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# BULLETIN

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## NON-COMPETITION CLAUSE FOR BOARD OF DIRECTORS AND SHAREHOLDERS IN JOINT STOCK COMPANIES

Today's economic order is essentially based on the principle of free competition adopted by the liberal economy. Pursuant to Article 48 of the Constitution, everyone has the freedom to work and enter into contracts in any field they choose. However, this freedom is not unlimited; the legislature has imposed certain restrictions to prevent the abuse of competition. The non-competition clause is one such restriction and appears in various forms in our legislation. Accordingly, members of the board of directors and shareholders of joint-stock companies have different obligations under the non-competition clause. This bulletin will address the responsibilities of both board members and shareholders under the non-competition clause.

### I. Board of Directors Members

In corporations, it is generally prohibited for persons holding management authority to engage in commercial activities independently of the company in areas falling within the scope of the company's activities or to be involved in another commercial enterprise operating in similar areas. This prohibition is based on the duty of care and loyalty imposed on members of the board of directors. Indeed, Article 369 of the Turkish Commercial Code (TCC) clearly states that members of the board of directors and persons responsible for management are obliged to perform their duties with due care and to protect the company's interests in accordance with the principle of good faith.

A Furthermore, preventing board members from using company secrets acquired in the course of their duties for their own benefit or for the benefit of another company is also one of the purposes of this regulation. Pursuant to Article 369 of the Turkish Commercial Code, even if management authority has been delegated to authorized managers, these persons are also subject to the duty of care and loyalty; therefore, the non-competition clause is also valid for them.

According to Article 396/1 of the Turkish Commercial Code, “A member of the board of directors may not, without the permission of the general assembly, engage in a commercial transaction falling within the scope of the company's business on his or her own behalf or

on behalf of another person, nor may he or she become a partner with unlimited liability in a company engaged in the same type of commercial activities." The company has the right to claim compensation from board members who violate this provision or to consider the transaction as having been made on behalf of the company.

This provision indicates that the non-competition clause imposed on board members is not mandatory in nature. For a legal rule to be considered mandatory, the parties must be unable to agree otherwise. However, Article 396 of the Turkish Commercial Code provides that this prohibition may be lifted by a general assembly resolution. Therefore, it is legally possible to lift the non-competition clause for board members on an exceptional basis.

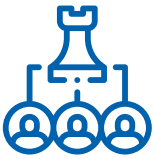
Two types of conduct are prohibited under this article. The first is "conducting commercial transactions that fall within the scope of the company's business." The purpose here is to ensure that board members refrain from engaging in business and transactions that would generate commercial profits in the area in which the company operates. In this context, the scope of the non-competition clause is limited to the areas of activity actually carried out by the company, not all matters listed in the articles of association.

The second type of prohibition is "becoming a partner with unlimited liability in a company engaged in the same type of business." This provision prohibits a board member from becoming a partner with unlimited liability in a general, collective, or limited partnership operating in the same field as the company. However, becoming a limited partner in a joint-stock, limited, or limited partnership does not fall under this prohibition.

If a board member violates the non-compete clause, the company has three options: seek compensation, treat the transaction as having been made on behalf of the company, or claim that any benefits accruing to a third party belong to the company. These discretionary rights may be exercised by other board members who have not violated the non-compete clause.

Finally, pursuant to Article 396/3 of the Turkish Commercial Code, these rights are limited to specific periods. Claims shall become time-barred if these rights are not exercised within three months from the date on which other members become aware of the violation, or within one year from the date on which the act occurred, whichever is earlier.

## II. Shareholders



Upon examining the provisions of the Turkish Commercial Code (TTK), it is evident that the statutory non-compete clause in joint-stock companies applies only to members of the board of directors, and no such obligation exists for shareholders. This is because the legislator has explicitly regulated the non-compete clause only with regard to board members, excluding shareholders from this scope. At this point, the doctrine is divided into two groups: one group states that shareholders are not subject to the non-competition clause, while the other group states that they are. To put an end to the debate at this point, in cases where a non-competition clause is desired, a definitive solution for the company can be achieved by signing a shareholder agreement between the partners.

The shareholder is expected to refrain from actions that would cause harm to the company or violate the principle of good faith; however, this is not considered a "fiduciary duty" but is evaluated within the framework of the principle of good faith as stipulated in Article 2 of the Turkish Civil Code.

The fact that shareholders are not legally subject to a non-competition clause does not mean that such an obligation cannot be imposed by contract. Pursuant to Article 329/2 of the Turkish Commercial Code, the liability of shareholders to the company is limited solely to the capital debt they have undertaken. At this point, provisions such as additional debts and

non-competition clauses may be added to the shareholders' agreement, as well as provisions stating that the partners are not subject to a non-competition clause.

However, even when a non-compete clause is included in a contract, it must be reasonably limited in terms of duration, location, and subject matter. Contracts that do not include such limitations will be deemed invalid. Indeed, in its decision dated June 11, 2015, No. 2014/11565 E., 2015/8187 K., the 11th Civil Chamber of the Court of Cassation ruled that a 15-year non-competition clause was invalid on the grounds that it excessively restricted economic freedom. On the other hand, provisions prohibiting competition during the period of partnership and for 2 to 5 years after leaving the partnership may be regulated by a shareholders' agreement.

## III. Conclusion

In corporations, members of the board of directors are subject to a statutory non-competition clause. However, this prohibition is not absolute and may be waived with the approval of the general assembly. If management duties are delegated to third parties, those parties are also subject to the same non-competition obligation.

In contrast, no legal prohibition on competition or duty of loyalty is expressly provided for shareholders who do not hold management positions. In some cases, shareholders engaging in activities that constitute competition with the company may be evaluated within the limits of the principle of good faith. In other words, shareholders may engage in activities in the same field as long as they do not harm the company's interests and do not create unfair competition. In such cases, where other partners demand a non-competition clause, a shareholders' agreement may establish more comprehensive non-competition restrictions for shareholders in addition to the law.



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