BILATERAL INTERNATIONAL AGREEMENTS REGARDING THE PROTECTION OF FOREIGN INVESTMENTS

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1. OVERVIEW

Globalization, as it is known, is on its way to the formation of a single market across the world, obscuring the boundaries of nation states, accelerating the movement of capital beyond the borders of a single country's output and leading the phenomenon of investing abroad and foreign capital. However, each country has a different legal system and investment legislation. This brings a variety of risks and uncertainties for the investors and entrepreneurs in the country of foreign investment. In order to prevent the possibility of unexpected losses and increased costs, the investors demand legal security, political and social predictability, convenience and other advantages before bringing their capital to a foreign country.

Such expectations of foreign investors with capital have led to the creation of multilateral or bilateral agreements on the promotion and protection of foreign investments between the countries.

In general, bilateral foreign investment agreements provide protection and benefits to investors in two main areas:

1) Bilateral Investment Treaties (BITs)
2) Double Taxation Treaties (DTTs)

1.1. Bilateral Investment Treaties (BITs)

The main feature of BITs is to identify the scope of measures, incentives and tax benefits that are available to nationals and companies of one State in the territory of the other State for the promotion and protection of foreign investment.

The principle of fair and equitable treatment is one of the main standards in BIT's. It helps to ensure that the nationals and companies of one state will not be treated differently from their own investors and/or will not be placed in a less privileged position than their own nationals in the territory of the other state. Therefore, the foreign investors of one state can compete with the host countries' investors. However, the meaning of the fair and equitable treatment standard is not clearly defined in the BITs. The definition of the standard is to be found beyond the national legal standards and in the international minimum standard in customary international law. According to this understanding, the international minimum standard of "fair and equitable treatment" is characterised as an obligation on states to ensure that aliens are treated in accordance with the ordinary standards of civilisation irrespective of the standards they accord to their nationals.

Most-favoured nation treatment is one of the other pivotal standards of the BITs. Most Favoured Nation is defined as a treaty provision whereby a State undertakes an obligation towards another State to accord most-favoured treatment in an agreed sphere of relationships. The standard is such treatment accorded by the granting State to the beneficiary State, or to persons or things in a determined relationship with that State, not less favourable than treatment extended by the granting State to a third State or to persons or things in the same relationship with that third State.

Widely recognized other BITs provisions similarly provide international law standards for the protection of aliens' fundamental rights and interests. For instance, most BITs regulate the exercise of the state's power to expropriate foreign investments. Thus, expropriation is permitted only if it is carried out on a non-discriminatory basis, for a public purpose, in compliance with due process and the principle of payment of compensation. Capital transfer and repatriation provisions guarantee the free flow of funds. The provisions of dispute resolution provide the foreign investor with direct access to arbitration against the host state. All of these measures are fundamental provisions that foreign investors want to secure when investing abroad.

It is important for the investors to know in advance whether they can eliminate direct and indirect losses to be incurred as a result of the host state's decisions and practices.

To date, Turkey has entered into 92 BITs, majority of which have been signed with developed or developing countries of Europe, Africa and Asia.[1] Of these BITs 75 are in force today and 17 are not. Remarkably, the number of Turkish BITs increased considerably after Turkish investors began exporting their capital abroad in the 1990s. A comparative review of the substantive rights offered by the Bilateral Investment Agreements and Turkish BITs demonstrate that Turkey have gradually evolved towards a more 'liberal' stance on foreign investment protections that prevail in international practice.

