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Turkey's Court of Cassation Refuses to Enforce an Arbitration Clause in English Based on a Turkish Language Requirement

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In a recent decision, Turkey's Court of Cassation refused to enforce an arbitration clause in an English language contract between a Turkish party and a foreign party based on Turkey's national language requirement for commercial enterprises, the Code on the Mandatory Usage of the Turkish Language in Commercial Enterprises No. 805 ("Law No. 805").

The Contract

The contract at issue is a Licensing and Distribution Contract ("Contract") between a Swiss company that produces and sells health products ("Swiss Co."), as licensor, and a Turkish company that handles the import, export, marketing, and sales of health products ("Turkish Co."), as licensee. The parties signed the Contract in English, without a Turkish counterpart. The Contract is governed by Swiss law and includes an arbitration clause.

The Turkish Court Proceedings

Swiss Co. filed for a declaratory judgment against Turkish Co. in the Turkish court of first instance, the 12th Civil Commercial Court of Ankara ("Commercial Court"). Swiss Co. asked the Commercial Court to declare that Swiss Co. had rightfully terminated the Contract based on Turkish Co.'s non-performance of its contractual obligations. Turkish Co. objected to the request of the Commercial Court to hear the merits of the case because of the existence of an arbitration clause. This argument was accepted by the Commercial Court.

Swiss Co. appealed the Commercial Court's decision. The Court of Cassation overruled the Commercial Court's decision on the grounds that the Commercial Court had failed to take into account in its decision Law No. 805 and the obligation of Turkish parties to draft contracts in the Turkish language, and it remanded the case to the Commercial Court.

On remand, the Commercial Court accepted the Court of Cassation's reasoning and denied Turkish Co.'s objection to its jurisdiction to hear the substantive case based on the arbitration clause. The Commercial Court noted that while the contract is valid, the arbitration clause could not be invoked by Turkish Co. Accordingly, the Commercial Court made a substantive ruling on the merits and decided that Swiss Co. had rightfully terminated the Contract.

Turkish Co. appealed the Commercial Court's decision, and argued that Law No. 805 did not apply

to commercial contracts, but only to commercial books and records. The Court of Cassation rejected Turkish Co.'s argument and upheld the Commercial Court's decision. It found that based on Article 4 of Law No. 805, Turkish Co. could not invoke the arbitration clause because it was in English. The Court of Cassation upheld the Commercial Court's decision that Swiss Co. rightfully terminated the Contract.

Turkish Co. has appealed the Court of Cassation's decision and asked for a correction of the judgment (*karar düzeltme*) and the case is currently pending before the 11th Civil Law Chamber of the Court of Cassation.

Law No. 805

Law No. 805 is relatively short, comprised of only nine articles. It was adopted in 1926, shortly after Turkey became a Republic in 1923, when Turkey was actively promoting the use of the Turkish language as state policy.

The most important provisions of Law No. 805 are as follows:

Article 1: *“All types of Turkish companies and enterprises shall use the Turkish language in all kinds of transactions, contracts, communication and bookkeeping in Turkey.”*

Article 2: *“For foreign companies and enterprises, this obligation applies to all kinds of transactions and communications with Turkish companies and persons, and whenever foreign companies are obliged to disclose documents and company books to government bodies or officials.”* Unlike Article 1, Article 2 does not include the word “contracts”.

Article 3: *“Even though the companies referred in Article 2 can use a secondary foreign language in their transactions, the Turkish copy shall prevail, and the binding signatures shall be put on the Turkish copy of such documents. In case the signatures are on the foreign language copy of the contract despite this prohibition, the Turkish text shall be acknowledged.”*

Article 4: *“Documents and papers that are drafted after this Law becomes effective and are in violation of the above articles will not be taken into consideration for the benefit of the companies and enterprises.”*

Article 7: *“Any person that acts in contradiction with the provisions of this Law shall be imposed with a judicial fine that is not less than one hundred days.”*

Jurisprudence

Although Turkish parties and foreign parties routinely enter into contracts only in English, to our knowledge this decision is one of less than a dozen cases in which the Turkish courts have applied Law No. 805. The Court of Cassation selectively applied Law No. 805 to deny enforcement of the arbitration clause by Turkish Co., but enforced the rest of the Contract (also in English) on behalf of Swiss Co. Unfortunately, the Court of Cassation did not give a detailed analysis in its decision.

