

## MEMORANDUM

### Types of Business Entities in Turkey

In accordance with UNCTAD World Investment Report 2011, Turkey, along with China, is cited as one of the two most popular destinations for foreign direct investments from transition economies. It is further reported by UNCTAD under Investment Country Profiles – Turkey February 2012 Report that the number of foreign affiliates in Turkey was 3,300 in 2010.

As per Turkish foreign investment legislation, foreign investors benefit from equal rights and equal treatment principles with Turkish investors. Therefore, it is possible for foreign investors to incorporate all types of business entities prescribed by the law. A foreign investor is entitled to establish a business entity on its own or with Turkish nationals of natural or legal personality in Turkey.

The main sources of law to be observed in terms of business entities are the Turkish Commercial Code dated February 14, 2011, numbered 6102 (the “**TCC**”); the Foreign Direct Investments Law dated June 05, 2003, numbered 4875 (the “**FDIL**”); and the Turkish Code of Obligations dated February 04, 2011, numbered 6098 (the “**TCO**”).<sup>1</sup>

Turkish legislation defines foreign direct investment as (i) establishing a new company or branch of a foreign company by foreign investor; or (ii) acquisition of shares of a company established in Turkey (any percentage of shares acquired outside the stock exchange or 10% or more of the shares or voting power acquired through the stock exchange) by means of certain economic assets listed under relevant law. For the purpose of this note, item (i) above will be analyzed limited to the types of business entities applicable in Turkey.

Among other methods of classification, actors of commercial life in Turkey are subject to differentiation according to whether they are of natural personality or legal personality. Natural persons may act as i) Ordinary Partnerships (*Adi Ortaklık*) or ii) Sole Proprietorships (*Gerçek Kişi Ticari İşletmesi*) whereas legal persons may be incorporated as i) Joint Stock Companies (*Anonim Şirket*), ii) Limited Liability Companies (*Limited Şirket*), iii) Limited Partnerships (*Komandit Şirket*), iv) Registered Partnerships (*Kollektif Şirket*) or v) Limited Partnerships Divided into Shares (*Sermayesi Paylara Bölünmüş Komandit Şirket*). It is also

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<sup>1</sup> Many of the fundamental legislation has undergone material amendments within last decade in line with the European Union harmonization process of Turkey. The Turkish Commercial Code dated June 29, 1956, numbered 6762 (the “**pTCC**”) and the Turkish Code of Obligations dated April 22, 1926, numbered 818 (the “**pTCO**”) were in force to a very recent date. Certain provisions of this previous legislation is still in force for a transition period.

possible for foreign companies to establish branches (*şube*), liaison offices (*irtibat bürosu*) and agencies (*acente*) in Turkey.

## **1. Natural Person Entities**

### **1.1.Ordinary Partnerships**

Ordinary partnerships are regulated under the TCO. Ordinary partnerships are unions void of legal personality where two or more natural or legal persons contribute with their assets and labor for the purpose of accomplishing a common goal. Partners of an ordinary partnership may contribute in the partnership in amounts, types and proportions they agree upon. Partners share the profits and losses of the partnership proportionate to their contribution unless otherwise agreed. They are subject to non-competition provisions as per the TCO. Decisions within the partnership are adopted unanimously unless otherwise agreed. Although an ordinary partnership does not have a legal personality, it is subject to corporate tax whereas not the partnership itself but the partners thereof are subject to income tax. Ordinary partnerships are not obliged to be registered with the trade registry, however, may do so upon demand of its partners. In practice, ordinary partnerships, with the exclusion of joint ventures which are also subject to provisions governing ordinary partnerships, are not common and preferred vehicles for foreign investment in Turkey.

It is however noteworthy to state that any company failing to satisfy the statutory conditions to qualify as a certain type of company subject to the relevant provisions of the TCC under Turkish law, would be deemed as an ordinary partnership.

