

## **Evolution of Business Law in Turkey: A Political Economy Perspective <sup>1</sup>**

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### **Abstract**

Recent literature shows that legal institutions have important implications for business activity and economic growth. While the scholarship has provided insights on the differential experience of countries, the Middle East has remained largely unexplored. This study examines the transplantation and evolution of business law in the late Ottoman Empire and early Turkish Republic, drawing broader implications for the economic and political determinants of legal transplantation. We argue that the underlying political economy context—in particular, the extraterritorial practices and the nation-building efforts—was influential in shaping the way commercial law was transplanted and evolved in Turkey.

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## **I. Introduction**

Recent literature in economics view legal institutions as important determinants of long-run economic and financial development. According to this view, legal innovations such as the joint-stock corporation and the private limited liability company fostered growth by allowing entrepreneurs to lock in capital, prevent untimely dissolution, take advantage of limited liability and more flexibly design control over the firm's assets. But such enterprise forms can better function and financial markets grow if the legal regime can more effectively protect investors from insiders (La Porta et. al. 1996 and 1997). There is still considerable disagreement about why these legal innovations emerged in some countries, but not in others. One branch of the literature, growing out of La Porta et al. (1998), claims that the legal origins of a country—whether common law or civil law—is a key determinant of the law's flexibility in adapting to changing economic conditions (Levine 1999). The assumption behind this line of research was obvious: Legal systems were largely exogenous, as most countries acquired them through colonization or conquest.

A growing literature challenged the legal origins on several grounds. First, some country-specific studies reveal a significant gap between statutory law and legal practice, implying vast potential heterogeneity between countries within the same legal family (Martínez-Rodríguez 2016, Hannah and Kasuya 2015). To the extent that such differences are also correlated with economic outcomes and financial development, earlier cross-country studies that categorized legal families by legal texts might have obtained biased inferences. Second, various studies showed that legal change in origin countries as well as legal change in transplants were deeply embedded in country-specific political economy (Parglender 2012, Mussachio and Turner 2013). Legal rules were not exogenous. Our study further supports this idea. By examining the case of legal transplantation in the late Ottoman and early Turkish Republic, we show that the Ottoman/Turkish political economy was an important factor in the transplantation of business law. We stress two features in this context: the practice of extraterritoriality, which familiarized much of the Ottoman population with the law that the state eventually transplanted, and the later nationalist

modernization efforts, which informed the reformers' attitudes towards legal change as well as economic actors' ability to voice demand for such change.<sup>4</sup>

Our study is also the first systematic study on the transplantation and evolution of business law in the late Ottoman Empire and early Turkish Republic. While there are many studies on the impact of legal institutions concerning economic activity in the Middle East, most of them focus on its earlier legal institutions derived from Islamic law. Scholars have recently explored how Islamic law diverged from Western Europe and what these differences implied for long term economic development (Kuran 2005, Kuran 2009, Rubin 2018). Yet, the question as to why legal modernization did not bring about the intended consequences in the region received little attention.<sup>5</sup> In the paper, we explore legal modernization in the region and stress two questions: How did policymakers choose which legal model to transplant, and what factors shape the peculiar aspects of the transplantation process? In particular, how did the transplanted law diverge from the origin law?

We attempt to answer these questions on nature of the legal transplantation by using primary sources on legislative discussions (particularly about company law), legal manuscripts, and new firm-level data that we have assembled. Together, these sources allow us to explore the factors shaping the transplantation process. First, we show that Ottoman reformers' choice to use the French legal code was not some haphazard decision; it was the culmination of a longer, drawn-out process that evolved out of legal practices in the Eastern Mediterranean. In the eighteenth century, European consular courts in Ottoman realms provided an exit option for non-Muslim merchants from Islamic courts by extending extraterritorial rights originally reserved for Europeans. These privileged merchants relied on French law extensively. Familiarity with the French legal tradition, especially among merchants and legal intermediaries who were responsible for developing the law contributed to the lawmakers' preference to follow French law as the model for transplantation.

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<sup>4</sup> In the eighteenth and nineteenth century context, extraterritoriality refers to claims of European states for jurisdiction over their citizens living and trading in the non-European world. This jurisdictional claim was justified with reference to the idea that the non-European world had primitive and arbitrary legal structure. See Kayaoğlu (2010: 18).

<sup>5</sup> Kuran (2004: 86-87) offers some preliminary explanations for why institutional transplantation did not bring about economic development in the region. Some of these explanations (namely, the lack of legal competence and state-centered development efforts that reinforced each other) are also corroborated by our findings.

The early efforts to transplant French commercial law reflected the top-down efforts to harmonize legal practice and formal law along with a concern for catching up with the developed countries. However, the gap between Ottoman and French laws widened after the initial reform and Ottoman law stagnated for almost 80 years. The sluggish development reflected two factors embedded in the late Ottoman political economy. The older and more experienced businesses, which were more familiar with the transplanted law and more likely to use and adapt it to local conditions, were mostly non-Muslim and could ‘exit’ through recourse to European consular courts. Access to these extraterritorial rights made non-Muslims less interested in demanding comprehensive legal change during the early, more liberal period of legal modernization (1839-1914). When the exit option was eliminated after 1914, a policy of ‘national economy’ replaced the previous liberal stance, deprived non-Muslims of agency in affecting legal change, and promoted the Muslim elite, who did not have the legal know-how and entrepreneurial skills needed to develop modern forms of business organization.

There were significant changes in commercial law in the early Republican period. However, these changes also reflected the ‘transplant effect.’<sup>6</sup> The legal reforms concerning business organization were intentionally selective to impose a degree of control over large companies, and incomplete due to partial and inconsistent translations of the targeted legal texts. The Turkish legislature, unlike in the origin countries, imposed very rigid controls over access to the corporation and the private limited liability company. These controls were justified with reference to a high risk of corporate misconduct and a strong need for statist regulation. Entrepreneurs and semi-public actors such as trade associations and chambers of commerce, did not seem to have made efforts for removing these entry costs. Since, during the Republican era, major business actors were bureaucrats and politicians who established and managed the largest corporations, most discussions on business law concerned the status and governance of corporations owned or supported by the state.

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<sup>6</sup> According to Berkowitz et. al. (2003: 167), the legal order in countries that receive the law through transplant effect “would function less effectively than origins of transplants that either adapted the law to local conditions and/or had a population that was familiar with the transplanted law.”

## II. The Road to the Transplantation in 1850

In the early nineteenth century, amid mounting fiscal and military challenges, as well as declining living standards relative to Western Europe, the Ottoman state became more willing to adopt Western institutions, especially legal rules. The Ottoman reformers were interested in legal reform for a multitude of reasons. First, European laws were seen as a way to homogenize legal practice and expand the hold of central bureaucracy. Given Islamic courts' pluralistic tradition and foreigners' extraterritorial claims, Ottoman central bureaucracy had little control over local legal practices. In this context, legal modernization—whether codifying Islamic law in the Western style or outright borrowing—was seen as an instrument for top-down centralization and became a priority during the nineteenth century.

