

M&A in Turkey's regulated markets

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Serra Basoglu Gurkaynak of Mehmet Gun & Partners analyses the regulatory framework of M&A transactions in Turkey and offers an overview of activity across the regulated markets

In 2013, a significant number of M&A deals closed in Turkey. According to the Turkish Competition Authority's 2013 annual report, there were 213 M&A transactions (and joint ventures) submitted to the Competition Authority for clearance in 2013. According to the records of the Competition Authority, the most active sectors have been energy, food and beverages, telecommunications, media and technology (TMT), transport and pharmaceuticals. The total deal value in 2013 was approximately \$17.5 billion.

The regulated markets, such as energy, TMT, pharmaceuticals and insurance remain attractive in terms of M&A in Turkey. In this article, we will analyse M&A activity in these industries, and will provide insight into the issues around M&A deals in these heavily regulated markets.

M&A in regulated markets 2013

The energy sector was particularly active in terms of acquisitions in 2013. Privatisations of electricity generation and distribution facilities and natural gas distribution facilities constituted around 40% of total M&A deals in terms of acquisition value.

Energy took the lead by volume, but the performance of the TMT sector in terms of M&A transactions was also considerable. The telecommunications, media, digital media, advertising and IT and software industries are booming, and the acquisition of television channels, media companies, advertising, on-line gaming and software companies were common place. The market was attractive both for local and foreign investors.

"Privatisations in the energy market powered M&A transactions in 2013"

According to a 2013 M&A report from one of the big four accountants (where financial sectors are deemed as banking, leasing and insurance), insurance was the leader in the financial sector for M&A in terms of deal value in 2013. There were only four insurance-related deals, but these amounted to nearly 70% of activity in the financial sector.

In the life sciences sector, both local and foreign players were active. Global players are more interested in either buying their distributors and small to medium sized local partners, or transferring the relevant portfolio from these companies to enter the Turkish market themselves. We expect to see the same trend in 2014.

Major M&A deals in 2013

Privatisations in the energy market powered M&A transactions in 2013, which led to the energy sector leading the way in overall M&A deals. The largest M&A transactions were made in the energy sector, with privatisations in the electricity and natural gas markets. The acquisition of Seyit Ömer Power Plant by Çelikler Group (\$2.248 billion), Bogaziçi Elektrik Dağıtım by Cengiz-Kolin-Limak (\$1.960 billion), Toroslar Elektrik Dağıtım (\$1.7 billion) and Ayedas Elektrik Dağıtım (\$1.2 billion) by Enerjisa, Baskent Dogal Gaz by Torunlar Group (\$1.162 billion) were the most significant deals in the sector.

The media sector saw tenders by the Savings Deposit Insurance Fund (SDIF) for two media companies in 2013, while 100% of AKS Televizyon (Show TV) was acquired by Ciner Group and 100% of Aksam Media Group was acquired by a private investor. The total value of these two acquisitions was approximately \$0.5 billion. One of the largest was the acquisition by Dogan Yayın of the 22% of Dogan Gazetecilik, with a deal value of \$122 million. Another television channel, TV 8, was also acquired by a private investor in Turkey for \$70million.

In the insurance sector, the largest M&A transaction of 2013 in terms of deal value was the purchase of a 94% stake in Yapi Kredi Sigorta (non-life segment) by Allianz SE, including Yapi Kredi Emeklilik (life and pension) from Yapi Kredi Bank for €684 million (\$937 million), a figure over 21 times the company's 2012 net income of TL76 million (\$36 million). Allianz SE's share in Yapi Kredi Sigorta was lifted to 99.78% after a mandatory tender offer (following the acquisition) with the remaining stake held by minority shareholders. Likewise, the third largest M&A transaction was the purchase of a 90% stake in Acibadem Sigorta (among the leading insurers in the life segment) by Avicenna Capital from Malaysia for €190 million (\$260 million) We also saw another private equity group on the acquisitions stage as Mediterra Capital acquired 100% of the ACP Sigorta ve Reasürans Brokerliği. Further, a significant insurance deal was the sale of 90% of the shares of Demir Sigorta to the Hariri family from Lebanon, where the deal

value was not disclosed.

When we look at life sciences related M&A transactions over the last few years, we could mark the acquisition of a 75% stake in Acibadem Saglik Hizmetleri by Malaysian's Khazanah for \$1,260 billion as the hit of 2011 in this sector. Likewise, in 2012, Amgen, the world's largest biotechnology company, agreed to buy Mustafa Nevzat Pharmaceuticals for almost \$700million to expand into Turkey. In 2013, the UAE private equity firm, Gulf Capital, acquired a 30% stake in Dogu Tip Merkezi with a transaction value of \$11 million. The average deal size in 2013 shows a limited number of large transactions; however, the life sciences market in Turkey is always attractive to investors, and we expect to see global players in the market acquiring strategic portfolios and manufacturing sites from local companies in 2014.

