# Could a Reduction in a State's Income Violate Public Policy – A View on Turkey?

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**The Public Policy Exception as an Unruly Horse**

There is an ongoing quest for a uniform application of the New York Convention. However, the interpretation of the exceptions to enforcement still varies. Albeit applying the same provisions, national courts continue to adopt different approaches to the enforcement of foreign arbitral awards. This is particularly true where the public policy exception is raised under Art. V(2)(b).

Considerable debate exists as to what the public policy is. To the extent it is capable of definition, the public policy is found to embrace nebulous concepts such as a state's most basic notions of morality and justice. Due to its vague and unpredictable application; the public policy described by an English judge as "*a very unruly horse, and when once you get astride it you never know where it will carry you*."[fn]*Richardson v Mellish* [1824]2Bing229, 252.[/fn]

Driven by the motivation of taking advantage of the ambiguous nature of the public policy, the parties often raise the public policy exception where all other arguments for setting aside or refusing of the enforcement of the foreign arbitral awards have failed. As described by one national court: "*the public policy ground is often invoked by a losing party raised to frustrate or delay the winning party from*

*enjoying the fruits of a victory.*"[fn]A v R [2009]HKCFI 342.[/fn]

Partially in reaction to this, in many developed jurisdictions, courts have taken very restrictive and demanding views of public policy. Indeed, some national courts acknowledged that even when their domestic rules were inconsistently applied in arbitration, this was not in itself enough to refuse enforcement provided, i.e., that international public policy was not violated.

On the other hand, the unruly horse has not been fully tamed in some jurisdictions. In those countries, the inconsistent or broad application of the public policy exception may cause a severe infringement of the legal expectations of the parties to the arbitration and significantly decrease those countries' reliability on legal predictability.

## Unruly Horse is not Fully Bridled in Turkey, Especially when the 13th Civil Division of the Turkish Court of Cassation is in the Saddle

In Turkey, the Turkish Court of Cassation's interpretation of the public order has changed throughout the years and embraces a trend towards a pro-arbitration approach. Nevertheless, it is still not possible to conclude that the task is complete and that the unruly horse of public policy is fully controlled in Turkey.

Previously, the Turkish Court of Cassation was using the public policy exception as a gateway to examine whether the tribunals correctly applied Turkish law or not. Although this appeal-like role ceased after the entry into force of the International Arbitration Act in 2001, the Turkish Court of Cassation continued to use the public policy exception as a tool to get "desired results". Indeed, in its previous decisions, the Turkish Court of Cassation found that the ICC arbitrations' scrutiny process violated Turkish public policy, and as a result refused to enforce arbitral awards with the ICC *cache*. Similarly, despite the parties having agreed that the seat of arbitration would be Switzerland and that Turkish law would be applicable, the Turkish Court of Cassation refused to enforce the final award stating that the "Turkish law" term also covers the Turkish procedural law, and the tribunal should have applied the Turkish procedural law as opposed to the Swiss procedural law.[fn]Court of Cassation 15th Civil Chamber, File No:1617, Decision No:1052 dated 10.3.1976.[/fn]

This perception has been changing, and Turkey has been transforming into an arbitration-friendly country thanks to the new pieces of legislation and change in the national courts' perception of arbitration. This is especially evident after the Turkish Court of Cassation's General Assembly on Case-Law Unification decision of 2012, in which it concluded that the lack of reasoning in a court decision or an arbitral award does not constitute a violation of Turkish public policy.[fn]Court of Cassation, General Assembly on Case-Law Unification, File No:2010/1, Decision No:2012/1 dated 10.2.2012.[/fn]

Current predominant practice of the Turkish Court of Cassation suggests that there is a violation of the foundations of Turkish public policy on enforcement of the arbitral awards only in cases where the award is contrary to the principles that underpin the public or commercial life of Turkey, as well as in cases where it is contrary to the fundamental notions of justice. In this context not every violation of the mandatory legal rules can be classified as a violation of the public policy.