Second, the reformers viewed legal modernization, especially in the case of commercial law, as a key strategy to engender development and catch up with the West. As early as the 1830s, Ottoman reformers noted the role of novel forms of business organization in facilitating economic growth.<sup>7</sup> Unlike legal transplantation in other fields of private law, there was no objection to the reformers' efforts to transplant Western commercial law. Some scholars attributed this to non-Muslims' dominance in trade and finance (Akçaoğlu 2009).

Commercial law was also relatively less controversial because of its subject matter. Civil code (*medeni kanun*) had to deal with issues such as marriage, divorce, and inheritance, on which the Sharia had clear provisions that diverged significantly from European law. While replacing these rules created considerable resistance among Islamic legal scholars, in economic and commercial matters, the bureaucrats were eager to claim that the Islamic law was capable of accommodating Western legal concepts such as fictitious legal personality and did not exhibit any resistance to such novelties.<sup>8</sup> As a result, in 1850, the Ottoman government promulgated the first European-style legal code in the region by translating and reproducing the first two parts of the 1807 Commercial Code as the Ottoman Commercial Code.

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<sup>7</sup> Sadık Rıfat Paşa, who was instrumental in launching a series of major political and social reforms after 1839, wrote on the important role corporations played in capital accumulation and economic development.

<sup>8</sup> Sir Anton Bertram, a British judge appointed to Cyprus in early 20<sup>th</sup> century, notes that while the concept of fictitious legal personality is strange to the Islamic law, the Islamic law “is at least perfectly familiar with the kindred conception of collective ownership” (Bertram, 1909: 35-36). He refers to Sava Paşa, the Greek-origin high-ranking bureaucrat who wrote extensively on Islamic jurisprudence, to claim that “there is no institution or conception of modern European law that, if it be but rightly approached, is not capable of ‘Islamization’”. See Bertram (1909: 36).

The choice to adopt French law was not a haphazard decision. First, the English book of statutes still lacked important features in 1850 (e.g., the Companies Acts) and thus could not be a model for transplantation at the time. More importantly, the commercial law and custom of the Levant was French (Bertram 1909: 28). The expansion of European trade in the Eastern Mediterranean during the eighteenth century led to a growing scope in Europeans' extraterritorial privileges, which came to include Ottoman non-Muslims, helped establish French law as the basis of legal framework for commerce and finance in the region.

Foreign merchants in the Ottoman Empire had long enjoyed these extraterritorial privileges thanks to the Capitulations, which were concessionary agreements the Ottoman government had made with European powers. These privileges allowed foreigners to use consular jurisdiction in commercial and civil disputes. European ambassadors could also extend these privileges to local non-Muslims by giving them *berats* (letters of protection). As foreign trade expanded in the eighteenth century, a market of *berats* bloomed. Non-Muslim Ottomans paid substantial prices to acquire these licenses and become protégés of European consular missions.<sup>9</sup> The *berats* placed their holders out of Islamic courts' reach and granted them access to European jurisdictions. Cases were usually decided through arbitration, in which prominent merchants of the area acted as arbitrators and the European consul or ambassador of the defendant acted as the judge. By the late eighteenth century, these protégés, approximately 1,700 traders in total, emerged as a central group in Ottoman-European trade.

In the early 1800s, the Ottoman administration designed its own privileged merchant corps as an attempt to replace the protégé system. Entry remained limited and fees were competitive with *berats* sold by European embassies. The new merchant corps, *Avrupa Tüccarı* (European merchants) for non-Muslims and *Hayriye Tüccarı* (merchants of goodwill) for Muslims, had the same fiscal benefits and exemptions as the European *berats*. Most importantly, it provided an alternative to Islamic courts by formalizing an arbitration procedure to settle disputes.<sup>10</sup> A new chancery was created to oversee the arbitration of these disputes, its members being

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<sup>9</sup> Artunç (2015) estimates the prices of French and British *berats* as approximately 55 times the Ottoman GDP per capita at the time.

<sup>10</sup> Local actors pursued access to foreign jurisdiction probably due to the disadvantages they had against foreigners in legal arbitration in Ottoman courts (Konan 2009; Kütükoğlu 1991)

drawn from prominent Muslims and non-Muslim merchants of that jurisdiction (Bağış 1983, pp. 66-7; Savvas Pacha 1902, pp. 54-6; Young 1905, p. 224). In this way, the Ottoman privileged merchants followed the European consular practice closely.

The arbitration was based on the customary law of merchants and that custom was French, a reflection of the strong French influence in Eastern Mediterranean trade (Eldem 1999).<sup>11</sup> The Ottoman commercial code and courts subsequently evolved out of these chanceries. In 1840, the government complemented these chanceries with proper commercial courts, which still employed privileged merchants as judges. The chanceries were subsumed into the new commercial courts only after the Law of 1860 (Savvas Pacha 1902, pp. 59-60; Young 1905, pp. 224-5).

The evolution of Ottoman commercial law shows that the administration did not simply import a foreign institution without diligence. When the lawmakers reformed the judicial system, they didn't have to look far. Most merchants engaged in foreign trade already had access to French law. There were legal practitioners, tribunals, and merchants familiar with French legal norms. The reform, therefore, accomplished two tasks. First, it naturalized 'foreign' institutions and legal instruments, which were already used in practice, into Ottoman law. Most important examples include the corporation and the bill of exchange. In doing so, the reforms affirmed the legality of these customs. Second, the new code made what used to be a separate legal jurisdiction—and access to which was previously rationed out—available to the whole public. In other words, the Ottoman legal transplantation was more about transforming a particularized institution into a generalized institution. Yet, the initial will to generalize access to Western legal institutions was only partially successful and did not translate into a dynamic legal system. In the next part, we will explore the reasons underlying latter stagnation.

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<sup>11</sup> French leadership in the Levantine trade came to an end in the aftermath of the French Revolution and the British emerged as the leading power when Eastern Mediterranean trade resumed in the 1820s after decades of war and disruption. See Pamuk (2000: 114). The rising British influence culminated in the signing of the Ottoman-British treaty of trade, Balta Limanı in 1838. But, expansion of English economic activity did not automatically translate into an Anglicization of the Ottoman commercial institutions. The fact that even the prevailing theories of free trade were transferred to the Ottoman realms through the French writers rather than English ones and the fact that French continued to be the *lingua Franca* among the Ottoman elite attest to the persistence of French influence.

## II. 1850-1908: The Era of Foreign Corporations

While the Ottoman Commercial Code of 1850 granted all Ottoman subjects access to French legal rules and new forms of business organization, the reform's success remained limited. The legal system remained essentially an inconsistent patchwork of Islamic and Western laws. The confusion might have discouraged Muslims' greater reliance on the new rules, especially since Muslims were unfamiliar with the European rules and business forms. Non-Muslims, who would have benefited the most from the new commercial code, had little incentive to affect change since they could more easily exercise their exit option and enjoy European consular jurisdiction directly through their extraterritorial privileges.

