

Chambers

GLOBAL PRACTICE GUIDE

Definitive global law guides offering
comparative analysis from top ranked lawyers

Real Estate

Turkey

Hergüner Bilgen Özeke Attorney Partnership

chambers.com

2019

TURKEY LAW AND PRACTICE

Law and Practice

Contributed by Hergüner Bilgen Özeke Attorney Partnership

Contents

1. General	p.4	4. Planning and Zoning	p.9
1.1 Main Sources of Law	p.4	4.1 Legislative and Governmental Controls Applicable to Strategic Planning and Zoning	p.9
1.2 Main Market Trends and Deals	p.5	4.2 Legislative and Governmental Controls Applicable to Design, Appearance and Method of Construction	p.9
1.3 Proposals for Reform	p.5	4.3 Regulatory Authorities	p.9
2. Sale and Purchase	p.5	4.4 Obtaining Entitlements to Develop a New Project	p.9
2.1 Categories of Property Rights	p.5	4.5 Right of Appeal Against an Authority's Decision	p.10
2.2 Laws Applicable to Transfer of Title	p.6	4.6 Agreements with Local or Governmental Authorities	p.10
2.3 Effecting Lawful and Proper Transfer of Title	p.6	4.7 Enforcement of Restrictions on Development and Designated Use	p.10
2.4 Real Estate Due Diligence	p.6	5. Investment Vehicles	p.10
2.5 Typical Representations and Warranties	p.6	5.1 Types of Entities Available to Investors to Hold Real Estate Assets	p.10
2.6 Important Areas of Law for Investors	p.6	5.2 Main Features of the Constitution of Each Type of Entity	p.10
2.7 Soil Pollution or Environmental Contamination	p.6	5.3 Minimum Capital Requirement	p.10
2.8 Permitted Uses of Real Estate Under Zoning or Planning Law	p.6	5.4 Applicable Governance Requirements	p.11
2.9 Condemnation, Expropriation or Compulsory Purchase	p.7	6. Commercial Leases	p.11
2.10 Taxes Applicable to a Transaction	p.7	6.1 Types of Arrangements Allowing the Use of Real Estate for a Limited Period of Time	p.11
2.11 Legal Restrictions on Foreign Investors	p.7	6.2 Types of Commercial Leases	p.11
3. Real Estate Finance	p.7	6.3 Regulation of Rents or Lease Terms	p.11
3.1 Financing Acquisitions of Commercial Real Estate	p.7	6.4 Typical Terms of a Lease	p.11
3.2 Typical Security Created by Commercial Investors	p.8	6.5 Rent Variation	p.11
3.3 Restrictions on Granting Security over Real Estate to Foreign Lenders	p.8	6.6 Determination of New Rent	p.11
3.4 Taxes or Fees Relating to the Granting and Enforcement of Security	p.8	6.7 Payment of VAT	p.11
3.5 Legal Requirements Before an Entity Can Give Valid Security	p.8	6.8 Costs Payable by Tenant at Start of Lease	p.11
3.6 Formalities When a Borrower is in Default	p.8	6.9 Payment of Maintenance and Repair	p.11
3.7 Subordinating Existing Debt to Newly Created Debt	p.8	6.10 Payment of Utilities and Telecommunications	p.12
3.8 Lenders' Liability Under Environmental Laws	p.8	6.11 Insuring the Real Estate that is Subject to the Lease	p.12
3.9 Effects of Borrower Becoming Insolvent	p.9	6.12 Restrictions on Use of Real Estate	p.12
3.10 Consequences of LIBOR Index Expiry	p.9		

6.13 Tenant's Ability to Alter and Improve Real Estate	p.12	8. Tax	p.14
6.14 Specific Regulations	p.12	8.1 VAT	p.14
6.15 Effect of Tenant's Insolvency	p.12	8.2 Mitigation of Tax Liability	p.14
6.16 Forms of Security to Protect Against Failure of Tenant to Meet Obligations	p.12	8.3 Municipal Taxes	p.14
6.17 Right to Occupy After Termination or Expiration of a Lease	p.12	8.4 Income Tax Withholding for Foreign Investors	p.14
6.18 Right to Terminate Lease	p.12	8.5 Tax Benefits	p.14
6.19 Forced Eviction	p.13	8.6 Key Provisions in the Federal Tax Reform Legislation	p.15
6.20 Termination by Third Party	p.13		
7. Construction	p.13		
7.1 Common Structures Used to Price Construction Projects	p.13		
7.2 Assigning Responsibility for the Design and Construction of a Project	p.13		
7.3 Management of Construction Risk	p.13		
7.4 Management of Schedule-related Risk	p.13		
7.5 Additional Forms of Security to Guarantee a Contractor's Performance	p.14		
7.6 Liens or Encumbrances in the Event of Non-payment	p.14		
7.7 Requirements Before Use or Inhabitation	p.14		

TURKEY LAW AND PRACTICE

Hergüner Bilgen Özeke Attorney Partnership is composed of approximately 150 individuals with a variety of educational and professional backgrounds. The 90-member legal team, 15 of whom are Hergüner partners, are involved in cases that require a full grasp of Turkish and cross-border jurisdictions, as well as different cultures and languages. The firm's Real Estate team, comprised of two partners and eight associates, advises the world's leading international retailers, real estate funds, and developers in Turkey's most famous shopping and residential complexes, urban re-generation projects, and tourism facilities. In addition to pure real estate transactions, the team also provides permitting and licensing related advice, cross-disciplinary input in infrastructure projects along with the firm's Infrastructure and Project Finance team as every infrastructure project

has a real estate leg including both privately owned and government owned/controlled land. The real estate team also specialise in sophisticated real estate litigation, arbitration, and represent local and international developers and investors before civil courts, administrative courts, tax courts, and arbitral tribunals. The team's practice includes: commercial leases; real estate investment trusts; real estate investment funds; structuring; restructuring; building permits; retail centres; sale and lease back; residential projects; inheritance matters; airports and ports; construction licences; energy projects; mining/extractive industry; zoning legislation; highways, bridges, and tunnels; investment funds; pipelines; urban regeneration projects; and tourism facilities

