

EFFECT OF PARTNER'S DEATH ON COMPANIES

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Abstract The death of a partner has important legal consequences on the company's shareholding structure in companies comprised of a community of people. According to Turkish law of succession, the succession shares of the deceased partner pass to his successors. In some companies, this change in shareholding structure does not cause any changes, while in others it results in dissolution of the company. These legal consequences, which vary according to type of the company upon death, are separately analyzed in our study.

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share
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1 Introduction

Article 124 of the Turkish Commercial Code (“TCC”) recognizes the following types of companies: the unlimited liability company, the commandite company (ordinary and capital divided into shares), as well as joint-stock, limited and cooperative companies.

Privately owned unlimited liability companies and commandite companies, joint stock companies, limited liability companies, and commandite companies with share capitals, are regulated as capital stock companies (TCC, Art. 124(2)). The cooperative constitutes a separate group apart from this definition.

The differentiating factors in each form of company are the partners' identities and relationships, the shares of capital contributed to the company, and the share rates acquired in consideration for the amounts contributed. While the partners' personalities and relationships are the paramount consideration in private companies, in capital stock companies the amount of capital contributed to the company the principal concern.

2 Changes Caused by Death of the Partner in Companies

Since the identity and relationships of the partners are important both in unlimited liability and in commandite companies, which are private companies (sole proprietorships), it is more difficult for the partners to enter or exit these companies or to transfer shares, and as a rule, they can do so only upon unanimous resolutions. The death of any one partner, or the loss of a partner's capacity to act, or a partner's bankruptcy may lead to automatic dissolution of such companies.

It is easier for partners to enter and exit from joint-stock, limited and commandite companies with share capital, all of which are capital stock companies, because such companies share the common characteristic that the capital is more important than the personality and identity of the partners. Accordingly, the death, loss of capacity or bankruptcy of the partners, as a rule, do not terminate the company.

Since the unique characteristics of each form of company and the impact of any of the partners' death are different, we will now analyze each form of company individually.

2.1 Unlimited Liability Companies

An unlimited liability company is a type of company incorporated by and between real persons in order to operate a commercial enterprise under a trade name. The liability of the partners is not limited due to the successor's debts (TCC, Art. 211).

The effect the death of a partner has on the company under provision 253 is regulated separately, according to whether there is a regulation regarding the death of the partners in the articles of association.

2.1.1 If Death of the Partner is not regulated in Articles of Association

As for unlimited liability companies, if there is no regulation in the articles of association, stating that the company will continue with the successors of the deceased partner, the company ends as a rule upon death of the partner (TCC, Art. 253). However, the successors and all other partners can ensure the continuation of the company by unanimous resolution. In case the relevant resolution is not required to be made explicitly and the business of the company continues without objection, the relevant resolution may be deemed to have been passed implicitly.

Successors, who do not intend to join the company, are paid successor shares by other partners (TCC, Art. 253(1)). Thus, other partners can remove the successors that do not intend to join the company, thereby ensuring the continuation of the company among themselves. However, the partners must unanimously agree to continue the company and their failure to agree will result in the company's termination.

The successors have the right to independently decide whether or not to join the company (Poroy, Tekinalp & Çamoğlu, 2014: 233). Notification of this intent must be given to the other partners, not to the legal entity (Poroy, Tekinalp & Çamoğlu, 2014: 233).

If all the successors prefer not to join the company, the other partners must unanimously pass a resolution among themselves to continue the company (Pulaşlı, 2014a: 404; Poroy, Tekinalp & Çamoğlu, 2014: 233). Otherwise, the company will dissolve (TCC, Art. 243; Turkish Code of Obligations (TCO) Art. 639/2). If there

is only one partner in the company, it is not possible to continue the company with a single partner (Pulaşlı, 2014a: 404; Court of Appeals 11th Law Chamber, 2013).

The right of the successor, who does not intend to join the company, which arises from a succession of the company, vests on the date when it becomes certain that he either will not join the company or will not be taken into the company by other partners (Poroy, Tekinalp & Çamoğlu, 2014: 233). In this case, the succession share will be calculated according to the date of the partner's death and the share is paid on the first balance sheet date after separation (TCC, Art. 262(1)).