Successful implementation of the new legal code required complementary institutions, such as the creation of a legal infrastructure or training of legal professionals. The Ottoman government took some steps in this direction. It introduced new commercial courts to apply the new code under the Law of 1860 and set them up in various cities. A Code of Commercial Procedure was enacted in 1861 and a Code of Maritime Commerce was enacted in 1863; both codes were again translated from the French law. The Imperial Edict on Justice (*Ferman-ı Adalet*) promulgated in 1875 underlined independence of the judicial courts and the safety of judges and reiterated that state positions were open to all subjects of the Empire (Toprak, 30).

Yet, the familiarity with the notions and practices introduced with the new law was weak especially among Muslim businesses. For instance, the transplanted code required firms to keep accounts by using double-entry bookkeeping, but the Ottoman bookkeeping practice at the time (called *merdiven sistemi*) was based on a completely different set of principles. There were also no institutions providing education on economics, accounting, or business management up until 1870s.

The government tried to complement the reform by establishing schools designed to educate prospective bureaucrats in the Ministry of Justice about the new laws and regulations as well as other higher education organizations to teach secular and Islamic laws (Palabıyık, 2015). Especially in the Hamidian period (1876-1908), law education was systematized and Western law, along with economics, came to be taught as academic disciplines. Yet, Islamic law and secular legal systems continued to co-exist during this period.

The Ottoman religious establishment—dominated by the practitioners of the Hanafi school of law—resisted the reforms as their weight and importance within the state apparatus would relatively decline.<sup>12</sup> Ottoman bureaucrats were not willing to fully accept ‘foreign laws’ as it was considered an admission of inferiority. As a result, the leading Ottoman reformers initiated a project through which Islamic law, in particular *Hanafi* jurisprudence, was codified and presented in a new form. The *Mecelle*, the first attempt to codify Islamic law, was introduced in the Ottoman Empire, part by part, between 1868 and 1876. The result was an eclectic legal complex in which some parts were borrowed from Europe, and the rest was a modernized form of *Sharia*.

According to Avi Rubin (2007: 282), the massive borrowing from the French legal system side by side with the Sharia courts led to “a modified division of labor in the judicial bureaucracy.” Reformers also expected that the codification of the *Mecelle* would align Islamic legal practice with the custom of merchants. According to the reformers’ accounts, prior to the legal reforms, because of “judges’ ignorance of the Islamic law”, the merchants were reluctant to use Islamic law. Some judges, for instance, had refused to accept bills of exchange drawn between merchants as documents that could be acted upon (although according to the reformers, the bills of exchange were in line with Islamic legal precepts). This indicates that *Mecelle*, in fact, could also help justify the customary commercial practices and accommodate new institutions and practices introduced by the commercial code of 1850. Furthermore, co-existence of various courts based on both Western and Islamic traditions might have created “a certain space for forum shopping” for all Ottoman subjects.<sup>13</sup>

Nevertheless, scholars have also pointed to the inconsistencies between different parts of the civil law and the commercial law. For instance, the law of obligations, which was codified in *Mecelle* according to the Hanafi school of Islamic law, presented difficulties in interpretation and failed to deal with certain issues raised in the European legal systems (Velidedeoğlu, 1940: 196). More importantly, there is

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<sup>12</sup> As Amit Bein (7) notes, “the rapidly expanding government bureaucracy of the second half of the nineteenth century opened new employment opportunities and career paths for ulema”, but also “new secularist ideas and increasing competition from rapidly expanding new-style schools (...) appeared to increasingly threaten their employment prospects in government service.”

<sup>13</sup> According to Avi Rubin (2011: 15), the Nizamiye and the Islamic courts were “entwined components of a single judicial system,” and although there was a formal division of labor between them, the authorities allowed for a certain space for forum shopping.

little evidence on the use of new legal procedures and courts by the prominent Muslim families engaged in large scale business.<sup>14</sup> In fact, Ada Mafalde maintains that the new commercial courts were regarded as works in progress by most actors. For instance, Mataracıdaze brothers, a prominent family network with overseas business operations, were reluctant to apply to legal procedures in the New Commercial Code concerning commercial conflicts. Neither, they have attempted to form corporations. Nemlizedes, another elite family of mercantile background, did not try to form corporations until after 1914.

While the new legal system seems to have provided flexibility, it did not necessarily encourage adoption of novel forms of organization, such as the corporation, by Ottoman Muslim businesses. One reason why the use of new commercial code was limited might be related to the bureaucratic and political hassle that was involved in establishing enterprises using these forms. The registration of a corporation required a lengthy and costly process. An Imperial charter was required to incorporate. In the first step, the founders or their representatives had to go to the Ministry of Trade (*Ticaret Nezareti*) to purchase a model company statute, which was drafted by the government. While the model charter determined the standard outlook of Ottoman joint-stock company, it was possible to make modifications to the statute. After modifications, the founders had to present it to the Ministry. If the Ministry approved, then it sent the draft to the Council of State (*Şura-yı Devlet*) for further examination. After the charter was examined and approved by the Department of Finance (*Maliye Dairesi*) and then the General Council of the State (*Şura-yı Devlet Genel Kurulu*), it was sent to the Grand Vizier (*Sadrızam*). Upon approval, the Vizier sent it to the Council of Ministers (*Meclis-i Vükelâ*), which was the final authority to determine whether the charter was in line with the Ottoman Law of Commerce. After the Council's approval, once more the charter was sent to the Grand Vizier who had to deliver it to the Sultan. Upon the Sultan's approval, an Imperial edict authorizing the incorporation was issued.

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<sup>14</sup> The studies on trade networks and family businesses that depend on private archives are few and generally depend on the researcher's personal connections to the family. But, existing studies do not provide any evidence on the Muslim businessmen using commercial code or establishing novel forms of organization. See Mataracı (2016) and Cora (2013).

Table 1: The stages of incorporation

The draft of the company statute was examined by the ministry and changes are requested
<b>Council of State</b>
<b>Department of Finance</b>
<b>In the General Meeting of the State</b>
Minutes announce the decisions regarding the changes
<b>Grand Vizier</b>
For the further discussion
<b>Council of Ministers</b>
if approval was given
<b>Grand Vizier</b>
a letter in his own hand
<b>Sultan</b>
issue of the necessary edict
<b>Ministry of Trade</b> <b>(Also: Public Notary of the Istanbul Court of First Instance)</b>
If the company was granted special privileges ( <i>imtiyazlı</i> ), the concessionaire would transfer to the company all the rights arising from the concession
<b>Company</b>
(It would guarantee to carry out all the duties and responsibilities arising from the concession)
According to the statute, the incorporation of the company was not definitely completed until all the shares constituting the company capital had been signed and a payment of 10 % of the capital had been made

As summarized above, the incorporation process was subject to a highly cumbersome bureaucratic procedure and capital requirements, which could have been overcome only by the largest and well-connected firms. In fact, between 1850 and 1908, most of the corporations were established by foreigners through special concessions granted to them in order to undertake massive public projects.<sup>15</sup> Ottoman subjects, mostly

<sup>15</sup> We have surveyed the Ottoman Archives, contemporary primary and secondary sources to estimate the number of corporations established during this period (1850-1918). Data on the corporations

Muslim high-ranking bureaucrats and non-Muslims, did participate in the boards of these corporations, but rarely established any enterprise on their own. In other words, big enterprises, which were mostly foreign initiatives, operated beyond the realm of general rules of corporate law and consequently did not have any incentive to mold it.