Authors



Serkan Gül is a partner at Hergüner and head of the firm's Real Estate practice group. He specialises in real estate matters, and has written extensively on the subject. Mr Gül is a member of: the Association of Real Estate and Real Estate Investment

Companies (Gayrimenkul ve Gayrimenkul Yatırım Ortaklığı Derneği, GYODER); Strategic Thinking in Real Estate (Gayrimenkul için Strateji Platformu, GİSP); and the International Law Institute. Mr Gül advises clients in every aspect of real estate transactions, including asset and share deals, from the project's inception to completion. He has extensive experience in real estate investment funds and trusts, sale and leaseback transactions, construction, and zoning and permitting in deals that include residential properties, offices, shopping centres, hotels, and port facilities. Some of his most noteworthy work has included the sale of properties that had previously sat idle for long periods of time due to cost overruns and regulatory delays.



Enis Sinan Reyhan is an associate with the firm's Corporate Practice Group, working primarily on the Real Estate Team. Mr Reyhan advises clients on zoning, construction, licences and permits, and contracts such as sales, profit sharing, construction, and lease agreements. He advises foreign and domestic clients in the construction, commercial housing, resort and hotel, energy, retail, port, and transportation industries.

1. General

1.1 Main Sources of Law

Real estate practice in Turkey is not governed by a separate and dedicated body of law. Instead, Turkish real estate law is integrated into the general operation of civil law, and different aspects of real estate law are governed by chapters in codes of general operation.

At the very top, property rights are secured by the Turkish Constitution. In addition, the European Convention on Human Rights, as an international treaty duly subscribed by Turkey, also secures the right of property. These protections mean that the Turkish Constitutional Court and also the European Court of Human Rights have eventual jurisdic-

tion over property disputes, generally but not exclusively in disputes of private parties with the government. These courts may in certain circumstances also exercise jurisdiction in disputes purely between private parties, on account of argued violations of the government's obligation to actively protect property rights.

The Civil Code (*Türk Medeni Kanunu*) defines different property types, and regulates how property interests are created, transferred and extinguished. The Code of Obligations (*Türk Borçlar Kanunu*), which regulates contracts generally, also governs real estate-related contracts, including lease agreements, specifying procedural requirements for their formation or termination, and supplying certain substantive mandatory terms or default principles as necessary.

The Code on Zoning and Construction (*İmar Kanunu*) establishes the rules governing construction, including zoning requirements and various licences and permits necessary to construct and occupy buildings.

The Code on Land Registration (*Tapu Kanunu*) governs the registration of real estate.

Under the general framework established by the foregoing fundamental laws, there are more detailed codes and regulations addressing more specific areas of law. The most frequently cited of these in recent years has been the Urban Regeneration Law (*Kentsel Dönüşüm Kanunu*), as well as the Capital Markets Board's respective communiqués on Real Estate Investment Trusts (*Gayrimenkul Yatırım Ortaklıklarına İlişkin Esaslar Tebliği*) and Real Estate Investment Funds (*Gayrimenkul Yatırım Fonlarına İlişkin Esaslar Tebliği*).

1.2 Main Market Trends and Deals

The magnitude 7.6 earthquake which hit the vicinity of Istanbul in 1999 killed thousands, and laid bare the inescapable fact that Turkey's major cities sit on an active earthquake zone. Many older buildings were revealed to be incapable of withstanding another violent seismic event, and a massive campaign began to tear down weaker buildings and to replace them with stronger structures. This initiative gave rise to the enactment of the Urban Regeneration Law, which provides tax incentives, state-provided financing options and expedited regulatory review procedures for such replacement efforts.

The past 12 months have witnessed the continuation of a flurry of construction that has been made possible by the Urban Regeneration Law. These have tended to be small or medium-scale works, with each individual project often concerning no more than a single residential building, but these projects have covered virtually all of Istanbul, with multiple new constructions ongoing on nearly every block in the downtown area.

In terms of larger trends over the past year, there has been activity in mixed-use projects: many new developments incorporating hotels, offices and shopping centres have either begun construction or gone into operation in the main commercial districts of Istanbul. Additionally, the number of port developments/transactions has significantly increased.

Last but not the least, restructuring of under-performing commercial assets or restructuring of real estate-related loans became an increasing part of the workload due to the narrowing demand in residential real estate sector. Additionally, the unexpected recent fluctuation of the foreign exchange rates against Turkish lira (TRY) is likely to trigger non-performing loans (NPL) sales secured by properties in the near future.

1.3 Proposals for Reform

Even though the main pillars of Turkish real estate law are stable these days, some proposed changes to the tax code threaten to have considerable effects on real estate transactions. Under the current tax code, a piece of real property can be transferred tax-free by those not in the business of trading in real estate after it has been held for five years. A change to the tax code would scuttle this exemption, and render proceeds from such sales subject to income tax. The rate at which income tax would be assessed would decrease the longer the property is held. This change would likely have a chilling effect on sales of real estate; the tax exemption currently clears away what would be a major tax burden on would-be sellers. This proposal has been pending before the Grand National Assembly for five years, which indicates that there is not much momentum behind it at this time.

Another change in tax codes, one that actually has gone into effect, has been the grant of an explicit tax exemption to sales to consumers in urban regeneration projects. This change in the legislation was inspired by case law granting exemptions to sales of units to final consumers. The codification of this exemption should change the current approach of title deed offices and tax offices, which had been declining to grant it with regularity.

2. Sale and Purchase

2.1 Categories of Property Rights

Under Turkish law, the most basic category of property right is simple freehold ownership (*mülkiyet*). Freehold ownership gives the property owner the right to use, benefit from and dispose of a piece of property. These rights are conceptually separable from one another; more limited property rights can be created by carving out certain of these rights from simple freehold ownership.

