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Amendments To The Laws Regarding Real Estate Acquisition In Turkey **By Foreign Capital Companies**

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The provisions of Turkish Law relating to real estate acquisition by foreign capital companies have been significantly amended during this legislative year. On November 12, 2008, the government published a regulation outlining the implementation of the amendments. The aim of this paper is to briefly explain the new procedure introduced by the regulation.

Background

1. Previous provisions governing real estate acquisition by foreign capital companies.

Real Estate acquisitions by foreign capital companies, i.e. companies that are incorporated with foreign capital in Turkey in accordance with Turkish Law, or Turkish companies participated in by foreign investors (“foreign capital companies”)¹, were previously governed by Article 3(d) of the Foreign Direct Investment Law (“FDI Law”). According to Article 3(d) of the FDI Law, foreign capital companies were allowed to acquire real estate and limited rights *in rem* under the same conditions as those applied to Turkish citizens.

However, on April 16, 2008 the Constitutional Court annulled Article 3(d) of the FDI Law. On July 3, 2008 the legislature promulgated a new law to amend Article 36 of the Land Registry Law (“New Law”) to address foreign capital companies wishing to acquire real estate or limited rights *in rem* in Turkey.

2. The amendments introduced to article 36 by the new law.

According to the New Law amending Article 36 of the Land Registry Law, foreign capital companies may acquire real estate and limited rights *in rem* when the real estate or limited rights *in rem* are needed to carry out the activities of the company as designated in their Articles of Association (“AoA”). This rule is also applicable in cases where real estate acquired by such companies is transferred to another foreign capital company or where

¹ Full definition of the foreign capital companies is contained in the Foreign Direct Investment Law

domestic companies formed with domestic capital that own real estate are transformed into foreign capital companies by share transfer.

If a foreign capital company owning real estate is subject to liquidation and the real estate is intended to be acquired by the foreign real or legal persons co-owning the said company, Article 35² of the Land Registry Law shall also apply.

Article 36 also stipulates that foreign capital companies wishing to acquire real estate and limited real rights *in rem* located (i) in a military prohibition zone, security zone or strategic zone must obtain Turkish General Staff or Commandership permits or, (ii) in a private security zone must obtain permission from the governorship.

Real estate and limited rights *in rem* acquired or utilized in a way that breaches Article 36 shall be liquidated according to the instructions given by the Ministry of Finance. Otherwise, it will be liquidated and the proceeds shall be given to the owners.

The New Law sets forth that Article 36 will be implemented by regulations to be published by the Undersecretariat of Treasury, the Ministry of Internal Affairs and the Ministry of Public Works and Settlement. In order to provide guidance until the said regulation was published, the General Directorate of the Land Registry published a circular on July 17, 2008. The circular stated that acquisition of real estate and limited rights *in rem* by foreign capital companies is subject to permissions obtained from the governorships. However, as there was no regulation in place outlining the principles for such permission, governorships were reluctant to issue any permission and consequently, the realisation of real estate transactions involving foreign capital companies was brought to a halt.

On November 12, 2008, the regulation regarding the acquisition of real estate and limited rights *in rem* by foreign capital companies (the “Regulation”) was published and is now effective. Consequently, the realisation of real estate transactions involving foreign capital companies which, prior to the Regulation temporarily drew to a halt, is expected to resume.

The Regulation

1. The permission requirement and the commission.

According to the Regulation, foreign capital companies will only be permitted to acquire real estate and limited rights *in rem* upon obtaining permission from the governorships. Such permission will be subject to (i) whether the transaction is necessary to carry out the activities of the company as designated in their AoA and (ii) whether the real estate sought to be acquired is located in any of the specific zones explained below.

² Article 35 of the Land Registry Law sets forth the main principles (reciprocity rule and all legal restrictions) regarding real estate acquisition by foreign real and legal persons.

The Regulation stipulates that governorships shall establish a commission (the “Commission”) to deal with such permissions. The Commission shall consist of officers from different governmental bodies such as the relevant cadastre office, Provincial Directorate of Trade and Industry, etc., and is obliged to convene at least twice a month if an application has been made.