Local entrepreneurs had little incentive to pursue legal change. First, the industrial establishments in urban centers were mostly small-sized workshops using traditional technologies. There were few indigenous businesses that could operate at a scale large enough to make the corporate form advantageous. Second, those who could potentially set up large-scale enterprises were not interested in establishing corporations under Ottoman law. Muslims, as we summarized above, were reluctant to establish corporations either because they were not familiar enough with the new legal procedures or they did not see it worth the effort given the long and costly process of incorporation. In fact, the leading Muslim businessmen were involved in the foreign companies' dealings with the Ottoman states as intermediaries, i.e. initial recipient of concessions.<sup>16</sup> Their ability to participate in local politics and combine functions of an Ottoman official with that of an established businessman was crucial in their endeavors.<sup>18</sup>

Non-Muslims, on the other hand, still had access to an outside option. Some of them established corporations but they did without having recourse to Ottoman law. In Macedonia, for instance, the integration into Western commercial networks throughout the nineteenth century did indeed enable emergence of wealth Greek orthodox and Jewish families (Sotirios Dimitriadis, 2014: 38-39). The widening scale of local commerce and industrial enterprises might have encouraged some of these

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established during 1914-1918 come from special folders in the Ottoman Archives (*i.DUİTs*) designed solely for keeping records of corporate charters and seems to be more comprehensive. There was no such source or registry for the previous period. Therefore, we had to build our estimate for the number of corporations established prior to 1914 on a variety of sources that were created for different purposes and hence the numbers may not add up to a definitive account of corporate sector. Our survey indicates that 221 "Ottoman" corporations (corporations established according to the Ottoman jurisdiction) were established in the core Ottoman lands (Balkans and Anatolia) prior to 1914.<sup>15</sup> While this number may be flawed, it is the most reliable estimate at the moment, given available sources. If we make an unrealistic assumption and suppose all these corporations have survived until 1914, the number would still indicate a very small corporate sector in the Empire.<sup>15</sup> Furthermore, more than half of these 221 corporations were public utility corporations (providing services such as electricity, gas, water, railroads) and banks established mostly by foreign capital. In other words, between 1850—when the corporate form was introduced—and 1914, use of the corporate form by the Ottoman subjects was extremely limited.

<sup>16</sup> Nemlizade family based in Trabzon were outstanding examples of this type of involvement. See Cora (2006).

<sup>18</sup> Dimitriadis (2013).

entrepreneurs to use new organizational forms and demand legal change. Yet, there's little evidence that shows that Greek families used corporations in their industrial enterprises.<sup>19</sup> Rather, they seem to have drawn upon their family networks and parish committees to raise funds. In fact, according to contemporary sources, red tape was a grave problem and political relations were crucial in doing business.<sup>20</sup> Given these problems, even among non-Muslims, only the wealthiest and the most well-connected would be able to start large businesses. The continued access to extraterritoriality, however, could be an additional asset for non-Muslims. Despite the restriction on the sale of *berats*, wealthy non-Muslims were still able to gain access to European law through by securing legal protection.<sup>21</sup> For instance, the richest Jewish families of Macedonia, Allatini and Mizrahi families, established a limited company to undertake tobacco trade: "The Commercial Company of Salonique Ltd." (İpek, 2011: 62).<sup>22</sup> Interestingly, these families were also the recipient of concessions from the government that allowed them to establish corporations. In other words, their use of legal forms not recognized in the Ottoman law, at least as long as the Turkish nationalism became the dominant ideology, did not raise alarm or jeopardize their political ties. This does not mean that the Ottoman government was content with the extraterritorial privileges. In fact, the Ottoman state challenged the normative basis of extraterritoriality as early as the Paris conference (Kayaoglu, 2010: 48). But, at least until the last quarter of the nineteenth century, the government did not attempt to invalidate the capitulatory treaties underlying these extraterritorial rights.

As a consequence, the law of 1850 remained stagnant and the new legal forms – as they existed under Ottoman law – did not generate a wide scope of use in the

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<sup>19</sup> Lapavitsas (2006: 14).

<sup>20</sup> Lapavitsas (2006: 22) cites Baker (1877: 408-409): Operating a factory would require "a three months stay in Istanbul to obtain the license, bribes for various officials, as well as administrative and tax difficulties with custom authorities in Thessaloniki over the import of machinery."

<sup>21</sup> Zendi Sayek, 62: Izmir's 1944 census: government appointed a bureaucrat to assess the claim of over 1500 persons of Maltese and Ionian origins was entitled to British protection... Proteges were largely conflated with non-Muslim subjects or with foreigners... Many claiming foreign nationality were born in Ottoman territories and from parents who were Ottoman subjects. Sayek citinbg Engelhardt, *La Turquie et la Tanzimat*, 1: 64, 2: 102... "Periodic governmental query to investigate dubious claims to foreign protection and nationality indicate the persistence of the problem through the nineteenth century". Until 1863, consular protection extended not only to individuals but also to their entire household and were transmitted through inheritance... the number of proteges must have increased rapidly and steadily.

<sup>22</sup> The headquarters of this company—established in 1895—was in London, but it also had a board of directors in Istanbul. The company survived until the World War, during this period the company was merged into "Austro-Hellenic Tobacco Company". The largest shareholder in 1935 was German Jewish David Schnur. (İpek, p. 62).

population. Muslims were strangers to European law and had little incentive to acquire the know-how to navigate the new law. Instead, they exercised the safer option of securing concessions for public projects from the government and selling them to European corporations. Non-Muslims, who had become the Empire's economic elite by the nineteenth century and had been using French law since the 1700s, were deeply familiar with the 'new' forms and rules the law of 1850 introduced. But their outside option remained intact and they preferred to use European legal rules directly; they had little use for the Ottoman commercial law and no reason to demand institutional change. As a result, until 1908, the government adopted none of the amendments the French had introduced and the legal barriers to incorporation persisted.

### **III. 1908-1923: The Era of “National Corporations”**

By 1908, the Ottoman code was well behind contemporary European law and the legal asymmetries in the commercial realm were obvious: Ottomans faced high barriers in accessing corporate form due to the concession system and bureaucratic red tape. Foreigners and non-Muslims with foreign protection, on the other hand, were exempt from such procedures and could operate according to the general incorporation laws of Europe. While these asymmetries, in particular capitulations, became subject of rising concern and criticism by Muslim intellectuals, there was little room for political action. The earlier state-led efforts at industrialization had mostly failed and transportation infrastructure was considered an urgent need. In 1870s and 1880s, the state had undertaken massive modernization projects with resource to foreign direct investment (i.e., foreign corporations were granted concessions to establish corporations in transportation and utilities). Foreign debt had led to bankruptcy and eventually foreign management of the major revenue sources of the Ottoman state in 1880s. The military and political weakness of the Empire was very apparent to the European powers.

