

A Critical Overview of the Law on Movable Pledge in Commercial Transactions

I. Introduction

For maintaining the growth and sustainability of national economy, the Turkish government focused on small and medium-sized enterprises (“SMEs”) and aimed to create a stable and secure economic environment for SMEs. The availability of financing and the lack of different security options were seen as the biggest obstacles for the development and sustainability of the investment environment in Turkey¹. Therefore, increasing financing and different security options has been one of the objectives of the Coordination Council for the Improvement of the Investment Environment. In 2015, the facilitation of security options for SMEs by way of creating security over movables became one of the action items of the 64th Turkish Government’s action plan. It was the starting point of a legislative journey leading to the enactment of Law on Movable Pledge in Commercial Transactions no. 6750 (“the **MPL**”) which abolished the Commercial Enterprise Pledge Law no. 1447 (the “**CEPL**”) and came into force on 1 January 2017. Even though the MPL was brought with an intention to strengthen financing options of SMEs through a new legal framework for movable pledge, it is hard to conclude that the MPL met its objective considering the contradictions between the provisions of the MPL and the relevant principles of civil law and commercial law as well as the vague nature of some provisions of the MPL. Such conflicting provisions and problematic structure of the MPL seem

¹ Ticari İşlemlerde Taşınır Rehni Kanunu Tasarısı (1/753) ile Sanayi, Ticaret, Enerji, Tabii Kaynaklar, Bilgi Ve Teknoloji Komisyonu Raporu 4.

far from increasing the availability of financing for SMEs since it lacks a robust structure to create a reliable security².

II. Issues Regarding the Scope of Parties

Under the CEPL, a commercial enterprise pledge agreement could only be executed between individual business owners and companies on one side and financial institutions on the other side. As opposed to the CEPL, the MPL defines a larger group of business owners as parties. The MPL enables merchants, craftsmen, farmers, producer organizations and self-employed real and legal entities to enter into movable pledge agreements with financial institutions and it also enables merchants and/or craftsmen to establish movable pledge between themselves. This expansion of the scope of parties derives from the intention to enable SMEs to have different financing options rather than financing through banks or other financial institutions.³

While expanding the scope of parties, the MPL failed to solve some longstanding legal controversies which arose in the application of the CEPL. In regards to parties, the CEPL did not include any provision on the consequences of the assignment of the receivable secured by a commercial enterprise pledge, to a party which does not qualify as a party to a commercial enterprise pledge agreement under the CEPL. Similar to the CEPL, the MPL also does not regulate the consequences of such an assignment so as to leave the legal gap to remain unfilled. Therefore, if a secured receivable is assigned to a person that is not eligible to be a party to a movable pledge agreement by application of the law, such person may not be able to benefit from the security.

² Lale Sirmen, 'Ticari İşlemlerde Taşınır Rehninin Düzenleniş Biçimi, Niteliği ve Rehne Hakim Olan İlkeler', *Ticari İşlemlerde Taşınır Rehni Sempozyumu* (Yetkin Basımevi 1. Basım 2018) 22.

³ Zühtü Aytaç, 'Ticari İşlemlerde Taşınır Rehni Kapsamında Taraflar', *Ticari İşlemlerde Taşınır Rehni Sempozyumu* (Yetkin Basımevi 1. Basım 2018) 86.

III. Issues Regarding the Scope of Assets

The MPL broadens the range of assets to be pledged by introducing new asset categories within the scope of movable pledge⁴. These assets include, without limitation, present or future receivables, yielding perennial trees, livestock/animals, raw materials, perishable goods, stocks, and agricultural products. The logic behind these newly introduced asset categories might look similar to the floating charge under English law and might therefore be seen as an advantageous system with the ability of the business to use the underlying asset in the ordinary business operation. However, it is far from creating such a legal concept and establishing its implementation since neither the MPL nor other Turkish laws set out the necessary regulations which could make floating charge advantageous for the parties as in some cases under English law. Therefore, some of those assets, which are expendable or consumable during the normal course of business such as stocks or perishable goods, create a risk to place creditors in a less strong position in time than the one in which they were when the security was created.

On the other hand, the validity of a movable pledge established in accordance with the MPL is debatable due to the fact that some asset categories listed thereunder are subject, as per other special laws, to registration under different registries such as livestock, yielding perennial trees and commercial titles/trade names. Furthermore, the MPL sets forth registration procedures which are in conflict with registration procedures under other special laws. For instance, under the Turkish Civil Code no 4721, ownership and disposal rights of trees over a land are subject to

⁴ 6750 sayılı Ticari İşlemlerde Taşınır Rehni Kanunu (MPL) art 5 para 1.

⁵ Celal Göle and Gökhan Aydoğan, 'Ticari İşlemlerde Taşınır Rehni Kanunu'nun Ticaret Hukuku Açısından Değerlendirilmesi' (2017) 33 Banka ve Ticaret Hukuku Dergisi, 5, 24.

ownership rights of such land⁶. Therefore, establishing a pledge over such trees may be problematic to the inseparable nature of the disposal right of trees and the land. It also brings up another issue in relation to the enforcement of the security when it comes to sell trees as the pledged asset apart from the land⁷.