2. The scope of the Commission’s Assessment.

In accordance with the foregoing, the Commission’s assessment, when deciding to give permissions, shall include whether the real estate transaction is necessary for carrying out the scope of activities designated in the company’s AoA and whether the real estate in question is located in a military prohibition zone, military security zone, strategic zone or private zone. Further, aside from the acquisition of real estate by foreign capital companies, acquisition of limited rights *in rem* by foreign capital companies is also subject to the permission procedure.

It should be noted that there is no exemption in the Regulation for hypothecs created in favour of such companies. In Article 35 of the Land Registry Law, where all the restrictions are set forth regarding real estate acquisition by foreign real or legal persons, hypothecs to be established in favour of foreign real or legal persons are exempted from such restrictions. However, lawmakers made no exemption in this regard in Article 36. Effectively this means that a hypothec established in favour of a company incorporated under the laws of a foreign country is not subject to any restrictions whereas a hypothec established in favour of a foreign capital company incorporated under the laws of Turkey will be subject to some restrictions.

As this inconsistency has the potential to block transactions of banks subject to the FDI Law, the General Directorate of the Land Registry issued a circular (the “New Circular”) on November 20, 2008. According to the New Circular, if an application is made to establish a hypothec in favour of a bank which is subject to the FDI Law, the bank is required to obtain a one-time permission from the Governorship of the city in which the bank’s headquarters is located. The one-time permission makes it unnecessary for the bank to apply for permission for each subsequent transaction.

3. The application and assessment procedure.

It is stated in Article 4 of the Regulation that applications for permission to acquire real estate and/or limited rights *in rem* shall be made by the foreign capital company together with the following documents:

- a. A written statement of the objectives for such a transaction and information regarding the real estate;
- b. A written statement indicating that the applicant is permitted to conclude real estate transactions and the details of its representatives;
- c. The tax office and tax number of the applicant;
- d. A recent written statement (not older than one month) obtained from the relevant Trade Registry indicating the scope of activities of the applicant designated in its AoA and information on the shareholders (names, nationalities, their shareholding, etc.);

- e. A notarized written statement of identification of the foreign real person shareholders and/or a duly approved written statement regarding the scope of activities of the foreign legal person shareholders;
- f. The names, addresses and identifications of the managers of the company; and
- g. Last three years' balance sheet (if any).

For applications made for the acquisition of limited real rights *in rem*, the documents stated in (e), (f) and (g) above are not required.

It should be noted that additional documents and/or information may be requested by the relevant authorities during the course of their evaluation.

The New Circular also stipulates that if a company submits to the Land Registry Office a certificate of authority to purchase real estate which does not state whether the company is subject to the FDI Law, the official deed for the sale transaction (to be prepared by the Land Registry Office) must clearly state that the company acquiring the real estate is not subject to the FDI Law. If it is subsequently discovered that the company is in fact subject to the FDI Law the real estate acquired shall be liquidated in accordance with Article 36 of the Land Registry Law.

Pursuant to Article 5 of the Regulation, following application by a foreign capital company, the Commission shall obtain written opinions from various governmental entities. Article 5 does not specify a timeframe in which the Commission must request the written opinions. It should be noted, however, that Article 5 does clearly state a timeframe in which the governmental entities must reply to the Commission's request:

- a. within 7 days from the Provincial Directorate of Trade and Industry as to whether the scope of activities of the applicant requires such real estate acquisitions;
- b. within 30 days from the Turkish General Staff or Commandership as to whether the real estate is located in a military prohibition zone, security zone or strategic zone and if so, whether such transaction is permissible; and
- c. within 20 days from the General Directorate of Security as to whether the real estate is located within a private security zone.

The Regulation also states in the same article that the timeframe for obtaining the written opinions aforementioned starts when the written request for the opinion is received from the Commission by the relevant authorities. According to Article 9, in cases of acquisition of limited rights *in rem* by foreign capital companies, the Commission will carry out its assessment based on the written opinion obtained by the Provincial Directorate of Trade and Industry in accordance with (a) above.