Throughout the nineteenth century, furthermore, non-Muslims came to form an economic elite, most of whom had access to foreign protection. The political reforms, undertaken partially in response to the European pressures, enabled non-Muslims' participation in the bureaucracy and politics along with the spread of European patronage. These reforms, however, did not preclude the rise of separatist nationalism among the non-Muslims communities of the Empire. Increasing wealth of

the non-Muslim communities along with the spread of nationalist ideologies gave rise to a Muslim backlash.

Following the defeat in the Balkan Wars (1911-2), in which the Empire lost most of its European territories, Turkish nationalism turned increasingly hostile toward non-Muslims. In the process, the Young Turks, which started as a liberal reform movement and claimed to present all the ethnic groups of the Empire, turned into a group of ethnic nationalists determined to create a Turkish homeland. The Committee of Union and Progress (CUP), the political organ of the Young Turk movement, monopolized political power in 1913 and pursued policies aiming at ethnic reconfiguration of Anatolia. The attacks against Armenians and the accompanying plunder and confiscation of their property contributed to ethnic homogenization and demographic restructuring in Eastern Anatolia.<sup>24</sup> In Western Anatolia, many Greeks, pressured by deportations and forced conscriptions, started to flee to Greece. Furthermore, the CUP initiated a “national” economic policy, discriminating against non-Muslims through harassment, boycott, and exclusion from employment.

During World War I, the CUP government undertook some legislative and political actions favoring Muslims/Turks in the economic sphere. As mentioned above, unilateral abrogation of the Capitulations provided the government with unrestricted sovereignty. In December 1914, the government enacted the law concerning foreign corporations in the Ottoman Empire. Custom tariffs were increased first in October 1914 (from 8 percent to 15 percent) and then in May 1915 (to 30 percent). In 1916, ad valorem tax structure was annihilated and replaced by a protectionist one based on a specific tariff structure to support

The intensification of attacks against non-Muslims in the Empire also marked the end non-Muslims’ outside legal options. In 1887 and 1906, the Ottoman government had already attempted to subject foreign companies to Ottoman laws by enacting statutes requiring foreign corporations to acquire an official permission from the Ottoman Ministry of Commerce to operate in the Empire.<sup>25</sup> Yet, these statutes

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<sup>24</sup> The Armenian population, which had comprised 1.5 million at the beginning of the wars, was reduced to 100,000. For an assessment of the effect of the Young Turk economic policies on the Ottoman Armenian communities, see Üngör and Polatel (2011).

<sup>25</sup> “*Memalik-i Ecnebiyede Teşekkül eden Anonim Şirketlerin Memalik-i Devlet-i Aliyye’de İcra-yı Muamelat için Kuşad ve yahud Tayin Edecekleri Acenteler Hakkında Nizamname*” (1887) and “*Memalik-i Mahruse-i Şahane’de İfa-yı Muamele Etmekte Olan Ecnebi Anonim Şirketleriyle Sigorta Kumpanyaları Hakkında Nizamname*” (1906).

failed to take effect due to the foreign missions' objection that the new regulations violated the Capitulations. The outbreak of World War I allowed the CUP to abolish the capitulations in October 1914, affording the government to exercise unrestricted discretion over economic and fiscal policy.<sup>26</sup> The CUP immediately passed a new law that mandated foreign corporations to prove their activities outside of the Ottoman Empire.<sup>27</sup> While the legal costs of incorporation remained lower for foreign companies, the new regulation helped reduce the gap between foreigners and Ottomans, nevertheless.<sup>28</sup>

The removal of the Capitulations also allowed for protectionist measures. The government raised tariffs from 8 percent to 30 percent. At the same time, there was an empire-wide policy of "Turkification" that included harassment, boycott and exclusion from employment, targeting especially Armenian and Greek subjects of the Empire.

It is within this context of national economy program that Muslim-owned corporations flourished. During the war, the share of corporations established by non-Muslims<sup>29</sup> and by foreigners decreased significantly (from 18 percent to 5 per cent and from 31 percent to 6 per cent respectively). There was a substantial increase in the share of corporations established by Muslim subjects in total number of corporations (from 41 per cent to 79 per cent).

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<sup>26</sup> Towards the end of the nineteenth century, the capitulations came to be seen not only as a yoke on the Imperial sovereignty but also the foremost barrier to the development of the Empire and all previous efforts of the Ottoman government to weaken the capitulatory system were undermined by the European powers.

<sup>27</sup> "*Ecnebi Anonim ve Sermayesi Eshama Munkasim Şirketler ile Ecnebi Sigorta Şirketleri Hakkında Kanun-ı Muvakkat*" (December 1914).

<sup>28</sup> According to the 1914 statute, the ministry had to respond to the foreigners' application in three months. There was no such time limit for the grant of Ottoman corporate charters.

<sup>29</sup> Ethnic restructuring in the Empire should have also contributed to the decreasing number of new corporations established by the non-Muslims. By 1914, 150000 Greeks were already expelled from the Empire.

**Table 2:** Corporations' Founders, 1908-1918 (254 Companies).

Origin <sup>30</sup>	Number			Percentage		
	1908-1914	1915-1918	Total	1908-1914	1915-1918	Total
<b>M</b>	52	99	<b>151</b>	40.6	78.6	<b>59.4</b>
<b>F</b>	40	8	<b>48</b>	31.3	6.3	<b>18.9</b>
<b>N</b>	23	6	<b>29</b>	18	4.8	<b>11.4</b>
<b>NM</b>	7	7	<b>14</b>	5.5	5.6	<b>5.5</b>
<b>MF</b>	1	4	<b>5</b>	0.8	3.2	<b>2</b>
<b>FMN</b>	2	2	<b>4</b>	1.6	1.6	<b>1.6</b>
<b>FN</b>	3	0	<b>3</b>	2.3	0	<b>1.2</b>
<b>Total</b>	<b>128</b>	<b>126</b>	<b>254</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: Gökatalay, "Corporations in the Late Ottoman Empire", p. 31.

The speculative opportunities created by the war<sup>31</sup>, furthermore, provided an opportunity for political cadres to cooperate with local elites to use corporations as a vehicle for capital accumulation. The Artisans' League (*Esnaf Cemiyeti*), an association created with the direct support and involvement of the Ottoman political authorities, for instance, helped finance the three largest "national" corporations established to deal with food provisioning during the war. It registered Muslim tradesmen, most of whom were initially organized in guilds, and asked them to purchase shares. As such, it played a crucial role in establishing connections between political authorities and potential Muslim investors and enabled capital pooling in spite of the absence of capital markets.

There were other associations who were involved in raising revenue for the corporations established during this period.<sup>32</sup> The fact that most of the corporations restricted the transferability of the shares (either through restricting share transferability to foreigners or non-Muslims or just assigning a significant percentage

<sup>30</sup> F: Foreign, FN: Foreign-Non-Muslim, FMN: Foreign-Muslim-Non-Muslim, MF: Muslim-Foreign, M: Muslim, NM: Non-Muslim-Muslim, N: Non-Muslim

<sup>31</sup> When the World War began, France and Britain, major foreign investor states up until then, withdrew from the Empire; while Germany and Austria continued to invest (Geyikdağı, 2011: 526).

