# The Obligation of Independent Auditing of Corporations under the New Turkish Commercial Code

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The New Turkish Commercial Code ("New Code") has been enacted and will enter into force in July 2012. One of the major changes brought by the New Code regards mandatory independent audits of corporations. Pursuant to the current Turkish Commercial Code ("TCC"), a corporation has to contain a general board, a board of directors and a board of auditors. Under the New Code, a board of auditors is no longer considered a mandatory body of a corporation; instead mandatory audits by independent firms are established. An auditor also being a shareholder of the audited corporation is prohibited under the New Code; in other words, auditors must be from outside the corporation. Pursuant to the New Code, such an independent auditor has to be a certified public accountant or an independent financial advisor.

The current TCC does not mention the applicable standards of auditing, whereas the New Code states that auditing activities shall be done according to the Turkish Accounting Standards complying with the International Financial Reporting Standards. Today, with the progress of the international financial market and increased economic relationships between countries, corporations have a greater need to have transparent and illuminating audit reports and therefore, the independent auditing obligation has been enacted to satisfy that need.

## Auditing of Corporations under the Current TCC

Corporations consist of three mandatory bodies, namely; the general assembly, board of directors and board of auditors. The current TCC divides the auditing obligation of corporations into two, internal and external audits. The New Code, however, has abolished the obligation of internal auditing and made external auditing mandatory.

Under the current TCC, auditors do not have to have specific qualifications. In practice, most of the time auditors are selected by the majority of the shareholders (in General Assemblies) from among themselves, without regard to their qualifications. Auditors are obliged to conduct audit activities within the corporation and protect the financial rights of the shareholders; however, they're not obligated to be from outside of the company under current legislation. Therefore auditors are not expected to be independent and impartial, since they are from within of the company.

Auditors do not have to be real persons; they can be legal persons as well, since there are no such restrictions under the TCC. The New Code attempts to meet the need for professional auditing. Therefore, auditors shall be professionals in their fields.

The duties of auditors are specified both under the TCC and the New Code. Pursuant to the TCC, auditors' duties can be considered in three (3) groups, consisting of monitoring/supervision, management, and representation. The New Code does not mention some of the duties of auditors listed under the current TCC, such as inspecting the cash desk of the company, supervising the official buyers, calling general assembly meetings, being present at meetings of the board of directors and general assemblies, examining and analyzing the problems of shareholders, etc.

## External Audit of Corporations

An external audit of a corporation is carried out by persons or institutions from outside of the corporation. An internal audit aims to protect the interests of the shareholders, whereas an external audit aims to protect not only the existing shareholders', but also prospective shareholders' interests and the economic order of the public.

External auditing is not mandatory under current legislation. External auditing is done by Ministry of Industry and Commerce auditors according to the existing Bylaw on the Auditing of Corporations, to verify the accuracy and correctness of the financial statements. The New Code mandates an external audit be done in accordance with the Turkish Accounting Standards complying with the International Financial Reporting Standards and only by a certified public accountant or an independent financial advisor. Furthermore, the scope of external audits has been extended in the New Code. Auditing of financial reports, including year-end and interim financial statements, and auditing of the annual report of the board of directors are considered within the scope of external audits under the New Code.

## Auditing under the New Code

As mentioned above, a board of auditors shall no longer be a mandatory body of a corporation under the New Code. Corporations may still form a voluntary internal auditing body. The New Code regulates the term "auditor" in more detail, giving auditors and the profession of auditing more importance. The main reason for removing the mandatory internal auditing body from corporations is that it has not been functioning properly, creating a need for independent audits by outside organizations/auditors.

Under the New Code, independent auditing includes not only a company's accounts and balance sheets but also all financial statements, accounting records and consolidated accounts of conglomerates. While composing financial statements, the standards set by the Turkish Accounting Standards Board are to be taken as a minimum. Moreover, the technical details and ethical rules set by the International Auditing Standards shall be followed as a reference. Auditing activities shall be conducted within the scope of institutional management and transparency principles and audit reports shall be explicit, clear, and comprehensible, and shall serve to inform the shareholders.

## Autonomy of the Auditors

Auditors shall be chosen by the general assembly and, pursuant to the New Code, auditors shall have no relationship with the audited corporation and their duties shall not be transferred wholly or partially to third persons. Pursuant to Article 399 of the New Code, there has to be a court decision and a valid reason, such as a violation of impartiality, to discharge an auditor.

The conditions to be an auditor are specified in detail under Article 400 of the New Code. Unlike the current TCC, under the New Code, neither people working in a company nor its shareholders may be auditors of that company. Pursuant to Article 400/2 of the New Code, the same auditor may audit a company at most for 7 years; after this period, the auditor shall be discharged from the company. The same persons auditing the same company over long years may have difficulty maintaining objectivity and independence.

Some of the duties of auditors stated in the current TCC are not stated under the New Code, such as calling general assembly meetings and being present at meetings of the general assembly and board of directors, as mentioned above. On the other hand, the obligation of auditors to be Turkish citizens is not mentioned in the New Code. Some conditions, such as the bankruptcy or conviction of an auditor, automatically terminate his/her duties under the current TCC, whereas this rule is not accepted under the New Code. Also, after how many years a member of the board of directors shall become an auditor is not stated in the New Code.

## Conclusion

With the New Code, new regulations are applied to corporations to meet modern social and economic needs. Undoubtedly, it is economically advantageous for corporations to have impartial and objective auditors and an auditing system that is in conformity with certain rules and standards. In this way, the auditing of corporations shall become more functional and specialized.

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