Although the law does not provide any specific time for when these transactions must be executed, they must be concluded within an appropriate statutory period of time according to the concrete event. Otherwise, it is accepted that the company will dissolve (Poroy, Tekinalp & Çamoğlu, 2014: 234).

2.1.2 If Death of the Partner is regulated in Articles of Association

The unlimited liability company does not end upon death of any of the partners so long as there is a regulation in the articles of association stating that the company will continue with the successors of the deceased partner. The articles of association can also regulate whether the successors will become partners in the company and what kind of partners they will be, namely unlimited liability or commanditer (Pulaşlı, 2014a: 401).

The successors of the deceased partners are free to continue with the company as unlimited liability partners. In cases where the successors intend to continue the company, other partners must accept this decision. In this case, the successors have a founding right, and successor demands in this direction will bear consequence with no need for the company's acceptance (Pulaşlı, 2014a: 403).

In case any partner does not intend to stay in the company as an unlimited liability partner, among the successors, he may propose to be accepted into the company as an unlimited partner with the amount of the share he inherited from the deceased partner. However, contrary to the situation involving an unlimited liability partner, existing partners do not have to accept the partner's proposal to join the company as an unlimited partner (TCC, Art. 253(2)). Nevertheless, if any of the partners makes a declaration to become an unlimited partner, the type of company will have

to change, and the existing partners are required to accept this change (Bahtiyar, 2019: 96; Pulaşlı, 2014a: 403). In this case, a unanimous resolution must be passed by and between the other partners (Poroy, Tekinalp & Çamoğlu, 2014: 234; Pulaşlı, 2014a: 403). While the demands of the successors to join the company collectively must be accepted by the company, the participation of the successors in the company as unlimited limited partners are subject to acceptance by the other partners (Pulaşlı, 2014a: 403-404).

In accordance with the provision of Art. 253 of the TCC (2), the successors are required to notify the company, within three months from the date of death of the partner, whether they will enter the company with the capacity of a collective or unlimited liability partner. Until this notice is provided, the successors are considered as the commanding (unlimited) partners in the company. Successors that are not notified within three months shall have the title of unlimited liability partner as of the end of the period.

2.2 Commandite Companies

As with unlimited liability companies, commandite companies are private. They are incorporated to operate a commercial enterprise under a trade name. One or more of its partners is/are unlimited and other partners or partners have limited liability for company debts.

The main feature of the commandite company is that it has two types of partners, namely, active and silent, in terms of liability for company debts. The active partner has unlimited liability for the debts of the company, while the silent partner has limited liability.

Pursuant to Article 328 of the TCC on commandite companies, unlimited liability company provisions concerning changes between partners also apply to commandite company. The provisions regarding unlimited liability companies are applied regardless of whether the partner is an active or a silent partner. However, there are some differences in the event of the death of the silent partner.

Article 328 of the TCC provides that the death of the silent partner does not terminate the company unless otherwise stipulated in the articles of association. The deceased partner is replaced by his successors (TCC, Art. 316). Thus, the deceased partner's successor enters the company by operation of law, and successors do not have the right to choose in this regard (Poroy, Tekinalp & Çamoğlu, 2014: 271).

In case some successors do not intend to be partners in the company, the other partners must consent to this unanimously, as successors' exit from the company by taking the shares of the deceased partner constitute a termination (Poroy, Tekinalp & Çamoğlu, 2014: 271). However, a successor that does not intend to enter the company may also choose to renounce its succession rights (Poroy, Tekinalp & Çamoğlu, 2014: 271).

It is also possible for the articles of association to include a provision stating that in the event of death of the active partner the company terminates (Pulaşlı, 2014a: 447).

