



## **Turkey: Freeze on Voting Rights in Joint-Stock Companies**

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### **I. General Overview**

In joint-stock companies, shareholders, personally or through their representatives, vote in the general assembly meetings in proportion to their shares thereby indirectly contributing to the management, organization and future of the company. In the general assembly meetings, shareholders decide on significant matters such as appointment/dismissal of board members and auditors, share capital increase/decrease and dividend distribution. Having said that, voting rights of shareholders freeze under certain circumstances where shareholders are not eligible to exercise their voting rights in the general assembly meetings. Although there are certain circumstances which affect voting rights of shareholders under capital markets laws, in this article, our aim is to reveal cases that cause blocking voting rights under the Turkish Commercial Code (“TCC”).

### **II. General Consequences of the Freeze**

As a result of the freeze on voting rights, the relevant shareholder cannot exercise its voting rights deriving from the shares subject to freezing. Although it is not explicitly stated in all TCC provisions regulating freeze on voting rights, as a natural consequence, such shares are not taken into account in calculation of general assembly meeting quorums. It is also worth mentioning that freeze on voting rights has a permanent nature. For instance, in case of lack of voting rights, shareholders cannot exercise their voting rights in certain general assembly meetings and for certain meeting agenda items. On the other hand, in case of freeze on voting rights, shareholders whose shares are frozen cannot use their voting rights in all general assembly meetings until the issue, causing freeze on voting rights, is resolved.

### **III. Reasons for Freeze**

#### **1. Joint-Stock Company’s Acquisition of its Own Shares**

Article 379 of the TCC introduces a restricted system for joint-stock companies to acquire its own shares. In this regard, Article 379 of the TCC does not allow joint-stock companies to acquire their own shares for consideration in an amount exceeding 1/10 of their original or issued share capital or if this threshold will be exceeded at the end of a transaction. Companies may acquire their own shares only within the abovementioned thresholds and by complying other rules set out in the TCC, such as authorization of board of directors by the general assembly. This restriction is also applicable in case of a (i) third party’s acquisition of

shares on its behalf but on company's account and (ii) subsidiary's acquisition of parent company's shares.

Under Article 389 of the TCC, the shares acquired by the company and the shares of parent company acquired by the subsidiary are not taken into account in calculation of the meeting quorum of the general assembly meeting of the parent company. In addition, except for the acquisition of gratis shares, company's acquisition of its own shares does not grant any shareholding rights to the company. It is also explicitly stated that the voting rights of the shares subject to the acquisition and the related rights are frozen in the event that the subsidiary acquires the shares of the parent company.

The main reason behind freeze on voting rights is to protect the balance between the company's organs, since the board of directors (as the management and representation organ) would be entitled to use voting rights of the company in case of company's acquisition of its own shares. In the Turkish law doctrine, it is generally agreed that misuse of the voting rights of the acquired shares by the company management may adversely affect the balance of power between the general assembly and board of directors.<sup>1</sup>

## **2. Breach of the Notification and Registration Requirements**

A notification must be made to the trade registry as per Article 198 of the TCC and Article 107 of the Regulation on Trade Registry, once shareholding of a company ("shareholder"), directly or indirectly, exceeds or drop below 5%, 10%, 20%, 25%, 33%, 50%, 67% or 100% of the share capital of another company ("target company"). In such a case, the shareholder (whose direct or indirect shareholding in the target company exceeds or drop below the said thresholds) must notify the target company, in writing, within ten days following completion of the transaction. Following receipt of the notice, the target company must notify this to the relevant trade registry within ten days. Notification must be registered with the trade registry and announced in the trade registry gazette.

Article 198/2 of the TCC states that all rights arising from the relevant shares, including the voting rights, freeze until the registration and announcement processes are completed. The reason behind this notification is explained within the reasoning of Article 198 as to ensure transparency regarding these transactions. Freezing of all rights deriving from the relevant shares, on the other hand, constitutes the sanction to be imposed in case of breach of this obligation.

Relevant provisions related to 198 notification do not explicitly stipulate whether shares subject to the freeze on voting rights are taken into account in the general assembly meeting

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<sup>1</sup> Faruk Yeşilyurt, Anonim Ortaklıkta Pay Sahibinin Oy Hakkının Donması, 2017, p.136.

quorums. However, as a natural consequence of the freeze on voting rights, it should be accepted that such shares are not taken into account in calculation of the meeting and decision quorums of the general assembly meetings.<sup>2</sup>

### **3. Cross Shareholding**

Article 197 of the TCC defines cross shareholding as stock corporations holding at least 1/4 of each other's share. Consequences of cross shareholding are regulated in Article 201 of the TCC. Accordingly, a stock corporation which deliberately becomes part of a cross shareholding may use only 1/4 of its total votes arising from the shares subject to participation and its other shareholding rights; all other shareholding rights freeze except for the right to acquire the gratis shares. Additionally, these shares are not taken into consideration in calculation of the general assembly meeting quorums. Under Article 201/2 of the TCC, this restriction does not apply if a subsidiary acquires the shares of its parent company, or if both companies are parent companies of each other.

### **IV. Conclusion**

Under the TCC, there are certain cases causing freeze of voting rights. As a result of this, shareholders whose shares are frozen cannot exercise their voting rights until the issue causing this is resolved. In addition, the shares subject to freeze on voting rights are not taken into consideration in calculation of the decision and meeting quorums of the general assembly meetings.

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<sup>2</sup> Yeşilyurt, p.218.