

# New Measures to Be Taken By Turkish Companies in Technical Bankruptcy & Financial Distress

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The Ministry of Trade introduced the *Communiqué on the Implementation of Article 376 of the Turkish Commercial Code Numbered 6102* (“**Communiqué**”) detailing the measures to be implemented in companies subject to technical bankruptcy.

## What’s New?

The Communiqué provides helpful guidance about how companies and their shareholders and management must address a company’s financial distress.

The principal change introduced by the Communiqué is the option it gives companies not to take into consideration certain foreign exchange losses when calculating the loss of capital or insolvency under the TCC.

## Technical Bankruptcy & Financial Distress under the Turkish Commercial Code (“TCC”)

Article 376 of the TCC imposes obligations on the shareholders and management of companies to take certain measures to address the company’s technical bankruptcy or financial distress.

The TCC foresees the following:

- |                     |   |
|---------------------|---|
| <b>Capital Loss</b> | <ul style="list-style-type: none"> <li>If the last annual balance sheet of the company shows that ½ of capital (when taken together with its statutory reserves) has been lost, then the board of directors must promptly convene the general assembly of shareholders. At this meeting, the board of directors must present certain measures to rectify the financial distress.</li> <li>If the last annual balance sheet of the company shows that 2/3 of the capital (when taken together with its statutory reserves) has been lost, then the board of directors must promptly convene the general assembly to decrease the company’s share capital to 1/3 or less of its statutory capital or to replenish the company’s capital back to its pre-loss amount.</li> </ul> |
| <b>Insolvency</b>   | <ul style="list-style-type: none"> <li>The board of directors must prepare an interim balance sheet based on the fair market value of the assets if there are signs that the company is insolvent (e.g. if the company is not able to pay its debts to creditors).</li> <li>If it is clear from such interim balance sheet that the company’s assets are not sufficient to cover its debts, then the board of directors of the company must notify this situation to the commercial court of first instance where the headquarters of the company is located and seek the bankruptcy of the company unless the situation can be cured with the options available in Article 376.</li> </ul>   |

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## The Communiqué

The new Communiqué supplements Article 376 of the TCC by regulating how companies will implement the above-listed options in cases of capital loss or insolvency. The Communiqué:

- provides that the remedial proposals to be made by the board in cases of loss of  $\frac{1}{2}$  of capital may include (i) replenishment of the company's capital to its pre-loss amount, (ii) share capital increase, (iii) closing or downsizing of certain production units, (iv) sale of subsidiaries, (v) changing the marketing system of the company and the like; and
- elaborates how capital is to be replenished in case of  $\frac{2}{3}$  capital loss. This replenishment of capital is not an advance payment of capital nor can it be treated as a loan and be repaid to shareholders.

### 1) Calculation Principles on FX-debt

- Until January 1, 2023, when calculating loss of capital or insolvency under Article 376 of the TCC, companies can disregard foreign exchange losses arising from foreign exchange denominated obligations that have not yet been performed or paid. In the past, all foreign exchange losses on foreign exchange denominated obligations, paid and unpaid, had to be recognized when calculating loss of capital or insolvency under the TCC.
  - *Example:* A company has USD 100,000 in foreign exchange debt on January 2, 2018, when 1 TL was equal to 3.77 USD. It pays \$40,000 on September 17, 2018 when 1 TL was equal to 6.27 USD. In calculating its capital loss, the company will have to recognize the exchange rate loss relating to the \$40,000 already paid (or TL 250,800). However, it has the option not to reflect the exchange rate loss relating to the unpaid \$60,000 (or TL 376,200) in a calculation made in respect of September's balance sheet.
- How the F/X-losses resulting from the re-denomination of F/X-denominated contracts pursuant to another [recent change](#) in the F/X regulation should also be addressed with further guidance.

### 2) Exception to the agenda of a general assembly meeting

- If a company has lost  $\frac{2}{3}$  of its capital (when taken together with its statutory reserves), its general assembly of shareholders must discuss this issue during any upcoming general assembly meeting even if the company has convened the meeting with an entirely different agenda.

### 3) Option to follow Turkish Accounting Standards ("TAS")

- A company's state of capital loss or insolvency should be assessed on the basis of financials based on TAS. This allows companies, who are not subject to independent audit requirements to opt into TAS for the purposes of Article 376 of the TCC if such assessment will not result in capital loss or insolvency.

## Key Considerations

The Communiqué offers interim relief to companies by offering them the option to postpone recognition of exchange rate losses on unpaid foreign exchange obligations. As a result, these companies may avoid the consequences of falling within the scope of Article 376 of the TCC to take the required measures relating to file for bankruptcy. This may give companies breathing room until their economic performance improves or as they pursue financial restructuring. In addition to the benefit noted above, the Communiqué offers clearer and more detailed guidance on the process to be followed under the TCC in the event a company has lost between  $\frac{1}{2}$  and  $\frac{2}{3}$  of its capital or is insolvent.

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