The analysis is different if the silent (limited) partner is a legal person since legal persons do not have a successor to enter the company in the place of the deceased, such as is the with real persons (Poroy, Tekinalp & Çamoğlu, 2014: 271-272). Liquidation of the silent (unlimited) partner shall not result in the dissolution of the company (Poroy, Tekinalp & Çamoğlu, 2014: 272). In this case, however, the liquidators may ask the company to permit the legal person to exit from the company or transfer his share to any third party (Poroy, Tekinalp & Çamoğlu, 2014: 272; Pulaşlı, 2014a: 447). In case the Company does not agree to the liquidators' request, the liquidators may ask for the commandite company to be terminated (TCC, 328/245) (Pulaşlı, 2014a: 447; Poroy, Tekinalp & Çamoğlu, 2014: 272). The partners of the company may request the court to dissolve the company, claiming that the liquidation of the partner legal entity is justified pursuant to 328/255 (1) of the TCC (Pulaşlı, 2014a: 447-448; Poroy, Tekinalp & Çamoğlu, 2014: 272).

2.3 Joint Stock Companies

Since joint-stock companies are capital companies, it is the capital, rather than the personalities of the partners, that is important. Therefore, the death of any of the partners does not constitute legal justification for termination of the company (TCC, Art. 529-531). However, there are situations where the death of the partner has legal effects on the company.

Shares are, as a general rule, freely transferrable in joint-stock companies. However, with respect to registered shares, provisions called context, which either limit the transfer of shares or subject them to consent, may be included in articles of association. However, context is ineffective in some cases, namely, in situations involving the acquisition of shares through succession, sharing of succession, the property regime between spouses, or forced enforcement. Therefore, succession, in other words, the death of a partner, is one of the cases where the context is ineffective under TCC, Art. 493(4). Accordingly, the effect of the death of a partner on the company should be separately examined according to whether there is a context clause in the articles of association.

2.3.1 If There is No Context in the Articles of Association

If the context provision is not stipulated in the articles of association, the share of the deceased partner passes to his successors through succession (Pulaşlı, 2014b: 1394). In this case, his successors gain the relevant share by transfer and within legal succession (Pulaşlı, 2014b: 1394; Poroy, Tekinalp & Çamoğlu, 2014: 580).

There are situations where there is legal context even though the articles of association do not explicitly provide for context. In accordance with Article 491(1) of the TCC, in case the consideration for registered shares is not fully paid, those shares that were not fully paid for can only be transferred upon the company's consent. In continuation of the provision, however, the share transfer is excluded in case of succession, sharing the succession, the provisions of the property regime between the spouses or forced execution. Thus, the restriction does not apply if the transfer takes place through succession as a result of the partner's death. In this case, the company may refuse to give consent only if the solvency of the transferee is doubtful and the security requested by the company has not been provided (TCC, Art. 491(2)).

2.3.2 If Context is stipulated in Articles of Association

By inserting a context provision in the articles of association, it is possible to condition the transfer of the registered shares upon the company's approval. However, the law stipulates different arrangements on the context provisions stipulated in the articles of association, in terms of those shares listed on the stock exchange as compared to those shares not listed on the stock exchange.

2.3.2.1 At Off-Board Companies

Under certain circumstances, based on the context provisions of the articles of association, the company may refuse to approve the transfer of registered shares not quoted on the stock exchange. The first such circumstance is where the company refuses to transfer, asserting an important reason as contained in the articles of association and pursuant to TCC, Art. 493(1). Some authors assert that provisions of the articles of association regarding the composition of the shareholder's environment will constitute an important reason in case the company argues that it is entitled to refuse the approval based upon the economic independence of the business (TCC, Art. 493(2)). Thus, the company was not released in terms of stipulating significant reason in the articles of association (Poroy, Tekinalp & Çamoğlu, 2017: 142).

Secondly, the company may refuse its consent by proposing that the transferee purchase their shares for their own or other partners or third parties at their fair market value at the time of application (Court of Appeals 11th Law Chamber, 2015).

Accordingly, in such circumstances, the company is given a legal pre-emption right by proposing to purchase the shares at their fair market value against the transferee (Bahtiyar, 2019: 332). In order for the company to exercise this right, the articles of association must contain a provision conditioning the transfer of the shares upon the company's approval (Poroy, Tekinalp & Çamoğlu, 2017: 146). In addition, the company must disclose the price to be paid for the shares, at the time it makes its proposal to purchase the shares (Poroy, Tekinalp & Çamoğlu, 2017: 146).