In general the following are regulated under the BITs that Turkey is a party to:

- ✓ A preamble stating both the desire to intensify economic cooperation between the Contracting States and the recognising that encouraging and protecting investments will stimulate such economic cooperation;
- ✓ A number of definitions, the most important of which being the definition of 'investor' (who can claim under the treaty) and 'investment' (which investments are protected under the treaty);
- ✓ A list of the substantive rights protected under the treaty which include: (1) fair and equitable treatment; (2) national treatment; (3) most-favoured nation treatment; (4) full protection and security; (5) protection from expropriation; (6) protection from arbitrary and/or discriminatory measures and (7) a promise to observe obligations entered into in respect of the investment. Other common provisions regulate the host State's liability in the event that the investment is damaged due to war or civil unrest and guarantee the free transfer of payments in connection with the investment.
- ✓ Each Contracting Party shall, in its territory, promote investments by investors of the other Contracting Party and admit such investments in accordance with its laws (i.e. legislation, rules and decisions).
- ✓ Each Contracting Party shall provide fair and equitable treatment to the investments of investors of the other Contracting Party, once established, and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal of investments in its territory of investors of the other Contracting Party.

[1] The list of BITs that has been signed and ratified by Turkey can be found on the Ministry of Economy's Website regarding to Investment Abroad at http://www.ydy.gov.tr.

- ✓ More particularly, each Contracting Party shall accord to such investments full security and protection which in any case shall not be less than that accorded to investments of its own investors or investments of any other third State.
- ✓ If a Contracting Party has accorded special advantages to investors of any third State through an international agreement or reciprocal arrangement relating wholly or mainly to taxation with a third State or by virtue of agreements establishing customs unions, economic unions or similar institutions, that Contracting Party shall not be obliged to accord such advantages to investors of the other Contracting Party.
- ✓ The Contracting Parties shall guarantee the transfer of payments related to an investment. The transfers shall be made in a freely convertible currency, without undue restriction and delay. Such transfers include in particular, though not exclusively: a) proceeds of total or partial sale or liquidation of the investment; b) returns such as profits, interest, dividends, royalties or fees; c) funds in repayment of loans; related to an investment.
- ✓ The Contracting Parties shall create favourable conditions for investors of either Contracting Party in the territory of the other Contracting Party for the issuance of all necessary consents, authorizations and license reviews in accordance with the domestic law of the host country.
- ✓ If the investments of an investor of the one Contracting Party are insured against non-commercial risks under a system established by law, any subrogation of the insurer or re-insurer into the rights of the said investor pursuant to the terms of such insurance shall be recognized by the other Contracting Party, provided that the insurer shall not be entitled to exercise any rights other than the rights which the investor would have been entitled to.
- ✓ The Contracting Parties shall seek in good faith and a spirit of cooperation a rapid and equitable solution to any dispute between them concerning the interpretation or application of the Agreement. In this regard, the Contracting Parties agree to engage in direct and meaningful negotiations to reach such solutions
- ✓ Disputes between one of the Contracting Parties and an investor of the other Contracting Party, in connection with their investment, shall be endeavoured to be settled through consultations and negotiations in good faith before applying to an arbitral tribunal.

1.2. Double Taxation Treaties (DTTs)

Double Taxation Treaties are conventions between two countries that aim to eliminate the double taxation of income or gains arising in one territory and paid to residents of another territory. They work

by dividing the tax rights each country claims by its domestic laws over the same income or gains. DTTs are significant instruments of increasing the amount of foreign investment. Over 1,300 Double Taxation Treaties exist world-wide to prevent the double taxation of income of international investors, all of which aim to eliminate discrimination in terms of taxation that may occur between domestic and foreign taxpayers. Turkey has one of the largest networks of DTTs with more than 90[2].

The followings incomes and gains are entitled to relief from double taxation: Income from Immovable Property (Real Property); Business Profits; Shipping and Air Transport; Associated Enterprises; Dividends; Interest; Royalties; Gains; Independent Personal Services; Dependent Personal Services; Directors' Fees; Artistes and Athletes; Pensions and Annuities; Government Service; Students, Apprentices, and Teachers; and Other Income.

Items of income and gains that are mentioned above do not explain the conditions for relief. The text of the particular double taxation treaty must be referred to for full details. The specifics of a particular treaty can rule the right to taxation either in accordance with the law of a contracting state where the income is earned or in accordance with the law of the other contracting state where the income is transferred. Sometimes the right to taxation is shared between the two contracting countries. The provisions of the DTTs provisions provide exemptions and deductions in case taxation is made in both contracting countries over the same income.