<sup>32</sup> Another association, which played an important role, in the establishment of national corporations was the Navy Association (*Donanma Cemiyeti*), which is examined in detail in Gökatalay, "Corporations in the Late Ottoman Empire.", Chapter 3.

of shares as “*titres nominatifs*”) also indicates that the capital pooling in these corporations was not enabled through impersonal share markets. The role of political networks in the emergence of the Muslim/Turkish corporations during this period is also corroborated by the data on the founders’ identity. Among 151 Muslim corporations established during this period, we were able to identify that at least more than 40 per cent have a politically affiliated person<sup>33</sup> as one or several of its founders.

**Table 3: Identity of the Founders/Managers<sup>34</sup>**

Founder	Number of Companies	Percentage (%)
Merchant	47	31.1
<b>Political Authorities</b>	40	26.5
<b>Political Authorities &amp; Local Notables</b>		
Local Notables	17	11.3
Local Notables	28	18.5
Unknown	18	11.9
Women	1	0.7
Total	151	100

Source: Ağır and Gökatalay, “Hukuk ve İktisat”.

This account of late Ottoman corporations reveal the peculiar way corporate form was utilized in the late Ottoman Empire. Most of the corporations were established by the political cadres through non-economic means. Political support from government is not unusual in the history of chartered companies. In the European history, the prominent joint-stock companies were formed by merchants who acted as “political communities in their own rights” that were entitled with jurisdiction such as collecting taxes, providing protection, and administering law (Stern 2011: viii). In the Ottoman case, some of the earlier companies also seem to have claimed some sort of administrative jurisdiction: They obliged local communities to purchase shares and forced out *corvée* labor. These practices, however, were never legalized in corporate charters. More importantly, late Ottoman companies (as well the companies

<sup>33</sup> “Politically affiliated person” refers to the CUP members, bureaucrats, Pashas, and the military.

<sup>34</sup> Many corporate charters identified their founders as the original administrative board to hold power during five years after the establishment.

established during the early Republican period) did not come to represent ‘vested interests’ of a mercantile group. Rather, they were composed of actors who represented themselves not as businessmen, first and foremost as members of political parties.

Some of these corporations—those who were connected to the local elites that were against the Ankara regime during the Independence War—were expropriated later by the new Ankara government. Among those which survived the political turbulence, only a few survived for more than a couple of years, and did so only with the support of the government. The emerging Muslim business class, if one could speak about such an autonomous group with vested interests, was still very weak and dependent on the state. More precisely, there were only a few Muslim/Turkish actors that had a background in trade or industry in the corporate business realm. The ones that had such a business background were usually co-opted into politics, assigned managerial positions in the state-sponsored enterprises and embraced a statist stance .

#### **IV. 1923-1950: The Era of Legal ‘Revolution’**

After the Turkish Republic was established, radical reforms were introduced in all areas of law. The minister of Justice was Mahmud Esad (Bozkurt), a Turkish nationalist who completed his doctoral studies on the Capitulations in the Ottoman Empire at the University of Fribourg, Switzerland. For the leading political cadres of the early Republic like him, the motivation of legal transplantation was not filling of gaps in the law but rather drastic modernization of society. In fact, he stated that he desired “not reform but a revolution of law” (Bozkurt 1998). The commissions of legal experts under his guidance examined foreign laws and prepared the Turkish Civil Code, which contained all of the two Swiss codes, the *Schweizerisches Gesetzbuch* and the *Obligationenrecht*; and the Turkish Civil Code, which contained statutes from German and Italian codes. When the proposals were presented to Mustafa Kemal, he is reported to have asked if there were people that were capable to put these ‘translated’ laws into practice in the country. The minister’s answer reflected his strong belief in the urgent need for legal change: “If you were informed that better weapons were invented in Europe, would you wait until you have people who are able to use them or get them and then train the people who are capable of using them?”

Years later, on the occasion of the *Festschrift* of the Istanbul Law Faculty to mark the civil code's fifteenth anniversary, Mahmut Esad explained the reasons for the codification with reference to problems in the preexisting legal system:

“The Turkish legal system was backward and primitive. Three kinds of religious laws were in force, Islamic, Christian, and Jewish, each with its appropriate court. Only a kind of law of obligations, the “Mecelle,” and real property law was common to all. Second, such an odd system of justice, with three kinds of courts, could not correspond to the modern understanding of the state and its unity. Third and most important, each time Turkey had demanded the removal of the capitulation terms of the First World War by the victorious Allies, the latter refused, pointing to the backward state of the Turkish legal system and its connection with religion” (Watson, 2011: 14).

The efforts to prepare new laws during the World War, furthermore, had proven to very slow. It was probably much easier to borrow from an already existing, more sophisticated system that can be used as a model than the creation of new autochthonous law (Watson, 2011: 15).

The new commercial code depended primarily on the German and Italian codes because, according to the Mahmut Esat, they were the most up-to-date and the most comprehensive commercial laws in Europe.<sup>35</sup> The need to adopt a commercial law was an urgent need because “the current law failed to meet the needs of commercial courts and dealing with all matters continued to rely on custom”.<sup>36</sup> While the authorities were eager about legal transplantation and confident about the superiority of the donor law; they did not accept all the origin laws as given. In particular, legal rules concerning businesses seemed to have diverged significantly from the origin laws. First, the code still retained the concession system of incorporation at a time when these restrictions had eroded in the origin countries many decades ago: The council of ministers had to approve the company's charter before it could be registered. In fact, when the new code was being discussed in the Parliament, some of the deputies suggested that the charters of companies should be examined not only by the Council of Ministers, but also by the Ministries which were

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<sup>35</sup> TBMM Zabıt Ceridesi, 2. Dönem, 25. Cilt, İçtima: 109, p. 590-591, 29/5/1926, Ticaret Kanunu ve Ticaret Kanununun Tatbikine Dair Kanun Hakkında (Ticaret-i Berriye hakkında kanun layihası 1/835)

<sup>36</sup> Ibid.

related the the company's realm of operation. The Minister of Justice stated that the concession requirement was indeed an 'exception'—in the original draft, there was no requirement of concession—, which was introduced into the law because of peculiar characteristics of the Turkish economy (*memleketin vaziyet-i hususiyesi*); because corporations and cooperatives were “more directly linked to public law,” “more prone to harming public good” but, “this requirement would be removed in the near future.” Therefore, he suggested that more 'exceptions' (such as approval of each ministry) should not be required. Yet, the concession system remained in place until 1950s.