Turkish law permits the grant to a third party of the right to build on a piece of property (*üst hakkı*), and the holder of such a right becomes the owner of any structures that are built on such land in exercise of this right. If the right to build is intended to be independent and indefinite (*bağımsız ve sürekli*) then the holder of the right can register it in the land registry as a separate property interest, and this right is essentially treated no differently from independent real estate.

Turkish law also recognises condominium ownership, which allows independent units in a completed structure to be owned separately from the main structure, with the common areas of the main structure remaining under joint ownership with the owners of the other independent units in the building.

TURKEY LAW AND PRACTICE

Under Turkish law it is also possible to separate the right to use and to benefit from a piece of property from the right to disposal, and the complete right of use and benefit can be granted to a third party, in what is called a usufruct right (*intifa hakkı*). In a strict sense usufruct under Turkish law is a personal right rather than a property right, because this right cannot be alienated or devised, and does not include the right to make fundamental changes to the established use of the property. The grant to a third party of the usufruct right leaves the property owner with the sole right of disposal.

2.2 Laws Applicable to Transfer of Title

Transfer of title is governed by:

- the Civil Code, insofar as it defines the extent of the interest that is transferred;
- the Code on Land Registration, which regulates the procedures to be followed for the transfer and introduces restrictions against and specific clearance requirements for foreign ownership of real estate; and
- the Code of Obligations, which supplies the rules and background principles governing sales agreements.

There are no specific laws that govern transfers of real estate by type of use: residential property and commercial property alike are transferred under the same rubric. However, there are specific procedures that have been put into place that determine the alienation of property rights held by the government, such as by way of usufruct.

2.3 Effecting Lawful and Proper Transfer of Title

Real estate transfers are given effect at the time they are registered at the Land Registry Office. The Land Registry Office records provide a definitive record of real estate ownership, and they have their roots in the Ottoman land registry system. Land records are kept in duplicates in the central database in Ankara and at the local land registry office. These records are open to the public, and are reliably accurate.

Transfers of title must be recorded in order to gain effect. Similarly, all interests in real property, including mortgages, usufruct rights, rights of first refusal and rights of repurchase, must all be registered to ensure validity.

Given the definitive authority carried by title records, which are open to the public for inspection, title insurance is not at all prevalent, with virtually no risk to insure against.

2.4 Real Estate Due Diligence

When purchasing real estate, buyers generally engage lawyers for due diligence purposes. Lawyers inspect the land registry records and the usage restrictions included in the zoning plans for the particular locality. As the land registry records are authoritative, a thorough inspection of these public records generally suffices to provide assurance to pur-

chasers. Additionally, technical consultants are appointed for environmental and technical due diligence matters.

2.5 Typical Representations and Warranties

The types of representations and warranties given in real estate sales differ significantly depending on how the sale is structured. Asset sales typically entail very limited representations and warranties, given that comprehensive and definitive information about the encumbrances on land, including granted easements, established security, and pre-emptive rights are all revealed in public records. On the other hand, if the deal is structured as a share sale, with the entity holding the asset changing hands rather than the underlying asset itself, extensive representations and warranties are generally demanded.

Environmental representations and warranties are occasionally demanded but are seldom granted.

2.6 Important Areas of Law for Investors

Real estate law sits at the crossroads of constitutional law, private law and administrative law. As noted above, property rights are guaranteed by the constitution and international treaties. At a more local level, the most important area of law for a purchaser to keep in mind is property law, given that it determines the rights and obligations conferred to owners of real property. The law of obligations is also important, in that it defines the rules and principles governing contracts related to real property (sale agreements, lease agreements, etc). Next, zoning law should be kept in mind, as this determines the uses to which real estate can be put. A purchaser should also be mindful of secondary rules governing the issuance of construction and usage permits. Finally, land registration laws are also fairly important, given that they determine what information about real property can be gleaned from land registry records.

2.7 Soil Pollution or Environmental Contamination

The obligation to comply with environmental regulations is generally imposed on owners of real property rather than the property itself. As such, a buyer of real property is in principle not responsible for any contamination that has taken place prior to their taking ownership. However, the fact of contamination may carry with it the presumption that the current occupant has caused the contamination, and in such an event the occupant may need to defeat that presumption by proving that it was an earlier owner who caused the pollution. This is one area where due diligence findings may prove useful.

2.8 Permitted Uses of Real Estate Under Zoning or Planning Law

A buyer can ascertain the permitted uses of a parcel of real estate by consulting the zoning plans, plan notes for the concerned plot and zoning legislation. The zoning plans con-

cerning each locality contain specific instructions on how each parcel may be developed or used; these instructions both reveal the general plan for the use of the land in the locality and indicate how each parcel fits into the whole.

It is generally not possible to alter zoning restrictions for particular parcels on a project basis through agreements with local zoning authorities.

2.9 Condemnation, Expropriation or Compulsory Purchase

Turkish law does indeed permit governmental taking of land in cases of public need. The transfer can either take place voluntarily, or the government can file suit to condemn a piece of private property and in due course assume ownership.

Voluntary transfers can be in exchange for cash or for another piece of government-held property.

If the parties cannot come to an agreement on the consideration for a voluntary exchange, the government can file suit to establish the value of the land to be condemned. In a condemnation suit, the court appoints an expert to establish the value of the land to be condemned, and the parties can contest the experts' valuation in open court. The court then establishes the value of the land, and upon payment of this sum orders the registration of the land in the name of the condemning agency. The condemnation compensation may be split into instalments, and if this is ordered, then registration may be ordered after the payment of the first instalment.

In practice, developed land is rarely condemned – condemnation proceedings are almost exclusively exercised for rural property.

2.10 Taxes Applicable to a Transaction

Transfers of real estate through asset deals are subject to title deed registration fees, VAT and income tax. Share sales are subject to VAT and capital gains taxes. However, VAT, income tax and capital gains tax are subject to exemptions that are relatively easy to satisfy.

