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ATTORNEY PARTNERSHIP

Briefing note

February 2018

# Turkey introduces new restrictions for FX Loans to control Turkish companies' FX exposure

## Decree No. 32 on the Protection of the Value of the Turkish Currency has been amended with effect from 2 May 2018 to keep FX borrowings at bay.

### Introduction

As anticipated, the Council of Ministers passed an amendment giving effect to significant changes to the well-known foreign exchange legislation of Turkey, namely Decree No. 32 on the Protection of the Value of the Turkish Currency, (originally issued in 1989 and amended from time to time) (the "**Decree**"). The amendment is published in the Official Gazette dated 25 January 2018 and will come into force on 2 May 2018 (the "**Amendment**").

The changes primarily relate to the rules regulating extension of loans, both onshore and offshore, as more particularly described below. There is a distinction made between loans denominated in TRY ("**TRY Loans**") and loans denominated in foreign currency ("**FX Loans**") and the familiar concept of foreign currency indexed loans have been disallowed.

There are a number of restrictions introduced to the legislation with a view to curtailing the use of FX Loans by local companies that do not regularly benefit from foreign currency denominated revenues. The other main restriction relates to a credit balance threshold of USD 15 million.

Accordingly, as further explained in detail below, Turkish residents having a credit balance of at least USD 15 million or meeting certain other criteria may, subject to certain conditions, obtain FX Loans. For the purposes of determining the threshold, "credit balance" is deemed to include outstanding onshore and offshore FX Loans as at the utilisation date of the proposed loan.

### FX loans to be obtained from abroad

As opposed to the current position under the Decree, where Turkish residents can, relatively freely, obtain FX Loans from abroad, once the Amendment comes into effect, Turkish residents will only be able to obtain FX Loans from abroad if certain conditions are met as further described below.

Accordingly offshore FX Loans can only be obtained:

- by state entities and enterprises, banks, financial leasing companies, factoring companies and financing companies;
- by Turkish legal entities having an outstanding credit balance of at least USD 15 million as at the proposed utilisation date of the loan;
- by Turkish legal entities under an appropriate investment incentive certificate;
- for the financing of certain machinery and equipment listed under the Council of Ministers' Decree no. 2007/13033;
- by Turkish legal entities that were awarded domestic tenders which were open to international bidders;
- by Turkish legal entities carrying out defence industry projects approved by the Undersecretariat of Defence Industry;
- by Turkish legal entities appointed for carrying out projects under the PPP model;
- by Turkish legal entities that do not have foreign currency denominated revenues within the past three fiscal years, but can evidence and verify their estimated foreign currency denominated revenues (provided that the amount of FX Loans to be so obtained cannot

exceed the amount of the estimated foreign currency denominated revenues); or

- by Turkish legal entities fulfilling other criteria to be subsequently determined by the Ministry in charge of the Undersecreteriat of Treasury,

***Irrespective of whether or not such Turkish legal entities obtaining the loans have foreign currency denominated revenues***.

It is important to note that ***if any of the exceptions listed above apply***, then the restriction with respect to the amount of the loan will not be applicable even if the relevant Turkish legal entity has an outstanding credit balance less than USD 15 million as at the utilisation date of the loan.

Save for the entities enjoying the exemptions noted above, ***if the Turkish legal entities have foreign currency denominated revenues*** and they have an outstanding ***credit balance*** of ***less than USD 15 million*** as at the utilisation date of the loan, then the sum of the amount of the FX Loan to be obtained from abroad and the outstanding credit balance of such entity cannot exceed the sum of the foreign currency denominated revenues generated within the past three fiscal years.

Currently, Turkish real persons may obtain FX Loans from abroad under limited circumstances set out in the Decree (e.g. for commercial or professional purposes). Once the Amendment comes into effect, it will not be possible for Turkish real persons to obtain FX Loans from abroad.

## Onshore FX Loans

Currently under the Decree, Turkish residents can obtain FX Loans from Turkish institutions subject to certain conditions set out in the Decree, the most well-known condition being that only FX Loans with an average maturity of more than one year and having an amount equal to or more than USD 5 million would be eligible.

The Amendment introduces more restrictive conditions for obtaining onshore FX Loan by Turkish residents.

Furthermore, FX Loans can only be obtained from Turkish banks, financial leasing companies, factoring companies and financing companies:

- by state entities and enterprises, banks, financial leasing companies, factoring companies and financing companies;
- by Turkish legal entities having an outstanding credit balance of at least USD 15 million as at the proposed utilisation date of the loan;
- by Turkish legal entities under an appropriate investment incentive certificate (this condition currently exists under the Decree);
- for the financing of certain machinery and equipment listed under the Council of Ministers' Decree no. 2007/13033;
- by Turkish legal entities that were awarded domestic tenders which were open to international bidders (this condition currently exists under the Decree, although its scope is slightly different);
- by Turkish legal entities carrying out defence industry projects approved by the Undersecretariat of Defence Industry (this condition currently exists under the Decree);
- by Turkish legal entities appointed for carrying out projects under the PPP model;
- by Turkish legal entities that do not have foreign currency denominated revenues within the past three fiscal years, but can evidence and verify their estimated foreign currency denominated revenues (provided that the amount of FX Loans to be so obtained cannot exceed the amount of the estimated foreign currency denominated revenues);
- for foreign currency denominated financial leasing transactions in relation to acquisition of certain machinery and equipment listed under Council of Ministers' Decree no. 2007/13033 (this condition currently exists under the Decree, although its scope is slightly different);
- by Turkish legal entities if (a) such Turkish legal entities hold as collateral in Turkish branches of the banks, foreign currency or foreign currency denominated securities issued by, or with the guarantee of, central banks and central administration of OECD member states and (b) the amount of FX Loan to be obtained does not exceed the total amount of such foreign currency or foreign currency denominated securities (this condition currently exists under the Decree); or

- by Turkish legal entities fulfilling other criteria to be subsequently determined by the Ministry in charge of the Undersecreteriat of Treasury.

