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Default In Real Estate Projects

To whom it may concern,

Below please see our responses to questionnaire on default in real estate projects.

1. CONSTRUCTION CONTRACTS

1.1. Defending Employer's Interests

1.1.1. Before entering into a construction contract, how can the employer check the financial standing of the contractor? Is credit/financial information publicly available in your jurisdiction?

There is not a publicly available system for obtaining financial information of contractor in Turkish jurisdiction. Employer may only check whether the contractor company is in liquidation from the Chamber of Commerce records or Trade Registry Gazette and whether there is any execution filed against the contractor from the courthouses.

1.1.2. Does your jurisdiction have standard conditions for construction contracts? If yes, what type of clauses do they provide for employers in case of contractor's insolvency?

Construction contracts are mainly regulated in the Articles of 471-486 of Turkish Obligation Code No 6098 titled "agreement for work". At that part of the Code of Obligations, subjects like the obligations of both contractor and owner, cancellation, impossibility of performance and insolvency of contractor are regulated. According to the Art.470 of Turkish Code of Obligations "construction contract is a contract whereby the contractor undertakes to carry out work and the customer undertakes to pay him for that work. In other words, construction

contract is defined as a contract by which the constructor undertakes to compose and deliver a structure in return of the fee paid by the employer. The fundamental elements of construction contracts under Turkish Law are creating a structure, fee and mutual agreement. These elements are fundamental elements of construction contracts in Turkish Law. If a construction contract contains all of these fundamental elements it is regarded as valid under Turkish Law. Therefore, since parties are not obliged to regulate insolvency conditions in the construction contracts in Turkish Law, there are not standard conditions for construction contracts in case of contractor's insolvency.

1.1.3. What kind of securities does the employer usually demand from the contractor?

There are not standard clauses which provide security to the employer in Turkish Law. However, in practice, there are some securities which the employer demands from the contractor. Usually employer provides a security to the employer with the construction contract or with an independent contract such as cash, bonds, bank guarantees, personal security, collateral security in order to reimburse damages of the employer caused by deficiencies or defects of the structure, delay in performance and other damages. These securities guarantee that contractor will carry out its obligation in accordance with the contract. The employer is obliged to return these securities after the contractor performs its obligation to compose a structure dully. Moreover in flat for land type of construction contracts, the employer usually demands some securities from the constructor. In this type of construction contract, while the contractor undertakes the construction of multi-storey building (apartment or office) on the land, the land lord (employer) incurs a debt of transfer land shares to the contractor in exchange for flats previously agreed upon by the parties. This contract can be made by transferring some land shares or all the land shares to the contractor at the beginning of the contract. In that case, the employer demands some securities from the contractor. In order to secure employer's rights over the land, the land shares transferred to the contractor by the employer are encumbered with mortgage on behalf of the employer.

1.1.4. In case of contractor's insolvency during the project, what alternatives does the employer have in order to carry it through?

According to the Court of Appeals decisions and doctrine, in the event of insolvency of the contractor, the construction contract is not terminated. Pursuant to the Art. 198 of the Enforcement and Insolvency Law, in case of insolvency of the Contractor, employer has right to register cash value of the structure which the contractor undertakes to compose to the bankrupt's estate as bankruptcy receivable. Upon this request of the employer, the trustee of bankrupt's estate has right to take over the project and complete it if the talents of the contractor is not substantial for completing the project. Trustee of the bankrupt's assets may decide to perform the non-monetary obligation, if it deems this more beneficial for the estate. In that case, the employer has right to demand a guarantee from the trustee of bankrupt's estate. This matter is also clearly indicated in the decision of the Court of Appeals for the 15. Civil Circuit dated 05.05.2011 and numbered 2052/2753.

It should be noted that, employer has always right to terminate the contract before the completion of the project by paying the value of the completed parts and all the damages of the contractor. Art. 484 of the Turkish Code of Obligations states that the employer may cancel the contract by only paying the work done before its completion and discharge all damages to the contractor.

1.1.5. What kind of role do clauses regarding transfer of title play in construction contracts? Are clauses under which the contractor's materials, equipment and tools are deemed to be the property of the employer upon the moment the contractor brings these to the site valid in your jurisdiction and do they limit the powers of the bankruptcy estate?