Title registration fees of 4% of the value of the asset are assessed on sales of real estate by asset sale. These fees have been reduced to 3% on sales of residential and commercial property until 31 December 2019. These fees are generally split equally between the parties.

If the seller is a legal entity, VAT is assessed on the transferred property, at 18% for office space and commercial property, and at 1%, 8% or 18% for residential property, depending on its value per square metre. With a recent enactment, the VAT rate applicable for sales of residential property has been temporarily limited to 8%, with the exemption expiring on 31 December 2019.

Finally, income tax is assessed on the selling asset holder. For individuals the applicable rate is between 15% and 35%, but capital gains tax is not assessed on individuals who are not professionally engaged in the trade of real estate and who have held the sold property for five years or longer. For corporations the capital gains tax rate is 22%; corporations that do not engage professionally in the trade of real estate can shield 75% of the income from such a sale so long as the proceeds are retained in the company coffers.

In share sale transactions VAT and capital gains tax exemptions apply so long as the transferred shares have been held by the selling entity for two years or more. Share purchase agreements are exempted from stamp tax, with a recent change in the law.

2.11 Legal Restrictions on Foreign Investors

Foreign legal entities may not acquire real property in Turkey unless they are allowed to do so under special laws, such as the Petroleum Law, Tourism Law or the Industrial Zones Law. To overcome this legal barrier, investors often choose to establish Turkish SPVs. Turkish-incorporated companies with 50% or more foreign share ownership and/or management control are subject to approval by the governorship before they can acquire real property in Turkey. Turkish-incorporated companies in which the foreign ownership is under 50% and management is not under foreign control can acquire real property just like domestic concerns where all shareholders are Turkish nationals.

The governorship approval procedure involves an investigation of whether the real property is in a military forbidden zone, military security zone or strategic zone, or in a private security zone. If it is, then the acquisition is subject to clearance from the military or the provincial police directorate, depending on which of these exercises jurisdiction over the relevant sensitive area. If not, approval for the acquisition is routinely granted. The process is completed within one month approximately. Establishment of mortgages in favour of foreign capital companies, leases of real property by foreign capital companies, and acquisition of real property in organised industrial zones, technology development zones and free zones are not subject to the foregoing approval process.

3. Real Estate Finance

3.1 Financing Acquisitions of Commercial Real Estate

Acquisitions of commercial real estate are generally financed by loans and sale revenue generated from the project. Real estate investment funds, lease certificates and real estate investment companies are capital market instruments used for financing options for acquisitions of large real estate portfolios or companies holding real estate.

TURKEY LAW AND PRACTICE

3.2 Typical Security Created by Commercial Investors

There is no security specifically used by commercial real estate investors. Generally securities such as a mortgage, share pledge, personal guarantee, assignment of receivables, etc, are used for real estate-related funding.

There are two types of mortgage recognised under Turkish law: the principal amount mortgage and the maximum amount mortgage. Principal amount mortgages are established to secure amounts that have already been lent to borrowers, and contain unconditional and absolute debt acknowledgement of the borrower. Although the amount of the mortgage only shows the principal amount of the loan lent, the lender may request:

- the principal amount;
- foreclosure expenses and default interest;
- accrued contractual interest; and
- expenses made by the mortgagee(s) that were mandatory to preserve the value of the mortgaged property (including disbursement of insurance premiums that were the mortgagor's responsibility to pay).

On the other hand, the maximum amount mortgage secures an amount that is higher than the principal amount, incorporating in advance various expenses that may be incurred by the mortgagee, and do not permit the collection of any amounts above the ceiling amount.

Sale-and-leaseback structures can also be used in acquisitions of commercial real estate. Finally, Islamic finance-designed instruments such as sukuk may also be utilised.

3.3 Restrictions on Granting Security over Real Estate to Foreign Lenders

Securities are granted over real estate to foreign financial institutions without any restrictions. Repayments to a foreign lender under a security document or loan agreement are made without any restriction unless repayment constitutes a criminal act (eg, money laundering).

3.4 Taxes or Fees Relating to the Granting and Enforcement of Security

Stamp tax (0.94% of the amount subject to mortgage), and a mortgage fee (0.45% of the amount subject to mortgage) are paid for the establishment of a mortgage. Foreign financial institutions are exempted from taxes and fees arising out of securities granted over real estate.

The fee for enforcement proceedings is approximately 0.5% of the amount subject to mortgage.

In accordance with a recent change in the legislation, an exemption has been brought for half of the mortgage fee (0.225%) for mortgages established between traders.

3.5 Legal Requirements Before an Entity Can Give Valid Security

Under Turkish law, it is prohibited for a target company to provide funds, loans, security or guarantee to a third party to facilitate the acquisition of its own shares and such financial assistance transactions will be deemed null and void. This provision does not apply to (i) transactions conducted for the purpose of activity of the financial institutions, or (ii) security, advance payment and loans granted to employees of the target company or its parent company in order to acquire the shares of the company.

When granting upstream security or guarantees for a parent company, it may be difficult for board members to specify a convincing reasonable cause for the subsidiary to enter into such an arrangement to the benefit of its holding company or group companies.

3.6 Formalities When a Borrower is in Default

Under Turkish law, the creditor beneficiary of a mortgage must initiate an execution proceeding to liquidate the mortgage. Priority between claimants is listed as an obligatory rule of the applicable law. By law, a creditor beneficiary of a mortgage has priority over other creditors, with respect to mortgaged property.

An accelerated foreclosure procedure exists for principal amount mortgages and mortgages granted in favour of banks and financial institutions.

3.7 Subordinating Existing Debt to Newly Created Debt

In principle, the order of priority between creditors is regulated under the applicable law and contractual subordination is not expressly regulated under the law. According to Court of Appeals precedents, execution and bankruptcy rules relate to public policy and cannot be changed contractually. Accordingly, a subordination agreement is not enforceable against an execution office. However, parties may freely undertake to pay respective amounts to other recipients upon collecting receivables. In summary, a subordination arrangement may create a contractual obligation on the part of the parties, but will not have a preventive effect during any enforcement proceedings to be initiated before execution offices.

