

Responses from Turkey
for
AIDA Questionnaire
on the
Corporate Governance of Insurers
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Prepared by

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I. General

1. In your jurisdiction, what corporate governance models are available to insurance companies? In case multiple models are available, describe the main differences and the allocation of management and monitoring powers among the relevant bodies/committees and which model is generally or ideally adopted by insurance companies.

It is possible to say that companies operating in regulated sectors, such as banking, insurance and electrical energy, as well as publicly held JSCs, observe and comply with the corporate governance rules quite successfully.

The insurance companies are incorporated as joint-stock companies (société anonyme), where the Board of Directors of at least 5 directors are ultimately responsible for management. The company must establish a functioning

2. What are the main sources of regulation addressing corporate governance of companies (and in particular of insurance companies)? e.g., statutes, regulations, other rules/recommendations issued by national and supranational supervisors/regulators, self-regulation, codes of best practice, codes of ethics.

Currently, there are few corporate governance requirements that apply specifically to insurance companies in the Insurance law other than the requirement that the Board of an insurance company have not less than five members including the General Manager and that the General manager not be the Chair of the Board. Corporate governance for all commercial companies is regulated by the Turkish Commercial Code numbered 6102 which was revised in July 2012. The Commercial Code contains some basic provisions relating to:

- *Board composition.*
- *Appointment of board of directors.*
- *Duties and authority of the board.*
- *Limitation and duration of the board.*
- *Dismissal of the board.*
- *Representation and management.*
- *Delegation of authority.*
- *General Assembly.*
- *Resolutions.*
- *Call procedure for meetings.*
- *Committees.*
- *Remuneration.*
- *Audit.*
- *Risk.*

Publicly traded insurance companies must also comply with Corporate Governance Principles established by the CMB, or explain themselves to the CMB. These companies, however, comprise a small number of Turkey's authorized insurers.

The Turkish Insurance Regulator (the "Treasury") has published a Circular on Corporate Governance Principles of Insurance Companies, Reinsurance Companies and Pension Companies. This document is very general and contains few specific rules relating to Board composition, duties and responsibilities of directors, committee structure or reporting of control functions. Nor does it include an obligation for Board directors to ensure the fair treatment of policyholders. It is used by the Treasury as a guide to assess the effectiveness of corporate governance in its supervision of insurers.

The document requires insurers to establish a Corporate Governance Committee which prepares a report each year on corporate governance and on how the insurer adheres to six corporate governance principles:

- *Principle 1 – companies determine their corporate governance practices according to the principles of equity, transparency, accountability, and responsibility.*
- *Principle 2 – The company takes measures that will ensure protection of rights arising from legislation, articles of association, and other corporate regulations relating to shareholder rights*
- *Principle 3 – Companies perform their work and operations in a transparent manner.*
- *Principle 4 – The rights of stakeholders are protected independently from each other.*
- *Principle 5 – Board of directors and managers perform their tasks in a fair, transparent, accountable and responsible manner.*

Article 4(8) of the Insurance Law 5684 requires insurance and reinsurance companies to establish an effective internal control system, including internal audit and risk management.

The Regulation on the Internal Systems of Insurance, Reinsurance and Pension Companies establishes requirements regarding internal control systems, internal audit and risk management systems. • Article 4 of the Regulation requires insurers to have in place internal systems (internal control, internal audit and risk management requirements) that are adequate for the nature and scale of the business.

• Article 5 requires the Board of Directors to be ultimately responsible for establishing and maintaining an effective internal control system.

This Regulation on the Regulation on Financial Reporting of Insurance, Reinsurance and Pensions companies appear to require adherence to some of the standards in the ICP (e.g. ICP 7.5, ICP7.7 and ICP 7.8).

In regard to insurance groups, Regulation on Financial Structure article 21/A allows the Treasury in conjunction with other appropriate financial services regulators to audit the adequacy of group internal control systems, including internal audit and risk management. There are, however no specific requirements with respect to groups.

3. In your jurisdiction, are you aware of any insolvency or distress of an insurer directly attributable to poor corporate governance standards or practices or failure to adequately implement and apply such principles? If so, please identify the main triggers of the insolvency.

There is no publicly announced insolvency or distress.

4. In your jurisdiction, is corporate governance regulation applied according to the nature, scale and complexity of an insurer's business? If yes, please describe any significant differences and rationale for the differences.