According to the Art. 471 of Turkish Code of Obligations unless otherwise agreed, the contractor has to provide the materials, tools and equipment which will be used in the construction process.

1.1.6. In case of employer's insolvency or loan default of the employer, is it typical that construction contracts contain instruments (e.g. novation agreements) for the financier to take over the project and the construction contract?

This applicable under Turkish Law unless otherwise agreed by the parties.

1.2. Defending Contractor's Interests

1.2.1. What kind of securities does the contractor usually demand from the employer? Are any of these securities mandatory in your jurisdiction?

As it is stated in the answer of question 1.1.2 the fundamental elements of construction contracts under Turkish Law are creating a structure, fee and mutual agreement. Therefore, regulating securities in construction contracts is not mandatory in Turkish jurisdiction. However, there is a security provided by Contractor by Law. According to the Art.893 of Turkish Civil Law, contractor may request the registration of their legal right of mortgage if he/she cannot receive the fee agreed by construction contract. By this legal mortgage right, contractor may ensure the employer's land and the structure to be encumbered with mortgage. Therefore the contractor may secure his/her unpaid wages. The necessary conditions for the registration of mortgages are, the receivable shall arise from the construction built on the land, and the registration shall be requested within 3 months from the date of completion of the structure. It should be noted that the contractor cannot request the registration of the mortgage if the employer gives an adequate security.

1.2.2. What other provisions (e.g. title retention, down-payment clauses etc.) are usually included in a construction contract to protect the contractor?

Although it is not mandatory in Turkish jurisdiction for the contractor to demand security from the employer, contractor usually demands some securities in order to guarantee his/her fee in practice. In case of employer delays in payments, contractor can use the right of detention over the structure that he made according to the Art.950 of Turkish Civil Code. If employer does not pay the fee of the contractor and does not give an adequate security, the contractor shall foreclose the pledged property and collect his/her receivable after informing the employer pursuant to the Art. 953 of Turkish Civil Code. Moreover, the contractor may use the right of detention in case of loan default of the employer even if its receivable is not urgent. In addition, according to the Art. 1009 of the Turkish Civil Code, the flat for land type of construction contracts can put an annotation onto the title deed. By putting an annotation onto the title deed, the right of property arising from construction contract can be claimed against the owners of

the rights acquired afterwards. Therefore, putting an annotation onto the title deed protects both the constructor's and employer's rights.

1.2.3. Please describe the main effects on the contract in case of insolvency of the employer and focus on the following points:

a) Does your jurisdiction have standard rules for termination of a contract in case of insolvency of the employer? If yes, can the parties deviate from these rules in their contract?

In Turkish jurisdiction, there are not standard rules for termination of a contract in case of employer's insolvency. In other words the construction contract does not end by law when the employer becomes insolvent. However the doctrine states that, if the employer becomes insolvent and the structure is not completed at the time of opening of bankruptcy, it should be accepted as presumption that the construction contract is terminated. On the other hand, the contract shall continue to be binding if the trustee of the bankrupt's estate declares that they will take over the project and became one of the parties of the construction contract. If the contractor has not requested registration of the legal right of mortgage yet, the contractor demand security from the insolvent employer or trustee of bankrupt's assets for his/her fee receivable upon the insolvency of the employer. In case of such security is not provided by employer or trustee of bankrupt's assets in a reasonable time, the contractor has right to terminate the contract. Although it is advantageous that trustee of the bankrupt's assets to take over the construction contract instead of the employer, this option rarely applied in practice because of the reason that the trustee of bankrupt's assets does not have enough money to provide security to the contractor.

b) If the contract does not end by law, who gets to decide whether the contract is terminated or not?

As it is stated above, there are not standard rules for termination of a contract in case of employer's insolvency. Therefore, the contract's effectiveness depends on some possibilities. If the trustee of bankrupt's assets decides not to enter into construction contract it is accepted by the doctrine that the contract is deemed as terminated. During the bankruptcy process, trustee of the bankrupt's assets have

a duty of care to act in the best interests of the company, refrain from getting involved in anything that would be detrimental to the company or deprive it of profit or advantage which his skill and ability might properly bring to it. Therefore, trustee of the bankrupt's assets would decide not enter into construction agreement if it would be detrimental to the bankrupt. if in case of the trustee of bankrupt's assets decides to take over the construction contract but fails to provide adequate security to the contractor, the contractor has right to terminate the contract.

c) If the contract is carried forward, is the employer still in charge or does the liquidator take over?