The benefits of DTTs may be summarised as follows:

- ✓ To prevent or reduce the effects of double taxation;
- ✓ To avoid the application of international taxation regime;
- ✓ To harmonize taxation between contacting parties;
- ✓ To prevent tax evasion and financial fraud;
- ✓ To ease foreign investment;
- ✓ To increase transparency of financial transactions and economic cooperation;
- ✓ To ensure the fulfilment of the conditions of reciprocity;
- ✓ To increase the amount of investments between contracting parties within the framework of above targets.

[2] The list of DTTs that has been signed and ratified by Turkey can be found on the Revenue Administration's Website at www.gib.gov.tr

2. DISPUTE RESOLUTION AND ARBITRATION IN THE CONTEXT OF BITs and DTTs

Bilateral International Agreements usually require arbitration as a dispute resolution mechanism between the investors and host states. UNCITRAL (United Nations Commission on International Trade Law), ICSID (International Centre for the Settlement of Investment Disputes) and ICC (International Chamber of Commerce) are the major arbitral institutions which are often preferred in the resolution of foreign investment disputes. The application of such dispute resolution mechanisms by investors are offered either gradually after exhausting amicable settlement mechanisms in good faith or as an alternative to litigation in the foreign courts.

In general two major arbitration mechanisms are followed by BITs and DTTs to resolve disputes between foreign investors and the host country: Ad Hoc Arbitration or Institutional Arbitration. Ad hoc arbitrations are conducted entirely in accordance with parties' agreement to arbitrate, without designating any institution to administer the arbitration. Ad hoc arbitration agreements often select an arbitrator or arbitrators to resolve the dispute, the applicable arbitration laws and rules without institutional supervision. The parties will sometimes also select a pre-existing set of procedural rules designed for ad hoc arbitrations. For international commercial disputes, UNCITRAL has published a set of such rules, the UNCITRAL Arbitration Rules. The Rules provide a mechanism for the appointment of arbitrators if the parties are unable to agree upon a presiding arbitrator or sole arbitrator. If three arbitrators are to be appointed, each party shall appoint one arbitrator. The two arbitrators thus appointed shall choose the third arbitrator who will act as the presiding arbitrator of the tribunal. More than 60 bilateral international agreements of Turkey provide UNCITRAL Arbitration Rules as a dispute settlement mechanism for investors. In contrast, Turkey's BITs with Germany, USA, United Kingdom, France, Israel and Kuwait include dispute settlement mechanisms without the benefits of UNCITRAL Arbitration Rules.

In addition to Ad hoc arbitrations, investment disputes may also be resolved under the auspices or supervision of the International Centre for Settlement of Investment Disputes ("ICSID"). ICSID administers arbitrations and conciliations pursuant to the so-called "ICSID Convention" or "Washington Convention" of

1965.[3] The Centre is based at the Washington D.C. headquarters of the International Bank for Reconstruction and Development (or "World Bank"). ICSID's case load has increased significantly over the past several decades, rising from roughly 1 case filed per year in the 1970s to roughly 30 cases per year in 2012 and 2013. It is the most preferred dispute resolution mechanism for disputes involving claims by foreign investors against host states; investment disputes typically arise under contracts containing ICSID arbitration clauses or pursuant to bilateral investment treaties. Thus, ICSID Arbitration is most commonly preferred dispute resolution mechanism provided under the dispute resolution clauses of Turkish BITs. Turkey signed the Washington Convention on 24 June 1987 which became Law No. 3460 with its publication in the Official Gazette on 6 December 1988.

Turkey is also a party to the Convention Establishing the Multilateral Investment Guarantee Agency of 1985 (known as "MIGA Convention"), which is a standard form contract of guarantee, a set of general conditions of guarantee for equity investments, and a set of arbitral rules similar to ICSID's for resolving political risk insurance claims. Almost all BITs, which were created after Turkey's ratification of the Washington Convention, provide ICSID Rules of Arbitration in their settlement of dispute clauses. The exceptions to this practice are Turkey's BITs with the Russian Federation and the Republic of Iran.