The MPL provides an option to create a movable pledge separately over each asset as opposed to the CEPL which required the commercial enterprise pledge to be established over the entirety of such enterprise. Therefore, the MPL resolved the discussion regarding the validity of commercial enterprise pledge agreements under which parties thereto failed to include an asset of the enterprise to the list of pledged assets thereunders. However, the MPL introduces a restriction for commercial enterprise pledges in relation to scope of assets, such as to prohibit the establishment of pledges over the entirety of a commercial enterprise if the value of the rest of the assets owned by such enterprise covers the underlying debt⁹. For example, the pledge cannot be established over the entirety of an enterprise having assets which amount USD 1,000,000 or more, if the underlying debt is less than USD 1,000,000. The secondary legislation of the MPL provides for another restriction, conflicting with the MPL, that the value of the assets subject to pledge shall not exceed 120% of the underlying debt if the underlying debt is definite¹⁰. These rule, apart from being contradictory with the secondary legislation, turn out to be more prejudicial to the creditors considering i) the nature of the assets which can be consumed or disposed of or ii) the assets which cannot be liquidated separately as in the case of trees. Creating a limitation on the

⁶ 4271 Sayılı Türk Medeni Kanunu (Turkish Civil Code) art 718 para 2.

⁷ Kemal Oğuzman, Özer Seliçi and Saibe Oktay Özdemir, *Eşya Hukuku* (Filiz Kitabevi 11. Basım 2006) 413.

⁸ Eda Nur Tavukçuoğlu, '6750 Sayılı Kanun Uyarınca Ticari İşlemlerde Taşınır Rehnine Konu Olabilecek Varlıklar' (2018) 92 İstanbul Barosu Dergisi, 111, 112.

⁹ MPL art 5 para 2.

¹⁰ 31.12.2016 tarihli 29935 3. Mükerrer Resmi Gazetede yayınlanan Ticari İşlemlerde Rehin Hakkının Kurulması ve Temerrüt Sonrası Hakların Kullanılması Hakkında Yönetmelik (The Regulation on the Establishment of Security Interest in Commercial Transactions and Post-Default Rights) art 11 para 2.

value of pledged assets, constitutes a burden for creditors since it prevents them from having adequate level of security against their receivables.

IV. Issues Regarding the Good Faith Principle

The MPL sets forth a highly controversial principle of good faith. Since, Article 7 of the MPL states that ‘a third party who does not know or is not required by law to know that a movable is pledged, shall be deemed to be in good faith’. This principle is substantively different than the good faith principle generally accepted under Turkish law¹¹. For example, the Turkish Civil Code no. 4271 provides that a person who knows or is required to know of an unlawful registration, cannot be entitled to any right under such unlawful registration. The MPL, reversing the good faith principle, brings up a scheme that might cause an abuse of the good faith principle¹². Beside such a conflicting regulation, the term “or” under ‘a third party who does not know or is not required by law to know’ part also causes Article 7 to be controversial in itself. It might be interpreted as an “and” in order for Article 7 to make sense. The secondary legislation of the MPL, possibly in an attempt to clarify this article, regulates that a person shall be deemed in good faith i) if such person is not required to review the movables registry or ii) if such person does not have legal capacity to be a party to a movable pledge agreement, and does not know the content of the registry or is not required by law to know the same¹³. However, neither the MPL nor the Regulation on the Movable Pledge Registry determines who is required to review the movables registry. This gap also creates a burden for at least merchants and craftsmen if not for every entity, to check the movables registry each time they conduct an asset disposal transaction.

¹¹ Turgut Öz, 'Ticari İşlemlerde Taşınır Rehni Kanunu' (2017) 16 İstanbul Kültür Üniversitesi Hukuk Fakültesi Dergisi 151, 167.

¹² Sirmen (n 2) 29.

¹³ 31.12.2016 tarihli 29935 3. Mükerrer Resmî Gazetede yayımlanan Rehinli Taşınır Sicili Yönetmeliği (Regulation on the Movable Pledge Registry) art 17 para 2.

Therefore, this vague and inverted good faith principle, which can easily be defeated by a third party, bears a high risk for creditors in case of transfer of the pledged assets by the debtor to a third party.

The problematic good faith structure under the MPL may turn out to be a high risk for creditors considering that the MPL also regulates that any provision of a movable pledge agreement limiting the right of disposal over pledged assets of the owner shall be deemed invalid, which is against the structure of project finance agreements which include limitation on asset sales by the pledger as a usual practice. Such disposal right is not limited to the right of transfer or sale of key assets but any kind of disposal of any assets¹⁴. Therefore, creditors may not be able to direct a claim against a third party to whom pledged assets were transferred in case the third party claims that he acted in good faith. Therefore, both the vagueness of the good faith principle and the unlimited disposal right of the pledger may lead to increase in fraudulent asset transfers.

V. Conclusion

Superseding the CEPL, the MPL would be seen as a beneficial regulation for SMEs with reduced dependency to banks and other financial organizations requiring heavy security packages, especially for lower financing needs. However, the MPL brings controversial exceptions to the general principles of Turkish law and fails to provide creditors with enough assurance while introducing new opportunities favouring only debtors¹⁵. Considering such structure of the MPL which fails to ensure a balanced security structure with clear and reliable rights and obligations for both of the parties to the security, the MPL bears a risk to cause a reluctance of creditors and

¹⁴ MPL art 4 para 7.

¹⁵ Celal Göle and Gökhan Aydoğan, 'Ticari İşlemlerde Taşınır Rehni Kanunu'nun Ticaret Hukuku Açısından Değerlendirilmesi' (2017) 33 Banka ve Ticaret Hukuku Dergisi, 5, 28.

therefore result in a decrease in financing options. Also, the conflicting provisions between the MPL, its secondary legislation and other Turkish laws creates a new ground for legal disputes. Therefore, some amendments to the MPL and its secondary legislation seems necessary in order to establish a balanced security scheme and defeat its vague and conflicting legal provisions.

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