

Turkish Central Bank's New Circular on Capital Movements

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The Central Bank of the Republic of Turkey published a new Circular on Capital Movements ("**Circular**") which became effective on 2 May 2018, to mainly provide for adaptations to the amendments introduced by the Decree Amending the Decree No. 32 on the Protection of the Value of Turkish Currency¹ ("**Amending Decree**"). The provisions of the Circular, other than those regarding the Amending Decree, constitute simplified versions of their equivalents in the previous circular on the same subject.

1. Utilization Date of Foreign Currency Borrowings

The Amending Decree brought a foreign currency income condition for the legal entities resident in Turkey to make foreign currency borrowings and one of the exceptions of this rule is having USD 15 million loan balance before 2 May 2018. However, it is not clear under the Amending Decree whether the signing of the relevant loan agreements alone is sufficient to have such a loan balance or whether the drawdown of the loan by 2 May 2018 is also required.

The Circular did clarify this issue for financial lease and financing companies. Accordingly, for the loans obtained from financial lease and financing companies, the utilization date is the date of the execution of the relevant loan agreement. However, this issue continues to be uncertain for the loans obtained from deposit banks and shareholders. Based on the clear provision that the Circular introduced for the financial lease and financing companies, the interpretation that the utilization date will be "the date when the loan is transferred to the corresponding bank's account" gains strength with respect to the loans obtained from deposit banks and shareholders.

Therefore, the drawdown of these loans before 2 May 2018 is not required to be exempt from the mentioned restriction under the Amending Decree.

2. Further Exceptions to the Foreign Currency Borrowing Restrictions

The Circular brought three additional exceptions to the foreign currency income condition brought for the legal entities resident in Turkey to be allowed to make foreign currency borrowings:

- i. Foreign currency loans to be borrowed by Turkish residents for the financing of investments regarding renewable energy sources in accordance with the Law No. 5346 on

¹ Published in the Official Gazette No. 30312, dated 25 January 2018.

Use of Renewable Energy Resources for Generating Electricity². The amount of such foreign currency loans cannot exceed 80% of the total amount calculated by way of multiplying the annual generation amount with the subject price (local content rate included) for the remaining period with State guarantee.

- ii. Foreign currency loans to be borrowed by Turkish residents who won the tenders announced in the scope of Privatization Implementations Law No. 4046³ regardless of their currency, and for other public tenders in which the price is determined in a foreign currency. The amount of such loans cannot exceed the tender price.
- iii. Foreign currency loans to be borrowed by Turkish resident special purpose companies who are established for acquiring a new company share. The amount of such loans cannot exceed the total amount regarding the company shares that are projected to be acquired.

Additionally, the Circular provides explanations about the implementation of some already existing exceptions to the foreign currency income condition. The most important ones are summarized below:

- Concerning the exception provided for borrowing under an investment incentive certificate (*yatırım teşvik belgesi*), the foreign currency loan amount cannot exceed the foreign equity amount determined in the Investment Incentive Certificate. In case the amount is determined in Turkish currency, the Central Bank foreign exchange selling price at the date of utilization will be used for the calculation of the amount.
- Concerning the exception provided for public-private partnership projects, the Circular sets out that the amount of such loans cannot exceed the implementation contract value.
- Concerning the exception provided for holdings and group companies, the Circular establishes that while calculating the loan balance and foreign currency income amount of the utilizing company, the total amount of the loan balance and foreign currency income of all of the group companies will be used. However, the foreign currency loan will only be included in the loan balance of the utilizing company.

3. Shareholder Loans

The Circular provides that the foreign currency loans to be obtained from companies that are resident abroad are also included in the relevant Borrower's loan balance. Based on this provision, it can be interpreted that shareholder loans in foreign currency are also deemed as "foreign currency loan" (*döviz kredisi*) for the purpose of the Circular and therefore such loans are subject to the foreign currency borrowing restrictions.

4. Clarification to the Foreign Currency Income Definition

The Amending Decree provides that the foreign currency is the income generated from export, transit trade, sales and deliveries that qualify as export activities, and foreign currency generating services and activities.

The Circular introduces a more concrete scope for this term by making a reference to the meaning attributed to foreign income under the Communiqué No. 2017/4 on the Tax, Duty and Charge Exceptions on Export, Transit Trade, Sales and Deliveries that Qualify as Export Activities⁴. Accordingly, among others, the following items are qualified as foreign currency income for the purpose of the Amending Decree:

- Sales and deliveries of companies which won the tenders for the investments listed in the current year's program of the Ministry of Development and, although not included in this program, for public investments of the Ministry of Defense, the General Commandership of Gendarmerie and the Coast Guard Command,

² Published in the Official Gazette No. 25819 dated 18 May 2005.

³ Published in the Official Gazette No. 22124 dated 27 November 1994.

⁴ Published in the Official Gazette No. 30070, dated 18 May 2017.

- Sales and deliveries of manufacturing companies who undertook projects in the defense industry, security and intelligence fields,
- Services and activities of companies who undertook investment projects under the Build-Operate-Transfer Model,
- Activities of companies who undertook domestic and international transportation works tendered out domestically or internationally by public institutions or organizations,
- Manufacturing works regarding mining and operation of mines from the mine basins, which are tendered out internationally by the public institutions and organizations, in return for royalties,
- Services and activities of companies who undertook the building and renovating of facilities under the Public Private Partnership Model.

The Circular also introduces an obligation for the borrowers to declare their foreign currency income of the past three financial years when applying for a foreign currency loan. In this regard, the accountants of the borrowers will draft a report (approved by a sworn public accountant) based on the unconsolidated financial statements of the past three financial years. Then, the report and the “Foreign Currency Income Declaration Form” that is annexed to the Circular shall be submitted to banks and financial institutions.

5. Free Zone Legal Entities

The Circular sets out that legal entities established in free zones (*serbest bölge*) are foreign residents with regards to the application of the Circular except the branches of the Turkish banks and financial institutions. Therefore, the legal entities within the scope of the free zones are not subject to the restrictions brought by the Amending Decree to make foreign currency borrowings. However, the loans obtained from the free zone branches of Turkish banks and financial institutions are deemed as loans obtained from Turkish lenders. Accordingly, Turkish residents are not allowed to make foreign currency borrowings from the free zone branches of Turkish banks and financial institutions.

6. Sanctions

The sanctions to be applied in case of breach of the legislative provisions related to the protection of the value of Turkish currency are regulated under the Law on the Protection of the Value of Turkish Currency⁵ (“Law”). Under the current text of the Law, administrative fines between the range of TL 3,000 – TL 25,000 may be applied depending the gravity of the breach. However, the Law Proposition Amending Certain Laws, which is approved in the Committee on Planning and Budget of the Parliament, foresees to increase the amount of the administrative fines between the range of TL 10,000 – TL 50,000 for persons who acts in breach of the Law and the relevant secondary legislation.

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⁵ Published in the Official Gazette No. 1433, dated 25 February 1930.