Insurance specific rules regarding governance do not differentiate according to the nature, scale and complexity of an insurer's business. However, the Treasury allows simplified internal systems to be simplified for smaller companies; e.g. the Treasury can require a company to employ a manager responsible for internal control system, whereas in smaller organizations, internal control can be established as a form of system, without being incorporated as an internal department.

5. Please provide specific examples of corporate governance structures and practices that are better implemented through self-regulation rather than through legal or supervisory requirements.

N/A

6. In case your jurisdiction was recently requested to implement domestically certain corporate governance principles set forth by supranational regulations, describe the main obstacles and problems (if any) that resulted from such process.

Not applicable in insurance market

7. Are there any significant differences between general corporate governance rules and the specific rules governing insurance companies?

N/A

II. Fitness and Propriety of Board Directors

1. Are there any laws or regulations already adopted or any proposals in your jurisdiction, relating to the qualification and composition of board directors in an insurance company? If so, please explain.

The Turkish legislation foresees single Board structure. The general manager (or the CEO) must be a member of the Board, which ensures direct execution of the company management within the Board organization. As per the Insurance Law Art. 4 "(i) Boards of directors of insurance companies and reinsurance companies shall not be less than five persons including the general manager, and auditors shall not be less than two persons. The general manager is a natural member of the board of directors. (ii) Members of the board of directors should meet the criteria sought in founders of an insurance company and reinsurance company except the criteria of financial power; the majority of them should hold an undergraduate degree of at least four years, and they should have at least three years of experience in any one of insurance, economics, business, accounting, law, finance, mathematics, statistics, actuary or engineering fields.

2. In your opinion, what factors, conditions, or incentives might weaken the independence of the board of directors or individual members of the board?

The Board of Directors organization creates a high level supervision of company management but it lacks an actual executive organ as in a dual board (or two tier) system which is a corporate structure system that consists of two separate Boards of directors that govern a corporation. In a two-tier system, the structure is composed of two boards, the "Management Board", and the "Supervisory Board" each of these have different roles.

3. How does an insurance company ensure that individual board members and the board collectively have enough knowledge to monitor and oversee the activities of the insurer appropriately, particularly where specific expertise is needed?

There is a direct reporting mechanisms for internal systems. The internal audit department is compulsory for insurance companies and the head of internal audit must report directly to the Board or at least one Board member must be responsible for internal audit. Additionally, general manager (also a member of the Board) is also responsible for internal control.

4. Are there significant differences in terms of requirements and duties between executive and non-executive members of the board of directors of an insurer?

The executive members cannot be responsible for internal systems or the compliance with the anti-money laundering legislation. If the articles of association allows, certain members can be given liability for executive matters (e.g. IT, financial affairs).

The BoD is entitled to delegate its management powers to certain members of the BoD or to third parties (as managers), as long as the Articles of Association (the "AoA") provides for such delegation and the BoD adopts an internal directive (iç yönerge). However, at least one BoD member must always have representation powers.

BoD members and managers may be held liable in the event of a breach of their obligations set forth by laws or the AoA, unless they prove that they were not negligent. In the event of a delegation of powers, those who delegated powers may not be held liable, unless they breach the obligation to delegate to appropriate persons. It should be noted that if a power is delegated, which may not be delegated according to law or the AoA, the delegation will be deemed illegal, and the BoD member(s) will be held liable.

The powers of the BoD that are not subject to delegation are listed under Article 375 of the Turkish Commercial Code, which are as follows:

- a) High-level management of the company and the power to give instructions regarding the same;
- b) Determining the management structure of the company;
- c) Establishing the necessary organization for accounting, financial auditing and financial planning (at a level required based on the size of the specific company);
- d) Appointing and dismissing managers and other upper-level personnel, and persons who hold representation and binding powers;
- e) Carrying out high-level auditing of persons engaged in management in compliance with the law, the AoA, internal directives and written instructions of the BoD,
- f) Maintaining the share ledgers, BoD resolution and general assembly meeting minutes; organizing and submitting the annual activity report, and declaration regarding compliance with corporate governance rules to the general assembly; preparing for general assembly meetings; and enforcing the general assembly meeting resolutions; and
- g) Notifying the court if the capital of the company is in debt.

5. In your jurisdiction are there any black letter rules or general principles that enable directors to rely upon external opinions when addressing issues or aspects where specific expertise is needed?

Please see the response to question 4 above. The principal duties of the board members are as follows:

- a) to act prudently and diligently when conducting business and performing their duties and the business of the company;
- b) to monitor and supervise the management and the business of the company to ensure that it is in compliance with principles of good faith, and for the interests of the company and its shareholders;
- c) to keep confidential the information obtained during and after the term of duty;
- d) to refrain from attending board meetings regarding their own interests or the interests of certain close relatives; and
- e) not to engage in transactions with the company unless the GA meeting authorises the board for a maximum period of five years regarding the repurchase of shares.

