MARKET OVERVIEW

The Annual Turkish M&A Review 2018 by Ernst & Young reports that somewhere around 191 transactions were closed in 2018, with a total value of $9.3 billion. Leading sectors for the M&A market in 2018 were IT, financial services, energy and health. While the financial services sector hosted the highest level of deal activity in terms of deal value, the IT sector led in terms of deal numbers. Investors from the United Arab Emirates (UAE) were the most active acquirors with a total value of $3.1 billion across 13 transactions.

M&A activity

M&A values increased significantly in 2018 as compared to 2017. Additionally, similar to 2017, during 2018 numerous small and mid-sized transactions were closed. While foreign investors’ involvement decreased in deal numbers, in terms of deal value it increase by almost 40%.

The market was dominated by private M&A transactions in 2018, again similar to 2017. A total of 18 privatisations with a total value of $1 billion were completed, while private transactions had a total value of $8.3 billion. Privatisations corresponded to 11% of total M&A transaction values.

TRANSACTION STRUCTURES

The IT, financial services, energy and health sectors were all active over 2018. While the IT sector led deal activity in terms of volume, the financial services sector led in terms of deal values. The UAE was the most active single origin market for inbound foreign acquirors.

Financial investors

Financial investors grant certain standards to both target companies and M&A transactions. However, during 2018, economic and security related uncertainty caused a decrease in foreign investors’ interest in
Turkey. Accordingly, financial investors’ participation in M&A transactions decreased significantly, both in volume and value. The Annual Turkish M&A Review 2018 by E&Y reports that financial investors’ involvement decreased from 33% to 21% by deal number, as compared to 2017.

Recent transactions

The change of control and acquisition of the shares of 54% of Turk Telekom was one of the most significant deals. The most interesting aspects related to the involvement of foreign and domestic banks and other financial institutions, as well as regulatory bodies. Turk Telekom is a public company active in the telecommunication sector. The control of Turk Telekom was obtained by enforcement of pledges through a provision (Article 47 of Capital Markets Law No. 6362, Official Gazette December 30 2012 No. 28513 (Capital Markets Law)) concerning contracts of collateral relating to capital markets instruments. This transaction has been the first significant implementation of such provision. Additionally, the Turk Telekom deal was one of the largest deals in terms of value in 2018. Lastly, the Competition Board of the Republic of Turkey resolved that the transaction is not subject to its approval, as the change of control was obtained through Article 47.

LEGISLATION AND POLICY CHANGES

The key piece of legislation governing private M&A activity is the Turkish Commercial Code No. 6102, Official Gazette February 14 2011 No. 27846 (Turkish Commercial Code) for privately held companies. The Capital Markets Law provides the key framework for public company acquisitions.

The Law on Protection of Competition No. 4054, Official Gazette
December 13 1994 No. 22140, also governs certain M&A transactions depending on the value of the transaction and the dominance of the parties involved. Accordingly, certain transactions regulated under the Communiqué on Mergers and Acquisitions are subject to clearance by Turkish Competition Authority No. 2010/4.

In this regard, depending on the sector involved in a transaction, approvals from different regulatory bodies may be required.

**Recent changes in law**

On December 6 2018, an amendment on a mandatory mediation system for commercial disputes was introduced. Accordingly, pursuing mediation procedures for a commercial dispute (ie disputes concerning the collection of receivables and compensation) is stipulated as a condition for trial.

Additionally, in accordance with the facilitation of investment policies of the Turkish Government, certain trade registry procedures have been amended.

**Regulatory changes under discussion**

Certain significant amendments to the limitations on foreign exchange transactions have been made. Accordingly, pursuant to the amendment to Article 4 (Foreign Currency) of Decree No. 32 regarding the Protection of the Value of Turkish Currency, Turkish residents cannot enter into any contract amongst themselves in any type of movable and immovable property lease, leasing, employment, service and construction matters, including purchase and sales contracts for movable and immovable property, vehicle rental and financial lease contracts; whereas, price and other contractual payment obligations are determined in foreign currency, or indexed to a foreign currency. Furthermore, certain transactions with an element of foreignness are exempted from such limitations. Accordingly, (i) the service contracts concerning services that commence or are completed abroad; (ii) the immovable sale and lease contracts to which Turkish residents who are not Turkish citizens; or branches, offices, representative offices and liaison offices of foreign companies located in Turkey; or companies located in Turkey in which foreigners have 50 % or more direct or indirect shareholding or joint control and/or control, are parties as buyer, lessee or independent contractor, and lastly, (iii) the contracts which include foreign currency costs, are exempted from such limitations on foreign exchange transactions.

**MARKET NORMS**

The discrepancies between common law and civil law give rise to various misconceptions about the Turkish M&A market. The use of some boilerplate provisions of Turkish law (such as good faith and fair dealing, frustration or force majeure) in an English law-governed agreement creates problems of interpretation.

**Frequently overlooked areas**

The obligation to use the Turkish language is usually overlooked and disregarded. Recently, the Court of Cassation ruled that Law No. 805 on the Mandatory Use of the Turkish Language in Commercial Enterprises (Law No. 805) should have been considered in determining the validity of arbitration agreements. It opined that a Turkish party may not be allowed to base its jurisdictional objection on an arbitration agreement drafted in a language other than Turkish. Law No. 805, which constitutes the grounds of this decision, was accepted on April 10 1926, and introduced several obligations on Turkish commercial enterprises concerning the usage of Turkish. While Law No. 805 had been interpreted not to be applicable to those transactions having a foreign party, through the decision of the Court of Cassation the scope of implementation of the Law No. 805 has expanded.