However, this arbitration-friendly approach is apparently not endorsed by the 13th civil chamber of the Court of Cassation. The 13th civil chamber of the Court of Cassation is still continuing to abuse the public policy exception to not to enforce decisions against Turkey. In fact, the 13th civil chamber of Court of Cassation consistently sets aside, or refuses the enforcement of foreign arbitral awards, by arguing that "*the reduction in an income of the State would clearly violate the economic balance and public policy*."[fn]Court of Cassation, 13th Civil Chamber, File No:2015/16140, Decision No:2017/3322 dated 16.3.2017.[/fn]

One of the most popular decisions of the 13th civil chamber of Court of Cassation was dated back to 2012. The dispute was related to a concession agreement concluded between a GSM operator and the Turkish Information Technologies and Communication Authority ("TITCA"). The tribunal concluded that the discounts provided to distributors on wholesales were required to be excluded from the base of the shares. Accordingly, TITCA approached the Turkish courts to set aside this award due to a public policy infringement. The Turkish Court of Cassation held that even though the shares stipulated in the concession agreement did not constitute a tax *per se,* but that they were an important and continuous source of income for the State. Therefore, the reduction in such an income of the State would clearly violate both economic balance and public policy.[fn]Court of Cassation, 13th Civil

Chamber, File No:2015/16140, Decision No:2017/3322 dated 16.3.2017.[/fn]

Although this decision was believed to be an example of an unfortunate and singular decision, the 13th civil division of the Turkish Court of Cassation endorsed the same approach also in 2014, 2015, 2016, and 2017. In those decisions, the 13th civil division of Turkish Court of Cassation either set aside the arbitral awards by arguing that "*the reduction in an income of the State would clearly violate the economic balance and public policy*", or overturned the decision of the first instance court by suggesting the first instance court to undertake an evaluation whether such an award results in the decrease of the income of the State and decide accordingly.

In line with the work distribution of the civil chambers of the Turkish Court of Cassation, if the dispute is related to

1. water, electricity, natural gas, phone and internet subscription agreements,
2. waste water prices,
3. joint ventures,
4. invalid contracts, or
5. strict liability provisions,

set aside and/or recognition and enforcement actions are to be brought before the 13th civil division of the Turkish Court of Cassation. Accordingly, if one of the disputing parties is a state and the award requires a reduction in the income of that state, the recognition and enforcement of the award will likely be rejected, or the award could be set aside.

## Suggestions and Future Perspective

The decisions of the 13th civil division of the Turkish Court of Cassation are a reminder that dealing with the public policy exception continues to be a struggle for the Turkish courts. There is no doubt that the decisions of the 13th civil division of the Turkish Court of Cassation are contrary to the nature of the arbitration. These decisions suggest that if an arbitral award touches in the economic gains of a state, it violates its public policy and it is either to necessary to set it aside or

deny the enforcement of it.

To circumvent the vexing decisions of 13th civil chambers of the Turkish Court of Cassation, the parties might refer their disputes to ICSID arbitration rather than other arbitration institutions and/or to *ad hoc* arbitration. As widely known, the ICSID awards are directly enforceable in contracting states and there is no recourse available to national courts in ICSID arbitrations.

Otherwise, there is a risk that the final award would not be enforced or it would be set aside by the 13th civil division of the Turkish Court of Cassation. Investors and the arbitration practitioners are eagerly waiting with fingers crossed for one of the first instance courts which will insist on its decision and try to convey the issue to the General Assembly of the Turkish Court of Cassation to finally resolve the issue.

Nevertheless, the re-organisation of the structure of the Turkish Court of Cassation to establish a separate civil division specialised on international arbitration law is under consideration. If this happens, it would avoid any incompatibility among different chambers of the Turkish Court of Cassation, and would make Turkey an even more arbitration-friendly jurisdiction. As an English judge said in response to his distinguished predecessor's observations: "*With a good man in the saddle, the unruly horse can be kept in control*."[fn]*Enderby Town Fc ltd v. Football Association [1971] Ch 591, 606-7 CA*.[/fn]