### **1.2.Sole Proprietorships**

Sole proprietorship is a type of vehicle convenient rather for small-scale business activities, therefore, not advised as foreign investment instruments. Craftsmen and artisans in accordance with the Law numbered 5362, merchants in accordance with the TCC, self-employed single persons are examples of sole proprietorships in Turkey. Sole proprietorships are registered with the Trade Registry or Merchants and Craftsmen Registry.

## **2. Legal Person Entities**

### **2.1.Joint Stock Companies**

Along with the limited liability companies, one of the most common types of business entities preferred by foreign investors in Turkey is joint stock companies due to the organization thereof as well as the developed corporate governance principles applicable. Secondary legislation of the TCC regarding joint stock companies deserve separate analyses, besides; many of these regulations are not yet published since the TCC has recently entered into force.

Liability of shareholders of a joint stock company is restricted with the amount of share capitals they have contributed in the company. Upon enactment of the TCC, joint stock companies are allowed to be incorporated by and between one or more

# ÇETİNEL

shareholders of Turkish or foreign natural or legal person shareholders. Minimum capital requirement is TRY 50,000.-; and TRY 100,000 for joint stock companies adopting registered capital system. Mandatory bodies of a joint stock company are the General Assembly and the Board of Directors. Absolute authorities of the General Assembly and the Board of Directors are enlisted under the TCC. At least one member of the Board of Directors is required to be a Turkish national residing in Turkey. All joint stock companies are expected to comply with the Turkish Accounting Standards. Independent audit, transactional audit and special audit of joint stock companies are stated under the TCC. Until the entry into force of the provisions regulating new auditing system in joint stock companies, namely January 01, 2013, auditor(s) is a mandatory body of the joint stock company in accordance with the pTCC.

Whether or not the incorporation of a joint stock company is subject to the permission of the Ministry of Science, Industry and Technology depends on field of activity of such joint stock company. However, no distinction between Turkish investors and foreign investors in terms of acquiring permission of the Ministry of Science, Industry and Technology is applicable.

All joint stock companies are required to build a website containing corporate and financial information related thereto until July 01, 2013.

All joint stock companies are registered with the Chamber of Commerce and Trade Registry located in the headquarters thereof. Joint stock companies are fully subject to corporate tax.

Having mentioned that the provisions governing joint stock companies are rather detailed and comprehensive, it is noteworthy to mention that upon enactment of the TCC, certain unprecedented issues emerged in terms of joint stock company legislation in Turkish legislation. Certain innovations such as (i) single person joint stock companies, (ii) group companies (provisions especially aiming to protect the shareholders and creditors that remain outside of the group) and (iii) removal of *ultra vires* doctrine in terms of joint stock company transactions are result of the TCC's aim of facilitating joint stock company activities and such innovations are expected to remove or at least reduce procedural obstacles hindering business activities. On the other hand, certain monetary fines and imprisonments stipulated for shareholders and members of the Board of Directors of joint stock companies included in the recent codification deserve significant emphasis. Strikingly, shareholders are not allowed to become indebted to the company unless they pay their due share capital in full and profit and reserves of the company can cover previous years' debts. Similarly, members of the Board of Directors, enlisted relatives thereof, companies in which such member is a shareholder of may not become indebted to the company as well. Otherwise, respective shareholders and Board of Directors members are subject to considerable monetary fine.

## **2.2.Limited Liability Companies**

Limited liability companies are regulated under the TCC. Similar with the joint stock companies, the limited liability companies are also enabled to be incorporated with