Additionally, dispute resolution has been overlooked during the negotiation of deals. Consequently, in the event of a dispute between the parties, the delay in the decision-making process of the courts causes parties to face additional financial losses.

**PUBLIC M&A**

The main legislative text governing public companies is the Capital Markets Law. According to the Capital Markets Law, public companies that either have more than 500 shareholders or are publicly traded, are joint stock companies.

Pursuant to Article 12 of Communiqué on Takeover Bids No. II-26.1, Official Gazette No. 28891 of January 23 2014 (Communiqué on Takeover Bids) issued by the Capital Markets Board, control is defined as holding either or both of over 50% of the voting rights of a corporation, directly or indirectly, and/or privileged shares enabling their holder to appoint the simple majority of the members of the board of directors, or to nominate such majority of directors in the general assembly meeting.

**Conditions for a public takeover**

Pursuant to Article 11(4) of the Communiqué on Takeover Bids, a mandatory takeover bid cannot be subject to any conditions. However, under Article 20 of the Communiqué on Takeover Bids, a voluntary takeover bid may be submitted for all or some of shares of a publicly held corporation. If a voluntary takeover bid is submitted for some of the shares, and the number of shares covered by the demands for participation in the takeover bid is greater than the number of shares covered by the takeover bid, then the voluntary takeover bid process is conducted in accordance with a pro rata distribution method, in order to eliminate any inequality between the demanding shareholders. Since the form to be submitted to the Capital Markets Board requires the bidder to submit information on the conditions of a bid, it is implied that certain restrictions may be imposed on voluntary takeover bids upon the approval of the Capital Markets Board.

Furthermore, under the Communiqué on Material Events Disclosure No. II-15.1 (Official Gazette, January 23 2014, No. 28891), tender offers and public takeovers are subject to certain disclosure requirements.

It is also noteworthy that following the enactment of Law No. 6728, a 10% threshold has been determined for purposes of defining a related party with regard to transfer pricing requirements. In the meantime, the threshold for the rate of shareholding that can be subject to buyback by a company respecting its own shares is 10% under the Turkish Commercial Code.
Break fees

There is no specific regulation on break fees under capital markets legislation. Therefore, the Turkish Code of Obligations No. 6098 (Official Gazette, February 4 2011, No. 27836 (TCO)), is applicable. There is no restriction with regard to break fees under the TCO between merchants.

Especially in private deals, where the target is sold by means of a tender, break fees are frequently used for violation of exclusivity or lack of closing, for instance, with unsuccessful tenders. However, break fees are not very commonly seen in public M&A deals.

PRIVATE M&A

As per Turkish private M&A markets, purchase price adjustments have been the most popular mechanism for pricing and payment.

Recently, the locked box mechanism has been offered by a greater number of sellers, where a correspondingly increasing number of buyers accepted this alternative consideration mechanism.

On the other hand, the earn-out method has not been resorted to as commonly as locked box mechanisms and have been used more generally for partial share acquisitions, where one of the parties maintains its presence in the target.

Finally, an escrow mechanism has been seldom seen in the Turkish M&A market, since Turkish banks are not very enthusiastic about the application of such a mechanism and its facilitation.

Conditions for a private takeover

The most common conditions precedent for private takeover offers are regulatory authority clearances and approvals from regulatory authorities. Among these clearances and approvals, the most ubiquitous condition precedent is merger clearance from the Turkish Competition Authority. There might also be regulatory authority clearances required from other regulatory authorities, such as the Energy Market Regulatory Authority and Information and Communication Technologies Authority designated as conditions precedent, depending on the activities of the target companies.

Another often-used type of condition precedent is the approval or consent of third parties, where a change of control clause requires such approval or consent, with regard to the contracts and where the buyer will become a party. In relation to such consent/approval, if the target company holds certain licences or permits, such as an electricity distribution licence, approval must be obtained for certain changes in the shareholding structure of the licence-holder target company.

Other examples of conditions precedent are the resignation of the current board structure of the target company and its replacement with new members appointed by the buyer; undertakings with regard to the post-signing and pre-closing interim period; the disclosure of transactions out of ordinary course of business during an interim period; the transfer of loan agreements and security agreements in connection with the loans; exclusivity and break fees with regard to such exclusivity; and non-occurrence of material adverse events.

Foreign governing law

Under Turkish law, parties to an agreement having an international element may choose the governing law for the agreement. The choice of Turkish law as the governing law for Turkish target companies is the general market practice. However, during recent years, it has become increasingly more common that a foreign, non-Turkish, jurisdiction was designated as the governing law in order to eliminate the difficulties of recognition and enforceability of court decisions. In addition, arbitration has become more preferable as the means of dispute resolution, including both international commercial arbitration, such as the ICC and Uncitral arbitrations, and arbitration through the recently established Istanbul Arbitration Centre.

The exit environment

IPOs have been the most common exit strategy for transactions in which financial investors are involved. Additionally, option agreements are common. However, enforceability of option agreements under Turkish law is questionable.

OUTLOOK

No increase to M&A transactions is expected during the first half of 2019; however, there may be an increase in the second half of 2019. Accordingly, the Turkish M&A market is anticipated to be advantageous for long-term investors.