Involvement of regulatory authorities

Each regulated industry has its own regulatory body, which plays a significant role in the M&A deals in its particular market.

The regulatory body in the energy sector is the Energy Markets Regulatory Authority (EMRA). Licences in the energy sector are granted by EMRA, and it regulates and inspects all activities of the companies in the sector. As mentioned below, share transfers and asset transfers are subject to the approval of EMRA.

The main regulator in telecommunications is the Information Communications Technology Authority (ICTA). ICTA is an independent administrative authority responsible for the regulation and inspection of the telecommunication sector. It is the responsible body for the issuance of licences required for each type of electronic communication services. However, the main regulator in the media and broadcasting market is the Radio and Television Supervision Council (RTSC). This is an independent public authority responsible for regulating and monitoring radio and television broadcasts across the country.

The Ministry of Health is the main regulator in the life sciences market. In the pharmaceuticals sector, products cannot be launched on the market without obtaining a licence granted by the Ministry. In contrast, the medical device sector is not as regulated as pharmaceuticals, and medical devices do not have licences. However, as of July 2007, they must be registered at the Turkish National Drug and Medical Device Databank (TITUBB). The intention of the databank is to trace and control medical devices which are reimbursed by the Social Security Institution at national level.

"The life sciences market in Turkey is always attractive to investors"

The Undersecretariat of the Treasury (the Treasury) to which the

General Directorate of Insurance is attached, is the regulatory body of the insurance sector. M&A activities in the insurance sector are subject to the approval of the Treasury.

Insight for investors in regulated markets

M&A in regulated markets requires specific sector knowledge and in depth experience of the relevant regulations. Unlike unregulated markets, M&A transactions in regulated markets have certain unique dynamics, and parties must be fully aware of these in order to conclude a successful deal.

In terms of structuring a deal in regulated markets, industry restrictions and rules must be taken into account from the very beginning. The experience of advisors in the sector-specific regulatory side, in addition to general transactional expertise is of key importance and we have set out certain regulatory issues to be considered when buying or selling in the energy, life sciences, TMT and insurance sectors.

Energy

In M&A deals in the electricity market, investors must know that no share transfer during the pre-licence period is allowed. Furthermore, share transfers above 10% and asset transfers which change the ownership of the facility are subject to the approval of EMRA. Additionally, any type of transaction which ends up with a change of control of the licensed company is also subject to the approval of EMRA. The shareholders and directors of the licensees must meet certain requirements (for instance, they should not have committed certain criminal offences), and therefore the acquirer must review whether such requirements are met both by itself and the persons to be appointed as directors.

Although share transfers in the pre-licence period are restricted, existing legislation is silent on whether or not the pre-licence itself can be transferred as an asset. We believe that the pre-licence should not be transferred either, as it will be against the principle of the Electricity Market Law, which restricts share transfers to avoid a trade of pre-licences and which aims to give licences to serious investors who are committed to operating a facility in the electricity market.

Life sciences

In the life sciences sector however, we often see asset deals in the form of the transfer of marketing authorisations for pharmaceutical products. The critical point here is that transfers require the approval of the Ministry of Health, and their requirements need to be fully understood. Since the closing of these transactions is subject to the approval of the transfer of the marketing authorisations by the Ministry, the approval process may delay the closing of the transaction when compared to a straightforward asset

deal in another sector. The parties (especially the acquirer) should look at alternative trading options to start doing business during the transfer process in order to avoid loss of profit, clients and business during this pending period. Marketing authorisation transfer in and of itself may be considered as an asset transfer and the acquirer will be liable for transferring relevant employees who are dedicated to the specific products which are being transferred. Employment law issues often become a critical issue in this situation, and need to be given careful thought in the transaction documents beforehand.

Technology, media and telecommunications

In the media market, there are both ownership and market access restrictions imposed by relevant laws and regulations. Existing restrictions on the shareholding structure of private broadcast service providers is that direct foreign shareholding cannot exceed 50% of the total share capital of the broadcaster. Foreign persons can only become a direct shareholder in a maximum of two media service providers. Furthermore, in cases where foreign indirect ownership is in question, there are certain managerial obligations and restrictions imposed on indirect foreign ownership. It must be taken into account that the RTSC has the right to analyse the entire shareholding structure to determine indirect ownership, so that for example, the shareholder at the top of a private equity fund can be detected.

In our experience, the restrictions imposed on shareholding structures have, in the last few years, often caused foreign satellite broadcasters to evaluate particular types of direct investment in Turkey by establishing a joint stock company in line with the required managerial structure.

In terms of M&A transactions related to broadcast licensees, deals must be notified to the RTSC before the transaction to obtain consent, and also notified to the RTSC within 30 days of completion. If the RTSC objects to the transaction, stating that the resulting shareholding structure is not valid, it will require the parties to comply and make necessary capital structure changes within 90 days, or the licence will be revoked. Further, terrestrial broadcast licences may not be transferred and can only be terminated and returned to the RTSC.

