity wording to address this.

As outlined in the first section of this pack, as a matter of English law, the imposition of tariffs by the United States on Turkish products is unlikely to discharge or otherwise affect the enforceability of contracts for such products.

However, an English court will not enforce a contract or award damages for a contract made with the object of violating the law of a friendly foreign state. This principle is based on public policy and international comity. Therefore, if a foreign party enters into a contract with a Turkish company, performance of which is illegal in Turkey, then it is possible the English courts may not enforce that contract (or a guarantee given in connection with it).

It should also be noted that Article VIII(2)(b) of the Bretton Woods Agreement[8] and International Monetary Fund's Articles of Association provides that: "*exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of any member maintained or imposed consistently with this agreement shall be unenforceable in the territories of any member*." The United Kingdom, as well as other European Union member states, have passed article VIII(2)(b) into domestic law. Therefore, if Turkey's foreign exchange controls are in breach of the United Kingdom's exchange control regulations then an exchange contract that embodies Turkey's exchange controls will be unenforceable in the courts of England and Wales no matter what the governing law of the exchange contract is. Likewise, a guarantee linked to such exchange contract will be unenforceable.

[8] The Bretton Woods Agreement is a system for monetary and exchange rate management developed at the United Nations Monetary and Financial Conference held in Bretton Woods, New Hampshire in July 1944.

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03

ENFORCEMENT

TURKISH COURT JUDGMENTS & ARBITRAL AWARDS IN ENGLAND & WALES

Enforcement of Turkish court judgments in England and Wales

The common law rules apply to the enforcement of Turkish Court judgments in England and Wales. Turkish court judgments will only be enforceable in England and Wales if all of the following apply to the contract:

- It is final and conclusive – however all routes of appeal need not have been exhausted (although the courts of England and Wales may grant a stay pending resolution of Turkish appeal proceedings)
- It is for a sum of money, but not for taxes, a fine or a penalty – Turkish orders awarding specific performance or injunctions cannot be enforced in England and Wales
- It has been decided on its merits i.e. following consideration of the facts and application of principles of law.

However, Turkish judgments cannot be enforced directly. Rather, the judgment creditor must commence a debt action in England and Wales relying on the Turkish court order as the cause of action. It is likely that summary judgment can be obtained although the English courts have discretion in recognising Turkish judgments.

Such an action may be resisted by the Turkish judgment debtor if any of the following apply:

- The Turkish courts lacked jurisdiction according to the conflict of laws rules under English law i.e. the defendant had no territorial connection to Turkey or the defendant had not submitted to the jurisdiction of the Turkish courts. A defendant may have a territorial connection to Turkey where it carries out business itself in Turkey, has a fixed place of business in Turkey, or where it is a corporation and its representative carries its business from a fixed place of business in Turkey[9].
- The judgment was obtained by fraud, even if fraud was not pleaded in the substantive dispute.
- The judgment is contrary to the public policy of the United Kingdom or has been granted in contravention of Article 6 of the European Convention on Human Rights (the right to a fair trial).
- The proceedings were brought in contravention of a jurisdiction or arbitration agreement.

The English courts have indicated that demonstrating these grounds of resistance may be a high threshold to meet. In the case of *Tanir v Tanir*[10] a father applied to the English courts to enforce a Turkish judgment for EUR 115,000 against his son. The son failed to respond to the claim form, and default judgment was entered against him. The court decided the case on the basis that the default judgment had not been wrongly entered. However, the court went on to consider whether the son would have had a reasonable prospect of resisting the father's application to enforce the Turkish judgment. Garnham J held that:

[9] *Adams v Cape Industries plc* [1990] Ch 433.
[10] [2015]EWHC 3363 (QB).

- Despite a 'stark conflict of factual evidence' between each party's witnesses this was insufficient to demonstrate that the Turkish judgment was obtained by fraud, and
- An element of the Turkish judgment that applied additional costs where the judgment debtor did not make payment within the terms of the judgment did not amount to a penalty that contravened public policy.

