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The Court of Appeals Sheds Light on "Just Cause" for Termination, Exit Right and Squeeze-out of Shareholders

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I. Introduction

"Just cause" is a term that is used frequently under the Turkish Commercial Code No. 6102 ("TCC"). In broad terms, "just cause" may be defined as a situation in which the relationship between a shareholder and the company and/or between a shareholder and other shareholders becomes unbearable or untenable for valid legal reasons. Although the term "just cause" is frequently employed under the TCC, Turkish lawmakers did not opt to provide an explicit definition of this term under the TCC and instead delegated this duty to the doctrine and the courts.

In this article, we will focus on the use of the term "just cause" in the context of the termination of limited liability companies, exit right and squeeze-out of shareholders in limited liability companies, and we will assess and evaluate the purpose and meaning of the term in light of the recent Court of Appeals decisions.

II. Termination by Just Cause

Article 636 of the TCC lists the circumstances in which a limited liability company shall be terminated. In addition to the customary reasons for termination, such as termination pursuant to the articles of association, initiation of the bankruptcy process following a bankruptcy decision, termination through a resolution of the general assembly of shareholders, or termination as foreseen by other laws, the provision also allows each shareholder to file a lawsuit against the company to request the termination of the limited liability company, if there is "just cause" to terminate the company. Upon request, the court may terminate the company or rule for the "squeeze-out" of the plaintiff shareholder, or for another resolution that is acceptable and suitable for the case at hand.

The reasoning of Article 636 of the TCC refers to Article 531 of the TCC, in which the termination of joint-stock companies by "just cause" is regulated. The reasoning of Article 531 also confirms that the TCC does not explicitly define what constitutes "just cause," and that its definition is left to be decided by the relevant doctrine and the courts. The reasoning of Article 531 lists certain examples of "just cause" that have been accepted and recognized under Swiss

legal doctrine. For example, unlawful invitation of the shareholders to the general assembly meetings, continual violations of the minority shareholders' rights or the personal rights of the shareholders, obstruction or hindrance of the right to demand information and examination, continuous losses incurred by the company, and constant declines in profits are listed among the examples of "just cause" that are recognized under Swiss doctrine.

Since there is no clear-cut definition or elucidation on the scope and content of the term "just cause" in Turkish law, courts have been required to evaluate each matter on a case-by-case basis. Accordingly, the Court of Appeals has shed light on the meaning of "just cause" for the termination of limited liability companies over the years through its rulings.

In one illuminating case, where (i) the limited liability company had incurred continuous losses, (ii) significant disagreements existed between the shareholders, (iii) the limited liability company was in debt, (iv) the limited liability company could not carry out its business activities, and (v) the shareholders had no interest in the continuation of the company, the 11th Civil Chamber of the Court of Appeals ruled for the termination of the limited liability company (decision dated October 18, 2016, and numbered 11101/8204).

In another significant case, the 11th Civil Chamber of the Court of Appeals ruled (with the decision dated June 13, 2016, and numbered 10730/9482) for the termination of a family-run limited liability company due to the following factors: (i) shareholders were divorced, (ii) defendant shareholder had established another company with a different scope of activity, (iii) the manager had failed to provide due care for the management of the company.

Furthermore, in several other cases, the following reasons have also been accepted and recognized as "just causes": (i) mismanagement of the company, (ii) personal interests coming to the forefront (*i.e.*, being prioritized) among the shareholders of the limited liability company, (iii) company being in debt, (iv) the fact that it has become impossible to realize or fulfill the common objectives of the limited liability company. However, the Court of Appeals has also ruled that there are certain circumstances which do not constitute "just cause" for the termination of a limited liability company, such as the existence of due tax debts or the non-distribution of dividends.

III. Exit Right of Shareholders

Article 638 of the TCC sets forth that each shareholder has the right to exit and depart from a limited liability company by filing a lawsuit if there is "just cause" and if there is a provision in the articles of association of the company providing an "exit right" for shareholders.

The Court of Appeals has illuminated what constitutes a "just cause" that is sufficient to allow a shareholder to exercise its exit right in a limited liability company. In this context, the Court has ruled that (i) disagreements between shareholders, (ii) continuous violation of a shareholder's right to obtain information on the management and activities of the company, (iii) the alienation of a shareholder from the company, and (iv) a situation in which the company falls into debt due to the actions of the directors, would be deemed as "just causes" (11th Civil Chamber of Court of Appeals' decision dated June 22, 2016, and numbered 2015-9114/6883).

IV. Squeeze-out of Shareholders

Article 640 of the TCC regulates that a company may request the "squeeze-out" of a shareholder from a limited liability company due to (i) the presence of circumstances set forth in the articles of association of the company (pursuant to a general assembly decision), and (ii) "just cause."

The 11th Civil Chamber of the Court of Appeals has ruled (in a decision dated November 21, 2016, and numbered 2015-11660/8995) that (i) adverse statements against other shareholders, and (ii) breach of the duty of loyalty toward the company and other shareholders, will be deemed as "just causes" for squeezing out the relevant shareholder from the limited liability company.

IV. Conclusion

The continuity and preservation of companies is a fundamental tenet under Turkish laws. Therefore, the termination of a company should be the last resort for resolving disputes between shareholders and/or between a shareholder and the company. On the other hand, taking into account the necessities and dynamics of business relationships, Turkish laws do value and consider the possibility of the parties' wishing to leave a business partnership. Therefore, the concept of "just cause" is of great significance in cases where one or more parties would like to terminate a business partnership. Since there is no explicit definition of the term "just cause" provided under Turkish laws, the courts exercise broad discretion to define the term according to doctrine and their own judicial philosophies, and practitioners will be well advised to continue to follow the decisions of the Court of Appeals very closely.

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