# ÇETİNEL

one shareholder upon the entry into force of the TCC. Shareholders of a limited liability company are responsible from the debts of the company restricted with their share contribution, along with certain additional and secondary payment obligations set forth in accordance with the TCC. It is substantial to mention that is the public debts including tax debts of a limited liability company which may not be satisfied by the company itself, the shareholders thereof are directly responsible from such debts separate from such shareholder's liability to pay their capital contribution to the company. Therefore, each shareholder is liable from the public debts of limited liability company in amount of the share capital of the company, proportionate to their share contribution. Minimum share capital of a limited liability company is TRY 10,000.00-. Any limited liability company incorporated in accordance with the pTCC with share capital less than TRY 10,000.00- will be required to increase their share capital to TRY 10,000.00- within 3 years as of the date of issue of the TCC, namely February 14, 2011. Limited liability companies are managed and represented by their Managers appointed by the shareholders. Above explanations pertaining to auditing of the joint stock companies are applicable to limited liability companies. Likewise, limited liability companies are also required to build a website containing corporate and financial information related thereto until July 01, 2013.

All limited liability companies are registered with the Chamber of Commerce and Trade Registry located in the headquarters thereof. Limited liability companies are fully subject to corporate tax.

## **2.3.Limited Partnerships**

Limited partnerships, which are personal entities having legal personality under a trade name in accordance with the Turkish legislation, are governed by the TCC. These partnerships are composed of combination of two different types of liability regimes in terms of their partners; unlimited liability partners (*komandite ortak*) and limited liability partners (*komanditer ortak*). In practice, limited liability partners are those who are seeking for increasing the value of their capital contribution whereas unlimited liability partners hold the management and representation of the partnerships. Under certain exceptional circumstances, liability of limited liability partners of a limited partnership extends beyond the capital contribution of such partner. Limited liability partners, bearing specifications similar to the partners of a registered partnership in many aspects, may not be legal persons. However, a legal person may participate in a limited partnership by being an unlimited liability partner thereof. Limited partnerships are managed and represented by their unlimited liability partners. Limited liability partners may audit the partnership or cause independent auditors to carry out the audit. All limited partnerships are registered with the Chamber of Commerce and Trade Registry located in the headquarters thereof. Limited partnerships are not subject to corporate tax. Valuation of income tax liability of the partners of a limited partnership depends on whether such partner is a limited liability partner or unlimited liability partner.

## **2.4. Registered Partnerships**

Registered partnerships, which have legal personality in accordance with the TCC, may be incorporated by natural person partners each having unlimited joint liability against third persons for the debts and obligations of the registered partnership. Liability of the partners of a registered partnership is determined as secondary liability where the primary liability falls upon the registered partnership itself. Minimum capital requirement is not sought for registered partnerships; however, these partnerships are expected to be capable of operating a business entity in terms of the amount of their capital. Registered partnerships are managed by their directors and represented by their representatives. Directors and representatives of a registered partnership are any and all of the partners of such registered partnership unless otherwise determined by the partners; and one or some of the partners or any third persons are appointed as directors and representatives in the partnership agreement or by a resolution. All partners of a registered partnership bear the right to audit and inspect the partnership books, transactions and decision whether or not such partner is a director or representative. All registered partnerships are registered with the Chamber of Commerce and Trade Registry located in the headquarters thereof. One of the main advantages of registered partnerships is that they are not subject to corporate tax.

## **2.5. Limited Partnerships Divided into Shares**

Limited partnerships divided into shares, very uncommonly encountered in Turkish law, are regulated under the TCC mostly through references to the provisions governing joint stock companies. Certain aspects of such partnerships are similar to joint stock companies and still some other aspects are similar to limited partnerships. One of the main differences between a limited partnership and a limited partnership divided into shares is that, the capital of the latter is divided into shares in a manner similar to the capital of joint stock companies. In terms of minimum capital requirement and corporate bodies within the partnership, limited liability partnerships divided into shares are subject to the provisions governing joint stock companies. These partnerships may be incorporated by and between minimum five partners. Although otherwise asserted to the contrary as well, both limited liability partners and unlimited liability partners of such partnerships may be legal persons. All limited partnerships divided into shares are registered with the Chamber of Commerce and Trade Registry located in the headquarters thereof. These partnerships are subject to corporate tax. Valuation of income tax liability of the partners of a limited partnership divided into shares depends on whether such partner is a limited liability partner or unlimited liability partner.