3.8 Lenders' Liability Under Environmental Laws

Under the applicable law, polluters must bear all expenses for preventing, removal and cleaning of pollution. Applicable law requires that – where environmental pollution is a possibility – the parties must take the necessary measures in order to prevent pollution, and if pollution occurs they must take the required actions in order to stop the pollution or decrease the effects of the pollution. The same law explicitly states that polluters have strict liability due to environmental pollution. Therefore, lenders holding or enforcing security

over real estate should not be liable under environmental laws, as any pollution of the real estate is caused by the borrower.

3.9 Effects of Borrower Becoming Insolvent

In principle, securities established in favour of a lender are not voided by a borrower's insolvency. However, securities guarantee the creditors' position in such cases.

In the event of a borrower's insolvency, creditors can ask a court to declare the bankruptcy of the borrower. Bankruptcy results in the total liquidation of a bankrupt entity's assets and the satisfaction, pro rata, of its creditors. An important exception to this rule is mortgagees: as their receivables are guaranteed by specific security, bankruptcy rules require that they be repaid first, in full, before other, unsecured creditors.

On the other hand, when borrowers become insolvent, they can seek bankruptcy protection in the form of composition of debts. Under this device, debtors reach an agreement with their creditors regarding the extent of the deduction to be made in outstanding debts and the deferment of payments. Mortgagees are given exceptional rights under the composition of debts mechanism as well: even under the composition regime mortgagees may initiate proceedings for the sale of mortgaged assets to have their debts repaid, but may not realise the eventual sale of the secured asset while the protection is in place.

Another device of bankruptcy protection that used to be available, but which is no longer permitted, was the deferral of bankruptcy, which was imposed by a court upon the application of the debtor. The shift to a composition regime from a deferral of bankruptcy regime is a positive development, in that it promotes agreement between debtors and creditors rather than a court imposing a solution in its own judgment.

3.10 Consequences of LIBOR Index Expiry

The market may adapt to the new situation by setting forth a new benchmark rate, such as EURIBOR, in credit arrangements. A fall-back clause referring to another alternative benchmark rate may be used as well. For current agreements, parties may revise their agreement to adapt to the new situation by mutual agreement. The bottom line would be that courts would determine and refer to a new interest rate benchmark, upon appeal of parties, in the event of any dispute.

4. Planning and Zoning

4.1 Legislative and Governmental Controls Applicable to Strategic Planning and Zoning

Zoning plans must comply with the applicable legislation and more specifically with the planning principles, urbanisa-

tion principles and public interest, such as regional requirements, transportation opportunities, etc. This implies legislative control over zoning plans.

Moreover, smaller-scaled zoning plans must comply with larger-scaled zoning plans (hierarchy of zoning plans). Larger-scale zoning plans (spatial strategic plans, environmental plans) are enacted by ministries, whereas smaller-scaled zoning plans (implementation zoning plans) are enacted by local municipalities. This implies central administration's control over local authority.

4.2 Legislative and Governmental Controls Applicable to Design, Appearance and Method of Construction

Construction permits should be obtained from the municipality for any new construction, refurbishment or major modification. The construction permit and design documents should be in accordance with the legislation and zoning plans. The legislation defines detailed technical requirements for design documents. Additionally, various requirements and restrictions (eg, setback distances, ratio of footprint to parcel area, construction coefficient) are also regulated under zoning plans.

Oversight is conducted by the authority issuing the construction permit (eg, the municipality).

4.3 Regulatory Authorities

Zoning plans regulate the permitted use and development of individual parcels. Environmental zoning plans are enacted by the Ministry of Environment and Urban Planning. General functions (business, residential, etc) of regions are regulated under environmental zoning plans. Implementation zoning plans are enacted by municipalities, whereby specific zoning conditions (eg, construction coefficient, maximum height, set-back distances, etc) are specified. Accordingly, function restrictions (residential, industrial, etc), set-back distances, construction coefficient and maximum height are typical conditions and restrictions regarding development of projects. Moreover, there are restrictions connected to special status of the respective lands (forest, cultural heritage, natural heritage, etc).

In addition, the Housing Development Administration also exercises planning authority in certain specific, government-subsidised housing development zones that are placed under its jurisdiction.

Finally, the Ministry of Tourism and Cultural Heritage also exercises approval authority in zones of cultural heritage.

4.4 Obtaining Entitlements to Develop a New Project

The procedure for obtaining entitlements to develop a new project or complete a major refurbishment is as follows. An

TURKEY LAW AND PRACTICE

initial application is made to the municipality to obtain a zoning status certificate. Official designs (projects) are prepared by architects and engineers according to the conditions stated in the zoning status certificate. Such official designs (projects) are submitted to the municipality, along with other documents required for a construction permit application. The municipality approves the official designs (projects) and issues the construction permit. The application procedure generally takes one to three months, depending on the time spent drafting official designs (projects). Municipalities generally issue construction permits within one to three months.

Third parties do not directly participate in the construction permit procedure. However, affected third parties may submit an official letter to the municipality for revocation of a construction permit, within the scope of the general right of petition. This application does not affect the validity of the construction permit.

4.5 Right of Appeal Against an Authority's Decision

Under Turkish law, as a constitutional principle, all administrative decisions are subject to judicial review. Thus, an affected party may file an administrative lawsuit to declare the administrative act null and void or claim damages. Property rights holders may challenge the denial of construction permits, unfavourable revisions to zoning plans and parcelation plans, or any other administrative act. In addition, affected third parties (neighbours, etc) may initiate a lawsuit for cancellation of a construction permit.