Upon finalization of its assessment based on the opinions received, the Commission shall inform the applicant accordingly. Where the real estate is located within a military prohibition zone, security zone or strategic zone any disapproving opinions made by the General Staff or

Commandership shall be deemed final. If the real estate is located in a private security zone, the Commission shall make its own assessment and decision based on the opinions of the relevant authorities.

It should be emphasized that, as stated above, there is no time specification as to when the written request for opinions shall be sent by the Commission to the above mentioned authorities after the application has been made. There is also no specification as to when the applicant will be informed once the result of the Commission's assessment becomes clear. This, therefore, makes it difficult to envisage how long the permission procedure may actually take.

4. Other transactions requiring permission.

The Regulation also sets forth the principles regarding implementation of Article 36 in cases where domestic companies (formed with domestic capital) that own real estate are transformed into foreign capital companies by way of share transfer and in cases involving any kind of new foreign participation in existing foreign capital companies.

Pursuant to Article 11 of the Regulation, the Undersecretariat of Treasury³ shall inform the General Directorate of Land Registry on a monthly basis of any domestic companies (formed with domestic capital) owning a real estate that are transformed into foreign capital companies by way of share transfer. The General Directorate of the Land Registry shall then inform the governorship of the real estate owned by such companies and consequently, the Commission will assess whether those companies are able to hold the title to the real estate according to same procedures stated above.

The Regulation also provides that any new foreign participation into an existing foreign capital company shall be subject to the above mentioned process. However, in this case, the governorships are not required to request the opinion of the Provincial Directorate of Trade and Industry.

5. Post-acquisition.

In accordance with Article 13 of the Regulation, the Commission is also entitled to assess whether the real estate or limited rights *in rem* acquired by a foreign capital company is being used in accordance with the scope of its activities as designated in its AoA. The Commission may make such an assessment at its sole discretion or upon written application by real or legal persons.

If any non-compliance is detected, the Commission may allow the company a certain period of time to change how it utilizes the real estate or rights so that it is in accordance with its AoA. Failure of the foreign capital company to comply with the Commission's instructions

³ Under Turkish Law, these types of transactions are notified to the Undersecretariat of Treasury

may result, after an assessment pursuant to Article 13 of the Regulation, in application of the liquidation process mentioned below.

6. Violations and sanctions.

Real estate and limited rights *in rem* acquired or utilized in a way that is contrary to Article 36 and the Regulation will result in the owner having to liquidate the real estate or the limited rights *in rem* within 6 months. This period may be extended for an additional 6 months provided a valid reason is presented. Should the owner fail to liquidate the real estate or limited rights *in rem* within the given time period, the Ministry of Finance will proceed with the liquidation and will deposit all proceeds (net of costs incurred for the liquidation procedure) into a bank account opened in the name of the owners.

7. Conclusion.

In conclusion, the following points should be emphasised:

- There remains some uncertainty regarding the time limits provided in the Regulation. Therefore, it will take a while before the Regulation can be smoothly implemented and during this period there may be some instability.
- The Regulation provides that a foreign capital company wishing to acquire real estate and limited rights *in rem* is to apply to the governorship, whereas the expectations were that the land registries would be responsible for making such applications to the governorship. Therefore, for transactions that are currently suspended, foreign capital companies should restart the application procedure.
- The Regulation requires that the application be made together with a written statement by the foreign capital company indicating the objectives of such a transaction. No information is provided, however, with respect to how the assessment of the said statement will be made. There is a risk, therefore, that assessments may be subjective due to different approaches being employed during the review process.
- As a result of the major changes that have occurred relating to acquisition of real estate or limited rights *in rem* by foreign capital companies, it is paramount for foreign capital companies to consider the Regulation during establishment and framing of their AoA.
- As stated above, the Regulation, unlike Article 35 of the Land Registry Law, contains no exemptions for hypothecs established in favour of foreign real or legal persons. The New Circular introduced the possibility for banks subject to the FDI Law to apply for a one-time permission. It is important to note that the New Circular only mentions “banks subject to the FDI Law” and does not recognize any other type of financial institutions, credit providers or mortgage companies.

We assume that any uncertainties with regard to the application of the Regulation will be clarified in due time, most likely, the General Directorate of the Land Registry will issue additional circulars to address the existing issues.