Lastly, in order to prevent circumvention of the context provisions contained in the articles of association, the legislator has given the company the right to refuse to record the transfer of the shares in the share ledger, in cases where the transferee does not explicitly declare that he has acquired the shares on the name and behalf of the company (Bahtiyar, 2019: 333).

However, in cases where the shares are acquired due to succession, sharing of succession, or pursuant to provisions of the property regime between spouses or forced execution, the company only has the right to refuse approval by proposing to purchase the shares at their fair market value. Therefore, if the shares pass through

succession as a result of the death of the partner, the company may refuse to give its consent by proposing to purchase its shares only at their fair market value.

The company should also report the value of the share, while notifying that it will take over the share (Bilgili & Demirkapı, 2013: 553).

If the transferee does not accept the value of the shares placed on them by the company as set forth in its notice, the transferee may, within one month, request that the commercial court of first instance where the company headquarters is located to determine of the fair market value of the shares (Bilgili & Demirkapı, 2013: 553). If the transferee does not object to the declared value within one month from the date of learning the real value, the proposal to take over the share, given by the company, is deemed to have been accepted (Bilgili & Demirkapı, 2013: 554; Poroy, Tekinalp & Çamoğlu, 2017: 147).

In the event of succession of a share upon the death of a partner, the rights of the assets arising from the shareholding pass immediately to the successor, while the right to attend the general assembly and vote only pass upon consent of the company (TCC, 494(2)). If the company does not refuse the request for approval within three months from the date of receipt, or if the refusal is unfair, it is deemed to have given the consent (TCC, Art. 494(3)).

2.3.2.2 At Listed Companies (Quoted on the Stock Exchange)

The legislator has allowed companies listed on the stock exchange to prevent the transfer of shares in two cases. The first situation, governed by TCC, Art. 495(1), is where the company recognizes the acquirer of the registered shares as a partner, but the articles of association stipulate an upper limit for such an acquisition, based on the capital, expressed in percentage, and can reject the proposed transfer if this upper limit is exceeded. In other words, the company may prevent the acquisition of the share by setting the acquisition upper limit, which is based on the basic capital and expressed as a percentage, in the articles of association.

The company may also refuse to register the shares in the share register upon the transferee's explicit declaration that he bought the shares in his own name and account despite his request (TCC, Art. 495(2)).

The last paragraph of the provision contains an exception regarding the acquisition of registered shares listed on the stock exchange by succession, sharing of succession, provisions of property regime between spouses, or forced execution. The common denominator in each such case is that the company does not have the opportunity to refuse the transferee the title of partner. Therefore, in case of succession of the share in the listed companies upon death of the partner, the company does not have the opportunity to prevent the transfer of the share. Thus, the legislator has not provided the companies listed on the stock exchange with the legal pre-emptive right (Bahtiyar, 2019: 339). However, companies not listed on the stock exchange could refuse to approve the transfer by proposing to take over the shares at their real value if their registered shares were transferred by succession (TCC, Art. 493(4)). However, as this right does not exist for companies listed on the stock exchange, the company must accept the shareholding capacity of the transferee (Pulaşlı, 2014b: 1652). Even where the company has stipulated some rate limitations or other contextual reasons in the articles of association, those limitations shall be invalid in terms of the transfer of the share by succession (Pulaşlı, 2014b: 1652; Bilgili & Demirkapı, 2013: 556).

2.4 Limited Companies

Limited companies are also capital companies, and, unlike joint-stock companies, they also have features in common with sole proprietorships (private company's). Within this frame, pursuant to TCC, Art. 595, the approval of the partners' general assembly is required unless otherwise stipulated in the articles of association regarding the transfer of the basic capital shares. The transfer is valid upon this consent. Unless otherwise stipulated in the articles of association, the partners may refuse to give consent to the general assembly without any reason. In addition, the transfer of the basic capital share may be prohibited entirely by regulating the same in association articles.