On the other hand, the law leveled the field for Turkish and foreign corporations. Just before the new law was promulgated, both the Turkish and foreign corporations were subject to a concession process. But, the Turkish firms had to acquire the Council of Ministers' approval by a special decree and there was no specification as to how much time approval process could take. But, the process was more clearly defined for the foreigners.<sup>37</sup>

The aversion of the Turkish authorities towards general incorporation can be traced back to the late Ottoman period. Just a couple of years before the new Turkish state was established, In 1918, Mehmet Asım, editor-in-chief of the Ottoman newspaper *Vakit*, who also became a member of the parliament during the Republican era, writes the following about the corporations:<sup>38</sup>

“In order to understand the actual (or "true") economic development of a country, one must first examine the quantity and worth of the corporations in that country. Corporations are an important means of bolstering the economic prosperity of a country. Yet if these corporations are not kept under strict control, especially in countries such as ours whose inhabitants generally lack a good economic education, they can provide an opportunity for a group of crooked men to swindle away the wealth of the nation. In particular, if foreign investors are allowed to mingle among these crooked men, it is not difficult to guess how much harm they would do.”

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<sup>37</sup> In 1926, American Consul in Istanbul, Bie Ravndal, described the procedure that foreign corporations had to go through in detail. Accordingly, the formalities for registering a corporation only took about six weeks. G. B. Ravndal, *Turkey: A Commercial and Industrial Handbook* (No. 28). US Government Printing Office, 1926, pp. 203-204.

<sup>38</sup> The article appeared in *Vakit* in 1918. The original text is transcribed in C. Yılmaz, *Osmanlı Anonim Şirketleri*. Istanbul: Scale Yayıncılık, 2011, pp. 437-441..

While in the late Ottoman period and early Turkish republic, the concession system was justified with reference to potential risks (pertaining especially to the activities of the foreigners), in 1930s the concession system came to be justified with reference to the *etatist* (statist) outlook of the Turkish state. Ernst Hirsch, a German Jewish legal scholar specialized in commercial law, who immigrated to Turkey and trained a whole generation of legal scholars in the Istanbul Faculty of Law in 1930s and 40s, defended the concession system in following words:

“In a country ruled by a statist (*etatist*) government, the legal license of any legal entity cannot be unrestricted. That is why the formation of corporations are subject to concession by the legislator in Turkey.”<sup>39</sup>

Halil Arslanlı, Hirsch’s student and later collaborator who became one of the most important legal scholars of 1940s and 1950s in Turkey, wrote his thesis on the “The Effect of Statism on Corporations” and argued that a corporate entity cannot hold unlimited legal license in an ‘*etatist*’ state and explained the Turkish commercial code’s article regarding the concession system (Article 280) according to this principle.<sup>40</sup> Furthermore, Arslanlı points to some contradictions in the law due to the hybridity of the law, in particular inserting the “concession system” and related articles into French legal code, which was prepared according to the general incorporation principles.<sup>41</sup>

As a result of the concession system, incorporation continued to be a difficult and costly process, taken up almost exclusively by the largest enterprises in monopolistic and highly regulated sectors such as utilities. While incorporation was still subject to legislature’s concession in the 1926 code, the new Turkish code introduced the private limited liability company (*limited şirket*), or the PLLC. The introduction of the private limited liability form might be considered a significant novelty that made ‘limited liability’ more accessible for small and medium enterprises. According to the 1926 law, PLLC could be established by minimum of 2 persons and 1000 Turkish Lira as initial capital. These requirements were considered as the primary advantage of the PLLCs (Özbeý 1940, 10). Furthermore, there was no

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<sup>39</sup> E. Hirsch, *Ticaret Hukuku Dersleri*. Istanbul, 1938

<sup>40</sup> “*Etatist bir devlette hükmi şahsın hukuki ehliyeti gayri mahdut olamaz*”. See H. Arslanlı, *Türk hukukunda devletçiliğin anonim şirketlerin ehliyeti üzerine tesiri*. Unpublished dissertation, İstanbul Üniversitesi Hukuk Fakültesi, 1938.

<sup>41</sup> Arslanlı, *Türk hukukunda devletçiliğin*, referring to Articles 280, 300, 301, and 385.

official requirement of general meeting and auditor assignment for PLLCs that have less than 20 partners. These were also considered as a source of convenience provided by the PLLCs (Özbey 1940, 11).

There were, however, two issues that restricted the use of the limited liability form in the Turkish Republic. First, the provisions on the limited liability were taken from the French code in a condensed form. The reasons for this condensation is not clear,<sup>42</sup> but 7 years after the code was enacted, Mehmed Ali, the undersecretary of Trade, wrote a 200-page book on the legal features of the limited companies to clarify ambiguous elements in the Turkish commercial code and help illustrate the benefits of the form to the Turkish potential entrepreneurs.<sup>43</sup>

Second, in order to establish a limited liability firm, one needed to acquire permission from the Ministry of Trade. While this requirement was easier to meet compared to the Council of Ministers' approval needed for incorporation, it still made the Turkish law significantly more cumbersome compared to the French law, where a simple registration was sufficient for the firm to exist. In the above-mentioned book written to encourage spread of limited liability form, the author underlines the easy registration process as one of the advantages of the limited liability firms in other countries such as France and Germany. Yet, he also justifies the requirement on two grounds: First, the corporations, in Turkey, also required concession. In other words, Turkey was different from other countries in this respect as well and the reasons that require concession for corporations—without explaining what they were—would also justify a concession process, albeit a less demanding one, for the PLLCs as well. Second, as mentioned above, the legal provisions about the PLLC in the Turkish commercial code were incomplete/deficient and therefore, most rules concerning the company had to be incorporated into the contract. This, according to Mehmet Ali, implied too much freedom that might lead to creation of companies that would not fit into the 'limited' form and could harm stakeholders, most importantly the creditors of the firm (1933: 64-65).<sup>44</sup>

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<sup>42</sup> Mehmet Ali mentions that part of the law was taken from Germany, which had a separate act for the limited firms and part was taken from France. He says that the part that specifies contractual requirements for the limited firm were forgotten (“*her nasılsa unutulmuş*”) in the process of the transplantation. In another part, he says that lack of provisions concerning limited liability firms resulted from “absence of mind” (“*zuhul eserdir*”). See p. 68 and p. 79.

<sup>43</sup> Dr. Mehmet Ali, *Limitet Şirketler*, 1933.

Both the problems in the transplantation process (especially for parts concerning the limited form) and the averseness to adapt easier registration processes for the establishment of the private limited liability company might indicate a certain reluctance or ignorance on behalf of the policy makers about the introduction of this form in the country. Actually, it took 14 years after the Code of Commerce that introduced PLLC, for serious critiques of the concession system (for PLLC) to be raised by the Turkish legal scholars. In 1940, the chief editor of *Hukuk Gazetesi* (The Law Journal), Cevat Hakkı Özbey, published an article titled “There is a need for altering the legal provisions to promote limited companies and small scale enterprises.” In this article, Özbey argued for abolition of official permission requirement for the establishment of the private limited liability company. Yet, he also emphasized that he disagreed with the scholars who suggest, along with removal of the concession requirement, the abolition of official auditing for PLLCs. He considered the ‘official audit’ requirement as a legal provision in line with the two main principles of the Turkish state, statism (*devletçilik*) and populism (*halkçılık*). Legal scholars used the ideological underpinnings of the Turkish state as a justification for the strict state control. Whether this discourse reflected an actual ideological resistance against free incorporation and free registration (for PLLCs) inherited from the late Ottoman national economy or based on any observed threats to the so-called statist objectives of the Turkish government in 1940s is not clear.