Turkish legal entities are allowed to obtain FX Loans onshore if any of the conditions listed above is applicable, ***irrespective of whether or not such Turkish legal entities have foreign currency denominated revenues***.

***If any of the exceptions listed above apply***, then the restriction with respect to the amount of the loan will not be applicable even if the relevant Turkish legal entity has an outstanding credit balance of less than USD 15 million as at the utilisation date of the loan.

Similar to the FX Loans to be obtained from abroad, for onshore FX Loans, ***if the Turkish legal entities have foreign currency denominated revenues*** and they have an outstanding ***credit balance*** of ***less than USD 15 million*** as at the utilisation date of the loan, then the sum of the amount of the onshore FX Loan and the outstanding credit balance of such entity cannot exceed the sum of the foreign currency denominated revenues generated within the past three fiscal years.

It is important to note that, with the introduction of the new conditions, the restrictions with respect to the term and amount of FX Loans that can be extended by Turkish banks will no longer be applicable as from the effective date of the Amendment. Accordingly, if one of the conditions set out in the Amendment applies, then Turkish residents will be able to obtain onshore FX Loans without being limited with more than one year average maturity and USD 5 million.

Once the Amendment comes into effect, Turkish real persons shall no longer be able to obtain onshore FX Loans.

## FX indexed loans

Following the entry into force of the Amendment, Turkish residents will no longer be able to obtain foreign currency indexed loans either from abroad or within Turkey.

## TRY Loans

The Amendment does not introduce any notable change with respect to obtaining onshore and offshore TRY Loans. In the case of loans extended by offshore entities, Turkish residents can freely obtain TRY Loans, provided that the proceeds of such loans are transferred through the banks licensed in Turkey.

## Commodity loans

Under the Amendment, Turkish entities may still extend commodity loans to Turkish residents which is similar to the current position.

## Monitoring

Pursuant to the Amendment, for offshore FX Loans, the Turkish intermediary banks through which the proceeds of the loans flow, and for onshore FX Loans, the Turkish banks, financial leasing companies, factoring companies and financial companies extending the loans, are responsible for monitoring compliance with the restrictions on the credit balance and the amount of the FX Loans. Accordingly, the Turkish intermediary banks and lending entities will have increased responsibilities in monitoring the use of onshore and offshore FX Loans.

## Sanctions

As explained above, for both onshore and offshore FX Loans, there is a restriction with respect to the amount of FX Loan that can be utilised if the relevant Turkish legal entity borrowing the FX Loan has an outstanding credit balance of less than USD 15 million.

If it is later determined, for offshore FX Loans, that at the time of extending the loan, the credit balance made available by foreign banks (including offshore branches of Turkish banks but excluding branches in free zones), financial leasing companies, factoring companies and financing companies had exceeded the sum of foreign currency denominated revenues for the past three fiscal years, the excess part will either be accelerated or converted into TRY Loan. Similarly, this rule also applies to onshore FX Loans, except that, for the purpose of calculating the credit balance, only outstanding onshore FX Loans are taken into account.

This is because, Articles 17(4)(c) and 17/a(4)(c) imply that for the purpose of the above determination, the credit balance is to be calculated taking into account the amount of *offshore* FX Loans only for offshore borrowings, and the amount of *onshore* FX Loans only for onshore borrowings, rather than both onshore and offshore FX Loans (which may not be the actual intention, since the definition of "credit balance" covers both).

On the other hand, as to the exception relating to having a credit balance of at least USD 15 million, the Amendment is not clear on what will happen if it is later determined at the time of utilisation of the loan the credit balance was less than USD 15 million. This point may be further clarified under the regulations to be issued by the Central Bank or the Ministry in charge of the Undersecreteriat of Treasury.

## Transition Period

The onshore and offshore FX Loans extended prior to the effective date of the Amendment will be grandfathered, meaning that they are not required to be terminated. However, following the entry into force of the Amendment, FX Loans obtained prior to the effective date of the Amendment by Turkish legal entities whose outstanding credit balance (including offshore and onshore FX Loan) is less than USD 15 million may only be renewed if they comply with the exceptions set out in the Amendment. On the other hand, foreign currency indexed loans cannot be renewed, but they may be converted into FX Loans should they comply with the exceptions set out in the Amendment.

## Conclusion

- These changes are expected to impact, in particular, small or medium sized enterprises with no foreign currency denominated revenue.
- Companies that can evidence generating (actual or potential) foreign currency denominated revenues will be affected to a lesser extent so long as they remain compliant with the rules.
- There are still some areas that may require further clarification which may be addressed in the regulations to be issued by the Central Bank or the Ministry in charge of the Undersecreteriat of Treasury as contemplated under the Amendment.

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