

Debt Assumption Regulation

The Regulation Regarding Debt Assumption by the Undersecretariat of Treasury of Turkey entered into force on 19 April 2014. This briefing note provides a summary of the main developments addressed by the Regulation.

Introduction

By a change to Article 4 of the Public Finance and Debt Management Law (the "**Public Finance Law**") on 29 June 2012, assumption by the Undersecretariat of Treasury ("**UT**") of the external debt financings obtained for certain investments realised under the build-operate-transfer or build-lease-transfer models in case of early termination of the project agreement was made available.

On 9 March 2013, the debt assumption provisions under Article 4 were rearranged as a new Article (Article 8/A) of the Public Finance Law. This new Article 8/A was more comprehensive and introduced both changes to the previous provisions (such as the minimum investment amount threshold for certain projects) and new provisions (such as the limit of debt assumption). It also envisaged a regulation to be published that would set forth the governing principles and procedures for the debt assumption by UT.

As expected, the Regulation is a more detailed piece of legislation and includes specifics that were not included under the Public Finance Law. However, some aspects seem more restrictive than expected and may not be universally welcomed by financiers.

Eligibility for Debt Assumption

The minimum investment amounts required for projects eligible for debt assumption are set forth under the Public Finance Law. As a reminder these are, 1 billion Turkish Liras for projects realised under the build-operate-transfer model and 500 million Turkish Liras for projects procured by the Ministry of Health or the Ministry of Education under the build-lease-transfer model. The Regulation sheds some light on how these investment amounts will be determined. If the project is subject to the approval of the High Planning Council, the investment amount included in the feasibility report submitted to the High Planning Council will be taken into account. If no High Planning Council decision is necessary, the investment amount in the feasibility report used to prepare the tender documentation will be taken into account.

Authorisation for the Debt Assumption

As set out in the Public Finance Law, a Council of Ministers' Decree is necessary to be obtained for debt assumption. However, the Regulation suggests that such Decree should be obtained both before the tender and

before the execution of the debt assumption agreement. The debt assumption agreement signed following such authorisation will not be published in the Official Gazette, thus information on the debts assumed by UT will not be publicly available. A separate Council of Ministers' Decree is necessary for assumption of the renewed or refinanced debt or for amending any agreements that would affect the scope, cost or terms and conditions of the obligations of UT.

The Regulation also requires the relevant public administration not to have any unpaid obligation against UT in order for its project to be eligible for debt assumption. In addition, a protocol should be entered into between certain public administrations and UT regulating for the reimbursement obligations of the administration vis-a-vis UT.

Scope of the Debt Assumption

The Regulation distinguishes between the consequences of a termination due to the project company's default and termination due to reasons not attributable to the project company. In the former instance, it does not allow the debt assumption to be higher than 85% of the senior debt – defined as the debt obtained from abroad for the relevant investment – and all related financing costs whereas there is no such limit for the latter case.

The Regulation also introduces a limit for the unwinding costs for derivative products – which cover both interest rate and foreign currency risks – that can be covered by the debt assumption. UT will determine such limit for each relevant project but in any case it cannot be higher than 10% of the senior debt (excluding any default interest).

If it transpires that despite payment being made by the relevant administration, the amounts due under the senior debt (i.e. principal, default interest and other financing costs) remain unpaid because of the project company's default, such amounts will only be covered by the debt assumption if the shareholders of the project company provide a joint and several surety (i.e. a weaker form of guarantee subject to more strict formal requirements) to UT. The amount of such surety will be determined by UT but will be at least 10% more than the highest instalment payment to be made to the senior creditors.

The debt assumption cannot cover loans utilised to finance the equity undertaking or to finance the increased costs or liquidity requirements arising from the default of the project company.

Limit of Debt Assumption Undertaking

The limit for debt assumption for each financial year will be determined in the central administration annual budget law. The Council of Ministers is authorised to increase this limit by as much as 100% upon proposal of

the Minister in charge of UT. In order to manage the limit, the public administrations will send information to UT relating to the projects they envisage should benefit from debt assumption in the following financial year by the end of July of the previous financial year using the form attached to the Regulation.

Payment by UT

The final amount of the debt which is to benefit from the debt assumption will be notified by the senior creditors to UT following receipt of a copy of the project agreement termination notification sent to UT by the relevant public administration.

The Regulation prohibits restricting the right of UT to elect the payment method of the assumed debt (i.e. according to the original repayment schedule or as a lump sum payment). If UT chooses to pay the assumed debt as a lump sum payment, the term for such payment cannot be shorter than 2 months following notification to the creditors to that effect. Other terms and conditions of the payment will be determined under the debt assumption agreement.

Supervision and Reporting

The project company will obtain a foreign financing number from UT before utilising the senior debt. For the debt assumption agreements that have been executed before this Regulation entered into force, the relevant project company should apply to receive such number within 15 days following the date of publication of the Regulation.

The project company will notify UT and the relevant public administration of the utilisation and repayment of the senior loan by using the form attached to the Regulation within 10 business days of the utilisation or repayment. The signed copies of the senior loan agreement as well as agreements relating to derivative products will also be submitted to UT. UT may request any other information and documentation relating to the financing.

Exemption

The Regulation addresses the exemption the Public Finance Law provides for the ongoing projects. The projects that have been tendered prior to the entry into force of Article 8/A of the Public Finance Law will not be subject to the requirement to obtain the affirmative opinion of UT or to provisions regarding partial debt assumption or limit of debt assumption. Accordingly, it is still not clear whether excluding these projects from the requirement to obtain the affirmative opinion of UT before the tender but not excluding them from the requirement to obtain the affirmative opinion of UT before execution of the project agreement is intentional or just an omission. Furthermore, the Regulation requires the Council of Ministers' Decree to be obtained before the tender which has not been lifted for existing projects by the exemption provision of the Regulation. Accordingly, the eligibility of the existing projects for debt assumption is still unclear.

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