4.6 Agreements with Local or Governmental Authorities

It is not necessary to enter into agreements with local or governmental authorities to develop a project. Zoning plans grant the right to undertake construction under the conditions specified in the zoning plan, and no further agreement with the municipality is necessary to exercise that right. Construction requires the obtainment of a construction licence, but that is not an agreement per se, but rather an administrative approval process.

Agreements may be necessary in ancillary fashion, such as contractors needing to subscribe to utilities for consumption during the construction phase. Additionally, developers need to appoint licensed construction audit companies.

4.7 Enforcement of Restrictions on Development and Designated Use

If the planned construction does not comply with zoning conditions and designated use, the municipalities will not issue a construction permit. Moreover, if the planned activities do not comply with designated use, it is not possible to obtain an operation permit.

The Turkish government has granted to property owners a temporary right to legalise any incompliance that may exist in constructions, by making a declaration and making a payment calculated on the basis of the value of the property and the area of construction. These applications may be made until 15 June 2019.

5. Investment Vehicles

5.1 Types of Entities Available to Investors to Hold Real Estate Assets

Special purpose vehicles, real estate investment trusts and real estate investment funds are the types of entities that are available to investors to hold real estate assets. Real estate investment trusts and real estate investment funds are preferred by real estate investors due to tax exemptions granted to such entities. Real estate investment trusts and real estate investment funds are also preferable because these entities may create large-scale funds generated from the capital contributions of different investors. Special purpose vehicles may also be advantageous as they are not subject to restrictions and specific conditions stipulated under capital market legislation, such as valuation conducted under said legislation, etc. For this reason, special purpose vehicles are commonly used in practice.

5.2 Main Features of the Constitution of Each Type of Entity

Special purpose vehicles may be incorporated as a limited liability company or a joint stock company in the form of a publicly or privately held company. Real estate investment trusts may be incorporated as a joint stock company in the form of a publicly held company. Real estate investment funds do not have any legal personality and may only be held by qualified investors.

5.3 Minimum Capital Requirement

The minimum capital amount for a real estate investment trust is TRY30 million, and TRY100 million for real estate investment trusts incorporated for infrastructure purposes. The minimum asset pool for a real estate investment fund should be TRY10 million within one year of initiating the sale of participation shares to qualified investors. Joint stock companies should be incorporated with a minimum capital amount of TRY50,000; one-quarter of the said amount should be paid at the time of incorporation and the rest should be paid within 24 months of incorporation of the company. Limited liability companies should be incorporated with a minimum capital amount of TRY10,000; one-quarter of the said amount should be paid at the time of incorporation and the rest should be paid within 24 months of incorporation of the company.

5.4 Applicable Governance Requirements

Corporate law provisions are applied to special purpose vehicles as they are subject to the Turkish Commercial Code, including the capital maintenance rule, corporate benefit, etc. Real estate investment trusts are also subject to corporate law requirements stated under the Turkish Commercial Code. Real estate investment trusts and real estate investment funds are also subject to capital market regulations as they make use of funds provided by investors.

6. Commercial Leases

6.1 Types of Arrangements Allowing the Use of Real Estate for a Limited Period of Time

A lease is the basic type of arrangement that allows a person, company or other organisation to occupy and use real estate for a limited period of time without buying it outright. A right of construction may also be established as a type of right in rem in order to protect the owner's right against third parties. In practice, a right of construction is preferable to other types of use of real estate due to the fact that it gives property rights to the holder of the right of construction for a period of time. A mortgage may also be established over a right of construction as it is independently registered in the title deed registry with separate ownership rights.

Another type of right in rem is the usufruct right, which entitles the right holder to use and benefit from real property in the fullest extent. The usufruct right is a right granted to a specific person and may not be transferred. It is a right that is limited in time; usufruct rights granted to legal persons are limited to 100 years, and usufruct rights granted to natural persons being limited to the grantee's lifetime.

6.2 Types of Commercial Leases

There are no different types of commercial leases. All lease agreements are governed by the same regulation. However, leases may be classified as a ground lease or a building lease according to rental conditions.

6.3 Regulation of Rents or Lease Terms

Rents are freely negotiable under lease agreements. However, certain lease terms, such as eviction, rent increase, etc, are specifically regulated under the Turkish Code of Obligations as mandatory terms. Please note that major restrictive provisions do not come into effect until 1 July 2020 for commercial leases, and accordingly a liberal regime is applied for commercial leases.

A recently enacted piece of legislation prohibits denominating rents in foreign currency under certain conditions. This legislation applies to lease agreements where the lessor is a foreign capital company, but it is still possible to denominate rents in foreign currency in lease agreements where the ten-

ant is a foreign real person, foreign company or a company owned by foreign investors.

6.4 Typical Terms of a Lease

There is no minimum or maximum limit for lease terms. In practice, terms of leases are contractually agreed as ten to 30 years.

Structural maintenance should be carried out by the owner of the real estate, and daily maintenance should be carried out by the lessee. Parties may contractually agree otherwise.

Rent payments are mostly agreed by the parties to be made monthly; the term of rent may also be determined by the parties as quarterly or annually.

In commercial leases, leases may express rent as a fixed amount or as a fixed percentage of revenues derived from the use of the property. Market practice tends to combine the two, with payable rent being set at whichever of the two is higher.

6.5 Rent Variation

As per the Turkish Code of Obligations, if the rent is agreed in Turkish lira, the rent may be increased according to the consumer price index, but no higher. Rent may not be increased within the first five-year period if the rent is agreed in foreign currency. However, this provision for foreign currency rents will not come into effect until 1 July 2020.

6.6 Determination of New Rent

For a given period of time (ie, until the end of the third year following the end of lease term), the increased rate agreed by the parties applies for rent increases. At the end of such period, if the parties cannot mutually agree on the new rent, the court may render a new rent according to the market price, upon request of the parties.

6.7 Payment of VAT

If the lease property is part of a commercial enterprise or owned by a limited liability company/corporation, VAT is applicable; the VAT rate is 18% of the rent. Withholding tax is applicable for leases of natural person-owned real estate to commercial entities.