With the ICSID Convention having been ratified by more than 150 countries, the ICSID Centre provides a truly universal and most effective forum for resolving investment disputes through arbitration. To the extent that other forums are necessary, institutional dispute resolution mechanisms of major European arbitration centres like the Arbitration Rules of the ICC's International Court of Arbitration, the Institutional Arbitration Rules of the SCC (Stockholm Chamber of Commerce) Arbitration Institute and the Arbitration Rules promulgated by the United Nations Commission on International Trade Law (UNCITRAL) provide attractive alternatives. MIGA provides an institution for offering affordable political risk insurance worldwide in order to protect investors from non-commercial risks.

One of the most important provisions of the ICSID Convention is automatic recognition of ICSID arbitral awards that is stated under Article 54 of the Convention. It provides for the recognition and enforcement of ICSID awards by the courts of all States parties to the Convention. In addition to this general obligation, Article 54 offers certain procedural directions: Parties to the Convention shall designate the competent authorities for recognition and enforcement to the Centre; a party to arbitration proceedings may submit a

[3] Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, produced at Washington, D.C., 18 March 1965, available at www.worldbank.org/icsid.

certified copy of an award to such an authority; the modalities of execution are governed by the law concerning the execution of judgments of the country where execution is sought. This enforcement provision is a distinctive feature of the ICSID Convention.

Most other instruments governing international adjudication do not cover enforcement but leave this issue to domestic laws or applicable treaties. These domestic laws and treaties typically provide for some review of arbitral awards at the enforcement stage. The most important treaty in this context is the 1958 [New York] Convention on the Recognition and Enforcement of Foreign Arbitral Awards. It provides a universal constitutional charter for the international arbitral process, whose expansive terms have enabled both national courts and arbitral tribunals to develop durable, effective means for enforcing international arbitration agreements and awards. However, it is recommended that an investor check the legal status of the Convention to see whether the host country adopts any reservation or notification before ratifying the Convention. Article V of the Convention lists a number of grounds on which recognition and enforcement may be refused. The permissible exceptions to the obligation to recognize foreign awards are limited to issues of jurisdiction, procedural regularity and fairness, compliance with the parties' arbitration agreement and public policy; they do not include review by a recognition court of the merits of the arbitrators' substantive decision. To date, 146 nations have ratified the Convention. Turkey signed the Convention on 02 July 1992 which came into force on 30 September 1992.

One of the other most common arbitral institutions is the ICC's Court of International Arbitration which is located in Paris. The ICC is the best known arbitral institution in the world for handling international commercial arbitration, and many governments and government-owned companies have consented in international contracts to arbitration under the ICC Arbitration Rules. Such disputes may involve foreign investment claims as well as ordinary commercial issues. Turkey's BITs with Azerbaijan, Kazakhstan, Kyrgyzstan, Libya, Uzbekistan and Ukraine envisages ICC Arbitration Rules as a dispute resolution mechanism.

3. CONCLUSION

As discussed in detail above, bilateral agreeements are a good way for the states to promote and protect foreign investment in their territories. They help to protect the economic interests and legal rights of investors in a foreign country which ultimately helps to increase the flow of investment between the

contracting states. Bilateral agreements are also often coupled with tax exemptions and incentives offered to foreign investors from other countries in a bid to make the host country a more attractive place for investment.

It is highly advisable for businesses wishing to invest abroad to conduct a thorough review of the investment treaties between their country and the country in which they are planning to invest. A further examination of their legal rights, investment protection standards, double-taxation relief instruments and other applicable guarantees should also be made whilst assessing whether the host country is indeed an investment-friendly country. Finally, an effective and efficient dispute resolution mechanism is equally important as the incentives as it is vital for investors to have the safe knowledge that they have recourse to adequate legal remedies to recover their losses and damages in the event of disputes.

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