Yet, even in 1940s, the number of private limited liability companies established in Istanbul seems to have been relatively small compared to partnership forms. [In late 1920s, 97 per cent of all multi-owner firms were corporation or limited liability in France; whereas only 32 per cent of all multi-owner firms were limited liability private company or corporation in Turkey. Furthermore, the limited liability firms were mostly restricted to the very large firms, firms that are considered in the highest initial capital range (*fevkalade*) according to the Istanbul Chamber of Commerce.] In Istanbul, there were only 192 corporations (8 per cent of all firms) and 30 PLLCs (1 per cent of all firms) in 1926. While there is a slight increase in the share of PLLCs, the total of PLLC and corporations did not go above 15 per cent of firms until 1950s.<sup>45</sup>

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<sup>45</sup> Even as late as 1970s, the total of PLLC and corporations was not above 20 per cent of all firms established in Turkey. Source: TOBB (The Union of Chambers and Commodity Exchanges of Turkey), correspondence with the Head of Statistics.

While in the late Ottoman period and early Turkish republic, the concession system was justified with reference to potential risks (pertaining especially to the activities of the foreigners), in 1930s the concession system came to be justified with reference to the statist outlook of the Turkish state. Ernst Hirsch, a German-Jewish legal scholar specialized in commercial law, who immigrated to Turkey and trained a whole generation of legal scholars and practitioners up until the late 1940s, defended the concession system on a statist regime's need to limit and regulate the formation of all legal entities.<sup>46</sup> His student and collaborator Halil Arslanlı, who became one of the most influential legal scholars in Turkey in the 1940s and 50s, defended regulation on all legal persons based on the same statist justification.<sup>47</sup> Arslanlı blames the ambiguity and contradictions in the law on appending statist regulations into a commercial code which essentially relied on a liberal system of incorporation.<sup>48</sup>

During the Republican Era, the reform was radical, but there were still continuities from the past: The restrictions on access to corporate and private limited liability form are the most obvious. Interestingly, until the end of 1940s, there were no challenges to these restrictions. The Turkish business class was still characterized by its dependence on the state support and patronage. In 1920s, the government supported "private" enterprises directly by acting as the major shareholder and creditor. Deputies, in collaboration with merchants, acted as founders of the new corporations and served also in boards. The debates in the Parliament on corporations during this period reflected two themes: use of political clout in favoring certain groups in business and capacity of government control/audit. Concerning the corporations with partial state ownership, there were discussions reflecting the conflict of interest stemming from state's dual role as shareholder and regulator. These debates, however, did not lead to creation of statutory laws concerning these mixed enterprises and seem to have led to increasing discontent about corruption.

In 1930s, the government embraced state-led industrialization and import substitution. the government nationalized foreign-ownership railways and coal mines and established several state-owned enterprises in key sectors as part of the first five-year economic plan of 1934. The state also extended credit to firms directly and also empowered some businesses for the distribution and retail of goods that state-owned

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<sup>46</sup> Ernst Hirsch, *Ticaret Hukuku Dersleri*, 1938

<sup>47</sup> "Etatist bir devlette hükmi şahsın hukuki ehliyeti gayri mahdut olamaz". See Arslanlı (1938).

<sup>48</sup> Arslanlı referring to Articles 280, 300, 301, and 385.

enterprises produced (Tezel 2015, pp. 298–99). Thus, the government continued to selectively favor certain private enterprises. While most of the state economic enterprises were formed as corporations, they were considered a distinct legal form and regulated according to a specific law. Statism prescribed extensive regulation and control of private business. The single-party regime implemented tight restrictions on private enterprise, labor organization, and civic engagement in the 1930s. As such, the statist discourse helped propagate the idea that the private sector had to function in accord with national interests, justified restrictions on private enterprises, and rationalized expropriation. It was within this context that the government imposed an extraordinary tax called the Wealth Tax (*Varlık Vergisi*) justified by the exigencies of the war economy in 1942. The tax was arbitrarily assessed and fell disproportionately on non-Muslim minorities. In a recent paper, we showed that the tax led to the liquidation of non-Muslim-owned firms, which were older and more productive, reduced the formation of new businesses with non-Muslim owners, and replaced them with frailer Muslim-owned startups. We should also note here that between 1924–1935, there were no non-Muslim deputies in the Parliament (and only a handful after 1935).

Our examinations of the legislative discussions indicate that there were no objections to the restrictions on corporations and PLLC until late 1940s. In a debate on the introduction of corporate tax,<sup>49</sup> Salamon Adato, a Jewish deputy who had been elected from the opposition party in the first multi-party elections in 1946, stated that the law concerning businesses was outdated (“from 140 years ago”), imposed suffocating bureaucratic procedure (in particular, the process that requires approval of charter and changes in the charter) on corporations and PLLCs, and it would be very unlikely to expect businesses to flourish under such conditions. The minister of commerce, Cemil Barlas, stated that these regulations were necessary “given the level of economic development and the fact that there were not enough auditory institutions (banks had little capacity to audit corporations).” He referred to Germany in 1890s and stated that general incorporation during this early period of economic development in Germany had led to abuse of minority investors. Cemil Alevli, an established businessman and a deputy from ruling party, supported Adato and also

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<sup>49</sup> 8. Dönem, 18. Cilt 73. Birleşim; 20. 4. 1949

used an example from German history: He stated that family businesses, such as Bayer, could actually turn into successful business because they could incorporate and avoid untimely dissolution. This discussion in the parliament probably marks beginnings of demand for legal change that would eventually lead to the 1957 Commercial Law that adopts general incorporation.

## VI

Ottoman statesmen legitimized corporations as a means of technical borrowing and catch-up; but the institutional framework within which these corporations were adopted exhibit some features peculiar to the political economic environment of the Ottoman Empire. The introduction of General Incorporation Acts was late (1957) in the Ottoman/ Turkish case. Furthermore, the private limited liability company, which was introduced as a more flexible, convenient form for small and medium enterprises, was also subject to a burdensome bureaucratic procedure. The transplantation process was incomplete and contained serious contradictions that legal scholars acknowledged and tried to solve for many decades. The law, however, barely changed between 1850 and 1926 and between 1926 and 1957 in response to these problems.

This legal stagnation could not be explained solely with reference to lack of legal experience and bureaucratic learning gap. The Muslim business class was weak and dependent on state support and patronage. Non-Muslims was one group that could have demanded legal change; but they were already a minority in the population and stripped of their political voice. Within this context, the capital-pooling mechanisms depended mostly on traditional political and social networks inherited from waqf- and guild-like institutions in the earlier period and state banks in the later period; rather than modern instruments such as banks and stock exchange. Muslim entrepreneurs—with sufficient means and political/economic capital—benefitted from the political support and the evolution of traditional institutions into ‘corporate’ practices; but had no incentive to demand further reduction of barriers to entry (to demand easy access to corporate and limited liability form), to demand legal innovations or governance structures improving investor rights.