A look back at the few decisions in which Law No. 805 has been applied by the Turkish courts does not provide much guidance.

- 1977: The court enforced a clause which was written in the English language and contained in a

Turkish contract, finding that the clause was customarily in English.

- 1979: The court refused to enforce a due date clause which was in English and contained in a bank security letter in Turkish given to a government office.
- 1986: The court dismissed the argument that a foreign company doing business in Turkey should execute a contract in Turkish.
- 2006: In a dispute between a Turkish bank customer and a Turkish branch of a foreign bank, the court of appeals found that the lower court should have considered Law No. 805.
- 2009: In the same dispute, on remand the lower court decided that the Turkish branch of a foreign bank could not rely on a contract that was not in Turkish.
- 2012: The Court of Cassation directed the lower court to consider, because both parties to the contract were Turkish, whether Law No. 805 applied to the dispute, and if so, to decide whether the arbitration-related clauses of the contract would benefit the defendant.
- 2014: In a dispute between a foreign pharmaceutical company and a Turkish distributor, the court dismissed the case because it found the arbitration clause was invalid in the contract as it was drafted in English.
- 2015: In a dispute between two Turkish companies related to a sales agreement in English, the Court of Cassation remanded the case because the lower court did not consider Law No. 805. On a second appeal, the Court of Cassation remanded again, finding that the dispute should not be resolved based on the contract but on general Turkish laws.

Analysis

While the Court of Cassation's recent decision sheds some light on the interpretation of Law No. 805, it also leaves some questions. Significantly, the Court of Cassation's application of Law No. 805 to the Contract resulted in the enforcement of the Contract except for the arbitration clause. Because the Court of Cassation (and the Commercial Court in the earlier decisions) did not explain its reasoning in detail, we cannot be sure of the entire legal basis for the denial of Turkish Co.'s invocation of the Contract's arbitration clause.

The Court of Cassation may have differentiated between the parties, as Law No. 805 imposes slightly different obligations on Turkish and foreign parties. In fact, it reasoned, applying Article 4, that the arbitration clause could not be taken into account for the benefit of Turkish Co. That is, Turkish Co. failed to comply with Law No. 805 in making the arbitration agreement and cannot invoke arbitration as a defense in seeking termination of the Turkish court litigation against it. The Court of Cassation also may have reasoned that the arbitration clause was rendered inapplicable for both parties because an arbitration clause that could be invoked by only one party (here, Swiss Co., as a result of Article 4 operating to preclude Turkish Co. from invoking the arbitration clause) would be invalid under Turkish law. The Court of Cassation has a very high standard for assessing the validity of arbitration agreements, which must establish explicitly, exclusively, with certainty, and without any doubt the parties' agreement to arbitration. Here the Court of Cassation may have decided that an arbitration clause in violation of Law No. 805 is not exclusive, if not valid.

Going Forward

We await the final decision of the Court of Cassation, which could clarify the scope of application of Law No. 805. Until then, foreign and Turkish parties doing business together in Turkey should be cautious and may wish to execute their arbitration agreements as separate contracts in English and Turkish versions. For existing contracts including arbitration clauses between foreign parties and Turkish parties that have been executed in only English, if the parties agree, a Turkish version

of at least the arbitration clause can always be executed to avoid possible future complications.


The case reference is: *X v. Y*, Court of Cassation, 11th Civil Law Chamber, File No. 2016/5836, K. 2017/4720, dated 26/09/2017.

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This entry was posted on Saturday, September 29th, 2018 at 9:08 am and is filed under [Arbitral seat](#), [Arbitration](#), [Arbitration clause](#), [Domestic Courts](#), [Enforcement](#), [Turkey](#)

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