If the trustee of the bankrupt's assets decides to enter into constitution contract instead of the employer and provides adequate security to the contractor upon his/her request the construction contract is carried forward. In that case, trustee of the bankrupt's assets take over the contract and from that moment, the trustee of the bankrupt's assets is in charge.

1.2.4. What happens to the claim for remuneration of the contractor towards the employer:

a) In case of termination of the contract?

In case of termination of the construction contract, the contractor has right to register its remuneration claim to the bankrupt's estate as bankruptcy receivable with its default interest. Bankruptcy procedure is carried out as follows: If the assets of the company will not satisfy all its debts, the execution office invites all the company's creditors to declare their debts within a period of a minimum of 20 days to a maximum of three months. This period will start on the invitation's publication in a national newspaper distributed in all Turkey with a minimum circulation number of 50,000, at the registered head office of the company, and in the Trade Registry Gazette. This invitation will also announce the date of the first meeting of creditors. Creditors representing at least 25% of the total debt of the company must be present for the meeting to have the necessary quorum. Decisions are taken by a simple majority of the participants' votes, representing more than 50% of the total debt. This meeting will elect the bankruptcy

administration. The bankruptcy administration will convene a second creditors' meeting, with 20 days' prior notice. At this meeting, the creditors decide on how to sell the company assets, which will be through public sale or bargaining (that is, a method to sell the debtor's asset by negotiating the terms of the agreement with several parties in order to sell the asset for an advantageous price). After the sale and liquidation of the company assets, the proceeds from the sale are distributed to the creditors in accordance with the ranking list.

b) In case the contract is carried forward?

If the trustee of the bankrupt's asset decides that to perform the obligation arising from the construction contract is more beneficial for the estate, it may decide to enter into construction contract instead of the employer. Upon that, the trustee of the bankrupt's assets is in charge in performing the contract. Therefore, contractor shall assert his claim of remuneration to the trustee of bankrupt's assets. The remuneration of the contractor shall be paid by the trustee from the bankrupt's estates.

1.2.5. During the project, who usually owns the parts of the building that have already been finished? Are there any rules in your jurisdiction that would allow the contractor to get a freehold of the construction site and continue the project with a different employer?

According to the Article 718 of Turkish Civil Code, the property over land contains the air above and the layers below as long as there is a benefit in using them. This scope of the property right covers the building, plants and resources. Therefore pursuant to principle stated in the Art. 718 of Turkish Civil Code, during the project the party who owns the land shall have the ownership of the building that has already been finished. In many cases, since the employer has the property right over the land, he also owns the parts of the building that have already been finished. Contractor, in order to protect his rights may request the registration of their legal right of mortgage if he/she cannot receive the fee agreed by construction contract according to the Art.893 of Turkish Civil Law. There are not any rules in Turkish jurisdiction that would allow the contractor to get a freehold of the construction site and continue the project with a different employer.

1.2.6. What kind of provisions should/can a contractor include in the contracts with his subcontractors to protect himself in case of the employer's insolvency?

According to the Art.893 of Turkish Civil Law, contractor may request the registration of their legal right of mortgage if he/she cannot receive the fee agreed by construction contract. By this legal mortgage right, contractor may ensure the employer's land and the structure to be encumbered with mortgage. Therefore the contractor may secure his/her unpaid wages. Although it is not mandatory in Turkish jurisdiction for the contractor to demand security from the employer since there is a security provided by the law, contractor should demand some securities in order to guarantee his/her fee from the employer. In case of employer delays in payments, contractor can use the right of detention over the structure that he made according to the Art.950 of Turkish Civil Code. If employer does not pay the fee of the contractor and does not give an adequate security, the contractor shall foreclose the pledged property and collect his/her receivable after informing the employer pursuant to the Art. 953 of Turkish Civil Code. In addition, according to the Art. 1009 of the Turkish Civil Code, the flat for land type of construction contracts may demand to put an annotation onto the title deed. By putting an annotation onto the title deed, the right of property arising from construction contract can be claimed against the owners of the rights acquired afterwards. Moreover, contractor may demand cash, bonds, bank guarantees, personal security, collateral security in order to protect himself and the subcontractors in case of the employer's insolvency.