Enforcement of Turkish arbitral awards in England and Wales

Turkey is a signatory to and has ratified the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the 'New York Convention'). Therefore, arbitral awards made in Turkey or where the seat of the award is Turkey, are recognised as binding between the parties in England and Wales, and with leave of the court may be enforced in England as if they were judgments made by the English courts.[11]

Applications to enforce a Turkish arbitral award in England may be made without notice and must be supported by authenticated originals or certified copies of:

- The original award, and
- The arbitration agreement.

Where these documents are in Turkish, they must be translated into English, and the translations must be certified.

The courts do have a limited discretion to refuse to recognise a Turkish arbitral award, but may only do so on the basis of any of the following grounds applying:

- Incapacity of a party to the arbitral award
- Invalidity of the arbitration agreement under Turkish law
- Insufficient notice of the arbitration having been given to the other side, or the inability of the other side properly to present its case
- The award dealing with matters beyond the scope of the submissions to the arbitration
- Improper or unlawful constitution of the tribunal
- The award not yet being binding on the parties, or
- Enforcement of the award being contrary to public policy.

However, there is a strong presumption in favour of the courts granting leave to enforce arbitral awards of New York Convention party states. The presence of one of the above factors will not automatically prevent

[11] Section 101 *Arbitration Act 1996.*

the courts from enforcing the award.[12] Nevertheless, this discretion is not open ended, and it will be important to consider any Turkish arbitral award in light of Turkish procedural arbitration laws.

[12] *IPOC (Nigeria) v Nigerian National Petroleum* [2005] 2 Lloyd's Rep 326.

FOREIGN COURT JUDGMENTS & ARBITRAL AWARDS IN TURKEY

Parties may enforce foreign judgments or arbitral awards such that they have the effect of a "final judgement" in Turkey via local courts. However, an English court judgment or arbitral award cannot be recognised and/or enforced in Turkey immediately. Only foreign court judgments and arbitral awards regarding civil suits which have become final in accordance with the laws of the relevant foreign country may be enforced in Turkey, provided that an enforcement order is rendered and granted by the competent Turkish court.[13]

Enforcement of foreign court judgments in Turkey

Turkish courts will not enforce any foreign court judgment unless there is (i) a treaty and/or a bilateral agreement in effect between such country and Turkey providing for the reciprocal enforcement of judgments, or (ii) de facto reciprocity in the field of enforcement of judgments between such country and Turkey, or (iii) a provision in the law of such country which provides for the enforcement of judgments of the Turkish courts.[14]

A judgment rendered against a Turkish individual or a legal entity by a foreign court will be recognised and enforced by Turkish courts without re-examination of the merits of the dispute, subject to all of the following conditions being satisfied:[15]

- The judgment has become final and binding with no recourse for appeal or similar revision process under the laws of the foreign jurisdiction
- The judgment is not rendered by a court which does not have an actual connection to the parties or the subject matter of the judgment (provided that the defendant claims this)
- There is de facto or de jure reciprocity between Turkey and the relevant country (in case there is not a bilateral agreement between Turkey and such country or a treaty to which both Turkey and such country are a party)
- The subject matter of the judgment does not fall under the exclusive jurisdiction of the Turkish courts
- The judgment is not clearly against the Turkish public policy rules, and
- The person against whom enforcement is sought does not raise objections in the Turkish courts to the effect that he was not duly summoned to or represented at the foreign court or that the judgment was rendered in his absence in violation of the laws of the foreign jurisdiction.

[13] Article 50 and Article 60 of the International Private and Procedure Law (Law No. 5718) (published in the Official Gazette dated December 12, 2007 with no. 26728) (as amended from time to time, "International Private Law").
[14] Article 54 of the International Private Law.
[15] Pursuant to Article 54 of the International Private Law.

There is no treaty between England and Turkey providing for reciprocal enforcement of judgments, however there is authority to suggest that there is de facto reciprocity[16]. Therefore, a judgment rendered against a Turkish entity by a court in England should be recognised and enforced by the courts in Turkey without re-examination of the issues subject to satisfaction the conditions listed above.