### **3. Other Entities:**

#### **3.1.Branches**

Branches are semi-independent entities of a natural or legal person in accordance with the TCC. Semi-independence of a branch signifies that the branches are independent from the headquarters in terms of their external relationships concerning the company activities held with third persons; however, dependent to the headquarters in terms of legal personality, profit and loss as well as rights and obligations. A branch has to be entitled with the powers to carry out the fundamental activities of the company. Foreign companies are entitled to establish a branch in Turkey although their headquarters is located abroad. Branch of a foreign company should be registered with the Turkish Trade Registry in the location of the branch within 15 days as of its incorporation. Branches are sought to obtain a separate accounting and commercial books from the headquarters, however, whether it would have a separate capital from the headquarters or not is an issue of commercial preference.

#### **3.2.Liaison Offices**

Liaison offices are governed by the Regulation on Application of Foreign Direct Investments Law. In line with the recent legislation published in the Official Gazette on July 03, 2012, liaison offices are incorporated for a maximum term of 3 years as per the approval of the Ministry of Economy for the purposes excluding carrying out commercial activities. Such term may be extended for an additional 3, 5 or 10 years solely and strictly upon the decision by the Ministry or the liaison offices may be converted to branch or company if and when the activities require so. Liaison offices may be incorporated for exercising marketing and promotion activities, expenses of which should be funded from abroad by the mother company via foreign currency transfers; however, may not exercise activities resulting in invoicing or generating income. Liaison offices are required to report to the Ministry of Economy and be registered with the relevant Tax Office and Social Security Institution in Turkey.

#### **3.3.Agencies**

Agencies, facilitating companies and merchants to carry out their business activities through reducing costs and expenses, are regulated under the TCC. Agencies, established through written or non-written agreements depending on the particulars of the situation, act and execute transactions on behalf and account of the company and merchant they represent. It is noteworthy to mention that in accordance with the TCC, the procedure of application before the Ministry of Science, Industry and Technology is not required for branch incorporation of foreign companies. Whereas the branch managers of foreign company branches are under the obligation to publish the financial statements of the branch in Turkey within six months as of the approval of financial statements of the relevant company in accordance with the legislation governing the foreign company.

# ÇETİNEL

## **4. General Considerations and Statistics on Business Entities in Turkey**

Parallel to any other jurisdictions, several factors such as tax liability, scope of activities to be performed, contemplated minimum capital, personal liability of the partners or the shareholders affect the choice of business entity to be incorporated in Turkey. Statistics on Companies, Cooperatives and Trade Name Establishments 2009 by the Turkish Statistical Institute (TurkStat, *Türkiye İstatistik Kurumu*) reports the figures of business entities incorporated in Turkey in 2009 according to their types as follows:

Type of Business Entity	Number of Business Entity Incorporated in 2009
Joint Stock Company	1881
Limited Liability Company	41550
Limited Partnership	0
Registered Partnership	10
Limited Partnership Divided into Shares	0

Yet another study by the Turkish Chamber of Commerce reports on rather recent numbers of business entities incorporated in Turkey in May 2012 as follows:

Type of Business Entity	Number of Business Entity Incorporated in May 2012
Joint Stock Company	249
Limited Liability Company	2903
Limited Partnership	1
Registered Partnership	8
Limited Partnership Divided into Shares	0

As may be followed from such data, the overall ratio of business entities incorporated in Turkey has increased within time and the types of business entities preferred in Turkey condense on joint stock companies and limited liability companies.

The picture may slightly change upon coming into force of the TCC and TCO in July 1, 2012, however, it should be noted that the foreign investors are not encountering a thoroughly novel situation apart from what is applicable to Turkish investors. This being mentioned, already existing business entities will go under a significant reorganization to comply with the new laws, notably the TCC.