6.8 Costs Payable by Tenant at Start of Lease

A commission to the real estate agency and a deposit to the real estate owner are generally paid by the tenant at the start of a lease, as per the current market practice.

6.9 Payment of Maintenance and Repair

Areas used by several tenants, such as car parks, gardens or swimming pools, are classified as common areas, and expenses arising out of usage of these areas are distributed to tenants according to certain criteria (eg, land share, square metre criteria).

TURKEY LAW AND PRACTICE

6.10 Payment of Utilities and Telecommunications

If the building housing the premises has been converted to condominium use, then each tenant is able to obtain individual utilities accounts for their own use. Expenses incurred for common areas are generally allocated among tenants on the basis of square footage. Managers of such properties usually reserve for themselves by contract the authority to take into account other factors such as the tenant's location within the premises, the extent to which the presence of the tenant generates business for the facility as a whole, the tenant's business volume, etc.

The allocation of common expenses among tenants in shopping centres is governed by the Regulation on Shopping Centres (*Alışveriş Merkezleri Hakkında Yönetmelik*). The regulation specifies mandatory rules to be used when allocating common expense contribution amounts to tenants in shopping centres. The common expenses are, in principle, allocated according to square footage of the respective stores, restaurants, etc.

6.11 Insuring the Real Estate that is Subject to the Lease

Generally speaking, landlords insure the property against structural risks, and tenants insure the property against operational risks. Landlords also insure the common areas of shared-use properties, and can shift the cost of this insurance depending on the parties' bargaining positions. The law imposes the cost of mandatory insurance on landlords by default, but permits reassignment of these costs.

Landlords typically insure properties against fire, hurricane, explosion, water damage, flooding, landslide, snow damage, aircraft impact and earthquake. Terrorism insurance is also sometimes taken out. A lessee typically takes out a renter's all-risk insurance and also third-party liability insurance.

6.12 Restrictions on Use of Real Estate

The use of land is regulated under the zoning plan for the locality; these restrictions operate in the background, and supersede any conflicting provisions of any lease agreement that is signed between a landlord and a tenant. Furthermore, under the Code on Condominiums, operation of businesses is prohibited in residential buildings.

Restrictions on a tenant's use of real property are typically found in lease agreements, and these are binding on lessees under contract law.

6.13 Tenant's Ability to Alter and Improve Real Estate

Tenants may alter leased premises if this is permitted under their lease agreement. Structural improvements may require a licence from the local municipality, and these licences are only issued to landowners. As such, a tenant would have to obtain the landlord's consent to structural improvements.

Landlords typically give their consent to such improvements by issuing a power of attorney to their lessees for improvement purposes, under which authority lessees obtain the requisite licence and commence construction of improvements.

Having once consented to alterations to be made by a lessee, a landlord may not demand the return of the property to its previous condition. Similarly, a lessee may not demand compensation for any increase in the value of the property that may be caused by the lessee's alterations. Both of these default positions may be changed by agreement.

6.14 Specific Regulations

There are very few regulations that govern the lease of property by type of use. One such specific set of rules, the Regulation on Shopping Centres, has had little restrictive impact in practice.

6.15 Effect of Tenant's Insolvency

A lessee's bankruptcy during the term of a lease gives the landlord the right to demand assurances for payment of rents to fall due in the future. If the lessee or the bankruptcy administrator is not able to provide such assurances, the landlord is then entitled to terminate the lease.

6.16 Forms of Security to Protect Against Failure of Tenant to Meet Obligations

Landlords typically demand that tenants guarantee their obligations by posting a cash deposit or a bank letter of guarantee. The Code of Obligations has introduced a quantitative limitation in this respect, limiting the amount of such guarantees to be posted to three months' rent at maximum, but this provision will not take effect until July 2020. Until that time the amount of deposit can be decided between the parties to the lease. In any event, landlords tend to demand annual or quarterly payment of rent to obtain further security.

6.17 Right to Occupy After Termination or Expiration of a Lease

A tenant has the right to occupy leased premises for another 11 years after the end of a lease period. The landlord may terminate the lease by giving notice no less than three months before the end of the 11th year after the expiration of the lease, or each year thereafter. This is a mandatory provision of the law, and landlords therefore do not have a free hand in circumventing this entitlement given to lessees.

6.18 Right to Terminate Lease

The landlord may terminate a lease if the lessor has served written notice on the lessee twice in one lease term for failing to pay rent.

The landlord may terminate a lease if the lessee has undertaken to vacate the leased premises on a certain date but failed to keep its promise.

The landlord may also terminate a lease on the basis of need: if the landlord or the landlord's family must use the leased premises themselves, then the landlord may terminate the lease. Similarly, the landlord may terminate the lease if material repairs need to be made to the premises and the lessee's continued occupation of the premises under such circumstances is not possible.

Finally, the landlord may terminate a lease if the lessee fails to use the premises in accordance with the terms of the lease agreement. If the lessee's breach is nonmaterial the landlord must give at least a 30-day cure period; if the breach is material and the breach is unlikely to be remedied in the cure period, the agreement may be terminated with immediate effect.

The lessee may terminate the agreement in the event that the premises are materially unfit for use.

Both parties may terminate the lease if generally applicable contract termination grounds arise.

6.19 Forced Eviction

A tenant may be evicted prior to the originally agreed date if the grounds for termination discussed above (**6.18 Right to Terminate Lease**) arise. In such an event, eviction proceedings typically take one to one-and-a-half years.

In the event of eviction for failure to pay rent, a landlord may also seek to have the tenant evicted by way of execution proceedings. The execution office would serve a payment order on the tenant in such a case and, upon failure to pay within 30 days, begin the process to evict. This procedure is notably faster than eviction by court order.

Both eviction processes may be subject to appeal and the eviction order can be suspended while the appeal is pending.