In some cases, the transfer of the basic capital share is realized by operation of law. Pursuant to TCC, Art. 596 (1), in cases where the basic capital share is passed by succession, or by provisions regarding the property regime between spouses or execution, all rights and obligations are transferred to the person who acquired the basic capital share without any need for approval of the general assembly. Upon death of the partner, in case the share passes by inheritance, the basic capital share will be transferred to the successor by law.

2.4.1 Notification to the Company of Death of the Partner and Exercise by the Company of the Right to Refuse

Under TCC, Art. 596(2), if the basic capital share is inherited, all rights and liabilities are transferred to the person who acquired the basic capital share without the need for the general assembly to give its consent. However, the company has a statutory right to prevent the person who took over the share from entering the company. TCC, Art. 596(2) provides that the company may refuse to approve the person to whom the basic capital share has been transferred within three months after learning about the acquisition.

To exercise this right, the company must offer the person to whom the share is transferred the opportunity to acquire the shares at their real values to the account of his own or his partner or a third party shown by its partner or a third party, at their real value (TCC, Art. 596(2)). The company may exercise the right to create a unilateral founding capacity on its own behalf, or on behalf of its partners or a third party pursuant to its legal pre-emption right (Poroy, Tekinalp & Çamoğlu, 2017: 420). Receipt of the company's notification by the drawee has legal consequences; namely, a purchase contract is established between the company and the transferee (Poroy, Tekinalp & Çamoğlu, 2017: 420). The company is required to exercise its right of refusal clearly and in writing (Şener, 2017: 342).

If the parties cannot agree on the real value, it will be determined by the commercial court of first instance where the headquarters of the company are located, upon the request of one of the parties pursuant to TCC, Art. 597. The court uses experts to arrive at the value (Poroy, Tekinalp & Çamoğlu, 2017: 421). To determine the court will use various criteria such as the balance sheet, profit and loss accounts, tangible assets of the enterprise and the nominal values of the intellectual and industrial assets (Poroy, Tekinalp & Çamoğlu, 2017: 421-422). Although the statutory provision does not specify when the actual value will be taken as a basis, it is appropriate to utilize the closest date to the resolution date. Some experts reach this conclusion by analogizing this provision to a similar rule found in TCC, Art. 493(5) (Şener, 2017: 350-351; Topaloğlu & Özer, 2019: 1958).

The law does not specify organ giving rise to this right. However, since all managerial powers, except the rights granted to the general assembly by law or articles of association, are exercised by managers, logically this authority belongs to the directors as a rule (Poroy, Tekinalp & Çamoğlu, 2017: 420).

The company is deemed to have given its consent if it does not expressly and in writing refuse the transfer of the basic capital share within three months. The three-month period is the period of prescription (Poroy, Tekinalp & Çamoğlu, 2017: 420). The period starts when the company learns about the transfer of the share or the right holder applies to the company with documents evidencing the transfer (Poroy, Tekinalp & Çamoğlu, 2017: 420-421).

2.4.2 Effects and Consequences of the Exercise of the Right of Refusal

The company's refusal resolution is effective retroactively from the date of the transfer (TCC, Art. 596(3)). However, the refusal does not invalidate the general assembly resolutions passed within the period until the resolution on this matter is passed. Accordingly, the person who acquires the share has the right to attend the general assembly meetings, and votes casted during the interim period are effective. The relevant general assembly resolutions shall be valid (Şener, 2017: 344; Bahtiyar, 2019: 457).

Although the share is legally transferred to the acquirer as a result of death of the partner under TCC, Art. 596, the fact that the company can prevent the acquisition by passing a retroactive refusal resolution from the date of the transfer may cause other problems. For example, if the acquirer of the share has filed an action, in his putative capacity of successor partner, for termination with fair reason within the framework of TCC, 636(4), the court should not start the case until his partner status is finalized (Şener, 2017: 344). Otherwise, the termination action, which may be filed by the partners, will be subject to possible dismissal if the court ultimately concludes the partner does not have successor's capacity (Şener, 2017: 344-345).

Case law

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