

Insight: Litigation

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Turkcell Litigation – Pivotal Ruling

Privy Council confirms Cukurova's entitlement to relief from forfeiture

After more than five years of litigation between Cukurova of Turkey and Alfa of Russia, the Privy Council has delivered a pivotal ruling in Cukurova's favour.¹ The decision establishes that a borrower may be entitled to equitable "relief from forfeiture" even after a lender has exercised a power of appropriation under the Financial Collateral Arrangements (No 2) Regulations 2003² (the "FCA Regulations").

In December 2003, the FCA Regulations introduced the novel remedy of appropriation into English law. Since then, borrowers and lenders have been able to agree that, where a security interest is created under a security financial collateral arrangement, if the security becomes enforceable, the lender can appropriate the financial collateral in satisfaction of a due debt (under Regulation 17) without the need for a court order. This enables the lender to become the absolute owner of the collateral upon appropriation, subject only to a duty to account to the borrower for any excess in the value of the collateral over the outstanding debt. Unsurprisingly, the power of appropriation has been widely incorporated into English law security documentation.

Crucially, the Privy Council's decision confirms that, in appropriate circumstances, the power of appropriation is subject to equitable safeguards which may permit the borrower to redeem its security even after a valid appropriation.

Background

In late 2005, as security for a US\$1.352 billion loan facility from Alfa Telecom Turkey Limited ("ATT"), Cukurova Finance International Limited (a company incorporated in the British Virgin Islands) and Cukurova Holding A.S. ("Cukurova") mortgaged to ATT shares conferring a 13.76% indirect shareholding in Turkcell Iletisim Hizmetleri A.S., Turkey's largest mobile telecommunications company. In April 2007, ATT alleged several events of default against Cukurova and, ten days later, appropriated the charged shares under the terms of English law governed security documents which granted ATT the remedy of appropriation under Regulation 17 of the FCA Regulations. Less than one month later, Cukurova tendered over US\$1.4 billion to ATT in full repayment of the loan (including default interest). The tender was made without prejudice to Cukurova's position that it had not been in default and that ATT's appropriation had, in any event, been invalid. ATT refused to accept the tender.

The case was heard in the Eastern Caribbean jurisdiction and final appeal was to the Privy Council in London.



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¹ Cukurova Finance International Ltd & Anor v. Alfa Telecom Turkey Ltd (British Virgin Islands). White & Case has acted for Cukurova throughout the litigation.

² Subsequently expanded by the FCA Amendment Regulations 2010.

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The Decision

Having determined that ATT had been entitled to accelerate the loan and enforce its security, the central issue before the Privy Council was whether Cukurova was nevertheless entitled to relief from forfeiture and to redeem the charged shares.

Cukurova argued, by reference to authorities going back more than 250 years, that equitable relief from forfeiture is available to collateral-providers under the FCA Regulations in the same way that a mortgagor of property may be entitled to such relief. Whilst noting that the need for commercial certainty was a “very relevant consideration” when determining whether the equitable relief sought by Cukurova was available, the Judicial Board of the Privy Council (which comprised Lords Neuberger, Mance, Kerr, Clarke and Sumption) agreed that the FCA Regulations do not preclude such relief. Indeed, it was an important safeguard which was available to Cukurova in these circumstances, as Cukurova had consistently argued.

The Privy Council identified a number of particular features which were relevant to the exercise of its discretion to grant equitable relief. Among these were the following:

- ATT was interested in the shares, not as security for the loan, but for the control over Turkcell which they offered.
- ATT’s aim in entering into the transaction was to acquire the charged shares (via appropriation or otherwise) when (as it expected) Cukurova defaulted on the loan.
- In order to further this aim, ATT had taken a number of deliberate steps designed to make it more difficult for Cukurova to repay the loan (which it knew Cukurova was making efforts to do).
- By relying upon the appropriation provision, ATT would have been able to acquire the shares at a substantial discount to their market value (because the valuation mechanism agreed between the parties did not reflect any control premium).
- Even if all the Events of Default alleged by ATT had been established, they were limited in number and had not been committed wilfully by Cukurova.
- The Event of Default that was found by the Privy Council never threatened or prejudiced ATT’s financial position.
- Cukurova had gone to great lengths to tender repayment of the loan, in full, within a month of the appropriation.
- At all material times the value of the charged shares was sufficient to cover Cukurova’s debt to ATT.

The terms upon which relief is granted

The Board has yet to determine the precise conditions upon which the available relief should be granted to Cukurova. Significantly, the Privy Council’s judgment has raised several important questions concerning how much a borrower, who is granted relief from forfeiture following an appropriation by the lender, will be required to pay to the lender by way of compensation for having been kept out of the money from the date of appropriation to the eventual redemption date.

Further submissions on this point are being made to the Privy Council and a further judgment is expected in the coming months. We shall provide additional commentary at that time.