6.20 Termination by Third Party

A government agency may be able to terminate a lease only in exceptional circumstances. One such instance may be when the leased real estate is subject to condemnation. In the event of condemnation the lessee does not receive compensation from the government. Another such instance is if the leased property is subject to demolition under the scope of the Urban Regeneration Law: in such an event, a lessee would be given a total of 90 days to evict the premises, and would be evicted by the government upon failure to voluntarily surrender the property.

7. Construction

7.1 Common Structures Used to Price Construction Projects

Structures used in the global market (turnkey and cost-plus-profit) are also used in the Turkish market. Turnkey structures are commonly used in public tenders. For private deals, turnkey or cost-plus-profit structures may be used depending on commercial agreement of parties.

Moreover, there is a unique method that is commonly used, which has been created for construction to be made over private parties' land, known as 'construction in return for flat'. Under this structure, the contractor constructs the building without receiving any cash payment. The owner makes the payment to the contractor in the form of a flat or flats; accordingly, the owner and contractor share the flats in the constructed building, in line with a ratio determined under the agreement (eg, owner 55%, contractor 45%). The owner does not make any other payment for the construction.

Revenue sharing, which is a structure that resembles partnership, has been gaining traction in the market lately. Revenue sharing involves the contractor taking on the construction and sale activities, and the landowner and the contractor sharing the collected revenues in previously agreed ratios.

7.2 Assigning Responsibility for the Design and Construction of a Project

Contractors assume the responsibility and construction of a project through construction agreements. However, as per the Turkish Code of Obligations, owners are responsible vis-à-vis third parties. In the event that owners are required to pay any compensation to third parties, they are entitled to have recourse to their contractor.

At the contractor level, design and construction work is outsourced through subcontractors that are hired by contractors.

7.3 Management of Construction Risk

Contractors generally assume the construction risk on a project, thus limitation of contractors' liability is not very common. Moreover, clauses containing waivers, indemnifications and limitations of liability in favour of contractors are not generally applied by courts.

7.4 Management of Schedule-related Risk

Provisions on schedule-related risks are subject to freedom of contract; therefore, parties may agree on certain milestones and penalties. This is commonly used in practice. As per the law, an owner is entitled to compensation if the contractor does not comply with milestones and deadlines specified under the agreement.

TURKEY LAW AND PRACTICE

7.5 Additional Forms of Security to Guarantee a Contractor's Performance

Parent guarantees, performance bonds (bank letters of guarantee), and retentions are common securities given by contractors. Requesting guarantees from contractors is common for valuable lands, where owners have negotiating power.

Another method that is often used in the tranches, but not necessarily in high-profile construction projects, is the exchange of negotiable instruments (eg, bonds or cheques). While negotiable instruments ordinarily are used to settle outstanding debts, they are sometimes used as security in construction agreements.

7.6 Liens or Encumbrances in the Event of Non-payment

Contractors are entitled to request the registration of a mortgage over the land to guarantee their receivables. Owners may request removal of the mortgage upon fulfilling their obligations under the construction agreement.

7.7 Requirements Before Use or Inhabitation

An occupancy permit, certifying that the construction has been completed in accordance with the official designs (projects), should be obtained before a project can be inhabited or used for its intended purpose.

8. Tax

8.1 VAT

Sale of lands within the scope of a commercial enterprise and land owned by limited liability companies and corporations are subject to VAT. The generally applicable VAT rate for land sales is 18%.

However, the VAT rate applicable for flats generated from urban regeneration is 1%. The VAT rate applied to sales of flats can be 1%, 8% or 18%, depending on the tax value of the concerned flat. Application of the 18% rate has been temporarily suspended until 31 December 2019, and the rate of 8% applies to properties that would otherwise qualify for the 18% rate until this time.

Hergüner Bilgen Özeke Attorney Partnership

Büyükdere Caddesi 199
Levent 34394
İstanbul
Turkey

Tel: +90 212 310 1800
Fax: +90 212 310 1889
Email: info@herguner.av.tr
Web: www.herguner.av.tr



VAT is paid by the purchaser.

The sale of lands held by limited liability companies and corporations for more than two years is exempted from VAT. However, this exemption does not apply to limited liability companies and corporations that conduct real estate business.

8.2 Mitigation of Tax Liability

Methods such as division, mergers, share transfers, etc, are used to benefit from mutual tax agreements and exemptions.

Moreover, Real Estate Investment Funds and Real Estate Investment Trusts are exempt from corporate income tax. These structures can also be used to mitigate tax liability.

8.3 Municipal Taxes

There is no periodic tax applicable for occupation of business premises. However, a fee determined by municipalities is paid for obtaining and renewal of operation permits. There is no specific exemption for operation permit fees.

Moreover, a real property tax is paid to municipalities; this is determined by municipalities according to the value of the respective lands. There are no significant exemptions for businesses with respect to real property tax.

8.4 Income Tax Withholding for Foreign Investors

Income generated by foreign investors which are not resident in Turkey is subject to withholding tax (eg, 20% for rental income). Rental income is subject to income tax for real persons and corporate tax for companies. Income tax applicable for real persons varies between 15% and 35%, depending on the rent amount. TRY5,400 (applicable for year 2019) of rental incomes from residences is exempted from income tax. Corporate tax is paid over rental income generated by limited liability companies and corporations. General corporate income tax is 22%.

There is no general tax exemption for income tax and corporate tax accrued over rental income. However, if rental income is generated by a real estate investment fund or real estate investment trust, the relevant income is exempted from corporate tax.

8.5 Tax Benefits

Depreciation deductions may be made over buildings, facilities, etc, as per the method and rates determined under the legislation (eg, 2% of the building's annual value). Moreover, expenses made for the respective real estate may also be deducted from the income subject to tax.

Additionally, real persons can deduct a flat 15% of income generated from lease of real property.

8.6 Key Provisions in the Federal Tax Reform Legislation

The matter is not relevant in this jurisdiction.