"The outlook for further investment in Turkey in 2014 looks promising"

Electronic communication services are also a regulated area, and authorisations are granted by ICTA. Again, M&A transactions must be submitted to ICTA for approval, which will consider factors such as market conditions, competition requirements and the market share of the service provider when deciding whether to grant

consent to the transaction. If ICTA consent has been granted for a transaction, once again, the regulator must be informed of completion of the deal within one month under the post-closing obligations.

Insurance

In the insurance sector, share acquisitions directly or indirectly corresponding to or exceeding 10%, 20%, 33%, or 50% of the capital of an insurance or reinsurance company, and share transfers which will cause the shares of a shareholder to rise or fall, are subject to the approval of the Treasury. Share transfers granting a privilege of nominating members to the executive board to influence the company's supervision and management, are subject to such approval irrespective of the ratios mentioned above. In addition, portfolio transfers of insurance and reinsurance companies, which may be among the companies, or other organisations which engage in insurance activities provided that they have a licence in the relevant branch, are also subject to the approval of the Minister to whom the Treasury is attached. In case of failure to notify the Treasury of a merger, acquisition or a portfolio transfer, certain administrative fines would apply.

General managers and members of the boards of directors of insurance and reinsurance companies must meet specific qualifications, and the appointment of those persons is subject to audit and approval of the Treasury. These specific qualifications may create problems and result in delays in M&A transactions in certain cases. It is important for the acquirer to take the necessary action in a timely manner if it wants to discharge the general manager of the target insurance company. The new general manager, as well as members of the board of directors, should meet the criteria set out in the relevant legislation and the appointment should be notified to the Treasury for approval to prevent any delay in the transaction process.

Regulatory authorities often require detailed information about the entity acquiring the shares. This can create issues when the acquiring entity is a private equity firm, and these firms have a considerable interest in investing in companies active in regulated markets in Turkey. However, private equity firms may face difficulties in explaining to the regulatory authorities in Turkey their structure and concept. In most cases, regulatory bodies require a full shareholding structure, which includes all indirect shareholders. Such data can be very difficult to access in private equity firms.

These issues illustrate that transactional experience is not sufficient on its own for a smooth closing in M&A in regulated markets. The investor's professional advisors must also have regulatory experience related to the relevant market. Liaising with regulatory bodies in an effective manner and having a thorough understanding of their dynamics, as well as experience in dealing with these bodies is a key factor in the success of these transactions. It is as

important to know the regulatory steps and understand the regulatory mechanics that affect the pre-closing, closing and post-closing phases, as understanding how the regulatory bodies work to prevent procedural obstacles in an M&A transaction.

Other issues in M&A

Control of concentrations

Regardless of the industry sector, if an M&A deal is above a certain turnover threshold as defined by the relevant competition regulations, the transaction must be reviewed and cleared in advance by the Competition Board. This may create problems in terms of closing in certain transactions because it is not possible to take this step if the applicable revenue thresholds are exceeded.

On filing a notification to the Competition Board, a preliminary examination must be conducted within 15 days of the date of notification, after which it will render a decision on the notified transaction. If the board does not respond to the notification, the transaction is deemed cleared 30 days after the notification date.

In M&As within the electronic communications industry, the board must also take into account the opinion of ICTA.

The time line of the M&A deal must always be determined with these requirements in mind, because non-compliance with clearance requirements will make the acquisition invalid and the parties can face fines up to 1/1000th of their annual income.

Capital Markets Board regulations

Publicly traded companies are regulated by the Capital Markets Board and subject to detailed laws and regulations regardless of their industry sector. Certain shareholding changes in public companies need to be announced to the Capital Markets Board and indirect acquisitions are included in this requirement. With a change of control, a mandatory tender offer is triggered, which the investors need to take into account if the target is a listed company.

There are several disclosure requirements that are triggered by the negotiation, signing and closing of an M&A transaction, as well as insider information issues that need to be taken into consideration while a transaction progresses.

The voting privileges, composition of the Board, and appointment of Board members are all regulated by the corporate governance rules issued by the Capital Markets Board which will affect the structuring of an M&A transaction and its closing mechanism.

Therefore, where the target is a listed company, capital markets regulations, including approval and disclosure requirements, must also be factored in very carefully to the deal mechanics.

A promising outlook

Despite the recent political crises, the outlook for further investment in Turkey in 2014 looks promising. Investors are still analysing potential deals and the regulated sectors lead M&A transactions in the first quarter of 2014.

Investors are encouraged to seek sector-specific advice and experience when appointing advisors, in order to fully understand the regulatory complexity and dynamics in the Turkish market that are essential to the smooth closing of an M&A transaction in regulated industries.

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