2. LEASE CONTRACTS

2.1 Is a lease affected by the foreclosure of a mortgage or other in rem guarantee over the leased property? May the new landlord terminate the lease?

Art. 311 of Turkish Code of Obligations states that, " If a third party gets a real right on the property which affects the right of the lessee after the conclusion of the agreement, the provisions relevant to the transfer of leasehold shall apply by the way of comparison." According to the Art. 310 of Turkish Code of Obligations titled as transfer of the leasehold, "If the leasehold is transferred to another party after the conclusion of the agreement for any reason; the new proprietor shall be a party to the lease agreement." Therefore as per articles 311 and 310 of Turkish

Code of Obligations, a lease contract is not affected by the foreclosure of a mortgage or other in rem guarantee over the leased property. The new landlord will be the party of the lease contract by law due to the Art.310. Thus, the new landlord shall comply with the terms of lease contract and grant the right to use the property or benefit from such use to the tenant. However, the law also stipulates a regulation that allows the new landlord to terminate the lease contract. According to the Art. 351 of Turkish Code of Obligations “The new owner of the leasehold may terminate the lease agreement with a suit that would be brought after six months he noticed the lessee in a month beginning from his ownership if he necessitates to use the leasehold as residence or work place for his spouse, descendants, lineal ancestors, legal dependents, himself. The new owner may use his cancellation right due to his necessity with a suit that would be brought in a month beginning from the end of contract duration.” Therefore, although the new landlord the new landlord will be the part of the lease contract by law, he has right to terminate the lease in conformity with the conditions set forth in Article 351.

2.2 Does your jurisdiction afford any protection for the tenant in this case, for example, by guaranteeing the continuity of the lease agreement or a right of first refusal for acquisition of the leased property? Are there any requirements that need to be fulfilled if the tenant wishes to oppose these rights (if applicable) against his new landlord.

According to the Art. 1009 of the Turkish Civil Code, the rights arising out of the lease contracts may be subject of a caution on the land registry record. This matter is also indicated in the Art. 312 of the Code of Obligations which states that in case of immovable property leases, the entry of a caution on the tenant’s right for tenancy to the land registry record may be decided through the agreement. The entry of a caution on the tenant’s right for tenancy to the land registry record shall prevent the termination of the lease contract according to the article 351 of Turkish Code of Obligations by the new landlord. To prevent the new landlord from terminating the contract, there shall be an agreement of a caution on the tenant’s right for tenancy between the tenant and the landlord. Besides, this agreement shall be annotated to the land registry record.

2.3 In case of insolvency of the tenant, is the landlord entitled to terminate the lease? Are insolvency clauses common in lease agreements in your jurisdiction? Are they normally upheld in court?

Insolvency of the tenant is counted as one of the reasons of extraordinary termination in the Turkish Code of Obligations. According to Article 332 of the Code of Obligations titled as bankruptcy of the tenant, if the tenant bankrupts after handing over the leased property, the landlord may ask for a warranty for executory rentals. The landlord shall give a reasonable time to the tenant and the bankrupt's estate for getting the warranty. If such a warranty is not given to the landlord in the specified time, the landlord may immediately terminate the contract without following a new termination notification period. Therefore, since the insolvency of the tenant is explicitly regulated in the Article 332 of Turkish Code of Obligations, insolvency clauses are not common in lease agreements. Even though, there is not a provision bring forth in the lease agreement, the landlord is entitled to terminate the lease according to the abovementioned article, if a warranty is not given.

2.4. What kind of securities does the landlord usually demand from the tenant? How tenant's insolvency may affect the ability of the landlord to execute these guarantees and collect rent and other monies due to under the lease?

According to the Art. 342 of the Turkish Code of Obligations in residence and roofed work place leases, if the tenant is obliged to provide security by the contract, the security is limited to maximum three-month lease cost. If cash or negotiable papers is decided to be provided as security, the tenant shall pay the money into a forward savings account not drawing out without approval of the landlord, or deposit negotiable papers in the bank. The bank may release such security only by the consent of both parties, finalization of execution proceedings, or decision of the court. If the landlord notifies the bank in three months following the end of the lease agreement period that he has gone to court related to the lease contract or has initiated execution or bankruptcy proceedings, the bank is obliged to release the security on the request of tenant.

On behalf of Yalçın&Toygar&Tüfekçi Law Firm

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