Enforcement of foreign arbitral awards in Turkey

An arbitral award shall be recognised by a Turkish court subject to the provisions of the New York Convention and Articles 60 to 63 of the International Private Law. According to these provisions, a Turkish court shall not enforce an arbitral award, in the event that one of the following conditions of the International Private Law occurs:

- There is no valid written arbitration agreement or arbitration clause
- The arbitral award is contrary to public morals or public policy
- The subject dispute is not capable of settlement by arbitration under the laws of Turkey
- One of the parties was not duly represented before the arbitrators and did not expressly give its consent to the proceedings thereafter
- The party against whom the enforcement of the arbitral award is requested was not given proper notice of the appointment of the arbitrators or was deprived of its right of claim and defence
- The arbitration agreement or the arbitration clause is not valid under the governing law thereof or, failing any indication thereon, under the law of the country where the arbitral award was rendered;
- The appointment of the arbitrators or the arbitral procedure applied by the arbitrators is in violation of the governing law thereof or, failing any indication thereon, of the applicable law of the place wherein the arbitral award was rendered;
- The arbitral award deals with a dispute not contemplated by the arbitration agreement or the arbitration clause, or it contains matters beyond the scope of such arbitration agreement or arbitration clause,
- The arbitral award has not yet become binding or enforceable in accordance with the governing law thereof or the law of the country where the arbitral award was rendered, or has been set aside by the competent authority of the country where the arbitral award was rendered.

The presence of any of the conditions listed above may constitute a ground for rejection of an enforcement request.

[16] 11th Chamber of Law of Court of Appeals Judgment E. 2007/1335 K. 2007/3808.

Moreover, as both Turkey and the UK have ratified the New York Convention there is a treaty between Turkey and England providing for the reciprocal enforcement of arbitral awards subject to reservations and declarations made by England and Turkey in respect of the New York Convention.

On a separate note; under Turkish law, arbitration and submission to courts of a jurisdiction cannot co-exist in order for an arbitration clause to be valid. The Turkish Court of Appeal has resolved that in the event an agreement provides an "Arbitration and Court-option" jointly, the arbitration provision will be void; the intent of the parties to submit to arbitration must be clear and explicit so as not to give rise to any doubt, and the parties must be determined to have their dispute resolved by arbitration. Therefore, if an arbitration clause is included in an agreement in addition to the jurisdiction of English courts; such arbitration clause would be deemed void.

Regarding the language of the arbitration clause and/or arbitration agreement, the Turkish Court of Appeal refused, in one of its judgments,[17] to enforce an arbitration clause in an English language contract between a Turkish party and a foreign party pursuant to the provisions of the Law on Mandatory Use of Turkish Language by Economic Enterprises (Law No. 805) (*published in the Official Gazette dated April 22, 1926 with no. 353*) (as amended from time to time, the "**Law No. 805**").

In the light of the foregoing, it is recommended to have the arbitration clauses/agreements be prepared both in Turkish and English as per the provisions of Law No. 805.

[17] 11th Chamber of Law of Court of Appeal Judgment E. 2016/5836, K. 2017/4720 and dated 26/09/2017.

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CONTRIBUTORS

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Whilst every care has been taken to ensure the accuracy of the information contained in this pack at the time of publication, the information is intended as guidance only. It should not be considered as legal advice.

If you do have any queries, please contact your usual contact at HFW or any of the contributors listed below:

HFW

Commodities & Charters

Brian Perrott, Partner

Lee Forsyth, Associate

Construction

Ben Mellors, Partner

Aviation

Mert Hifzi, Partner

Paul Woodley, Senior Associate

Ports & Terminals

Alex Kyriakoulis, Partner

Joseph Botham, Associate

Guarantees

Alistair Mackie, Partner

Peter Emery, Senior Associate

Research undertaken by James Neale, Trainee.

Special thanks to the following for their contributions:

Şeyma Inal, Founding Partner, Inal Law

HFW has over 650 lawyers working in offices across the Americas, Europe, the Middle East and Asia Pacific. For further information about our commodities capabilities, please visit hfw.com/commodities

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