Under these principles, In the event of a delegation of powers, those who delegated powers may not be held liable, unless they breach the obligation to delegate to appropriate persons.

6. Describe the extent and scope of supervisors'/regulators' intervention with reference to the qualifications and to the activities of the board of an insurer.

As per Insurance Law Art. 20, "If it is found that an insurance company fails to meet the amount of minimum guarantee fund, to allocate the guarantee which it has to establish, to have sufficient and appropriate assets to cover technical reserves, to fulfil its obligations arising from contracts or that its financial structure is weakened to endanger the rights and benefits of the insured, the Minister, by giving an appropriate period of time to the insurance company, for strengthening the financial structure, may require the insurance company to replace part or all of the members of the board of directors or auditory board, or to appoint new members to these boards by increasing the number of existing members, or to request that the management of the insurance company or reinsurance company is assigned to a trustee.

7. Are there any special rules and regimes applicable to the governance of subsidiaries belonging to an insurance group, also in terms of information flows?

Only general rules on conglomerates and group companies will be applicable. There are only limited provisions regarding financial statement of financial holdings.

III. Risk Management

1. In your opinion, what is the biggest risk challenge (e.g. regulation, capital standard, pricing, interest rate, cyber, terrorism, etc.) facing the insurance industry today in your jurisdiction?

Due to political instability and changes in economy, the regulation is the biggest risk challenge.

2. What specific laws or regulations, actual or pending in your jurisdiction, will present significant implementation risk challenge toward the insurance industry?

The Personal Data Protection Law introduces new privacy principles, which imposes many requirements and failure to comply with these requirements can result even in penal liabilities.

IV. Ethics and Corporate Social Responsibility

1. Please provide any concrete examples where business ethical standards and/or corporate social responsibility standards have been applied and have changed the behaviors of the insurance company.

N/A

2. In your jurisdiction, are there any specific laws or regulations already adopted or any proposals, or any arrangements in place in the governance system, relating to the protection of policyholders' and/or financial consumers' interests?

N/A

3. In your jurisdiction, is an insurance company required to produce an annual Corporate Social Responsibility (CSR) report or a Global Sustainability Initiative (GSI) report? If so, what context needed to be disclosed in these reports?

N/A

V. Disclosure

1. In your opinion, what mechanisms shall be in place or considered in an insurance company to ensure the transparency of its governance structure? (e.g., the articles of association, the organization chart, any existing committees, the major shareholders, the ethical standard, corporate social responsibility, etc.)

The insurance companies must have a website, which will include information on their BoD members and their executives. The companies must also create a mechanism, which allow reporting of any fraudulent and/or issues which will require further investigation. The insurance companies must share their annual activity reports with the Regulator and also it should be shared via their official website. Likewise, financial statements, the name/title of the independent auditor must also be announced in the website.

There is also a mechanism of reporting wrongful practices to the Regulatory, by use of an online reporting system. Wrongful practice shall include company practices, intermediary practices and also beneficiary practices.

2. Are there any governance practices that, in your opinion, can best be achieved through disclosure rather than through specific supervisory requirements? Which governance practices should be mandatory for an insurance company?

Any fraudulent activity within a company or wrongful practices of executives should also be announced on a central system or on the company's website.

3. What is the interplay between market abuse regulations and other disclosure/transparency rules applicable to listed insurers and industry specific rules applicable only to insurance companies?

VI. Outlook

In respect of the corporate governance of insurers, please describe your criticisms on the system in your jurisdiction, any recommendations for the future, and/or the main challenges which insurance undertakings encountered.

One of the main criticism will about the judicial system not well prepared to handle corporate law cases, which causes the supervision and enforcement of corporate governance standards to fall largely upon the Regulator. While plans for an Istanbul International Financial Centre foresee the creation of specialised courts, up to now private supervision and enforcement has only played a minor role in Turkey.

However, it should be noted due to the reliance on public supervision and enforcement, the governance and effectiveness of the relevant public authorities, notably the Capital Market Board (CMB), is of high importance. The CMB has been strengthened over the years, and is now regarded as one of the most professional and competent authorities in Turkey. However, it has authority on only publicly held insurance companies. Additionally, the management of pension fund is also subject to the supervision of CMB, even if the pension company is not publicly held.

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