Arbitration Law in Turkey

The past two decades have seen an increase in trade globalization and growth of transnational companies, resulting in an escalation of cross-border disputes. In capital-importing countries like Turkey, this increase has led to a significant growth in the number of international arbitrations. In 2010, the number of disputes referred to the ICC Court of Arbitration that had at least one Turkish party was 76, i.e. nearly 10% of the total number of 793 claims raised under the auspices of the ICC that year. In 2011, this ratio was slightly less, with 46 parties from Turkey out of a total of 796. This increase in recent arbitrations has finally resulted in serious efforts to establish an international arbitration center in Istanbul, and has also prompted the development of more detailed provisions on local arbitration in the Turkish Civil Procedure Law.

I. A New International Arbitration Institution: Istanbul Arbitration Center

The "Strategy and Action Plan for the Istanbul International Financial Center," prepared by Turkey's State Planning Organization and approved by the High Planning Council, states that in order to make Istanbul a global financial center, *"it is necessary to make improvements in the area of law, in order to bring expeditious and effective resolution of disputes in the field of finance, to establish an institutional arbitration center and to accelerate legislation of draft laws that would contribute to the Istanbul International Financial Center Project."*[1]

The High Planning Council has characterized the establishment of an independent and autonomous institutional arbitration center that is capable of competing internationally with respect to cost, speed and effectiveness as "Priority No. 2." For this purpose, a working group comprised of scholars and jurists conducted an extensive study under the supervision of the Ministry of Justice regarding the structure and functioning of various arbitration centers around the world. These centers included the Arbitration Center of the Union of Chambers and Commodity Exchanges of Turkey; the German Arbitration Association; the American Arbitration Association; the London Court of International Arbitration; and the Zurich Arbitration Center, among others.[2] Upon completion of the working group's study, it prepared and submitted a draft Law of the Istanbul Arbitration Center (the **"Draft LIAC"**) that would govern the rules and principles of the establishment, organization and operation of the Istanbul Arbitration Center, to the Prime Ministry in March 2011.

Although the Strategy and Action Plan for the Istanbul International Finance Center was prepared in October 2009, the Istanbul Arbitration Center, the establishment of which is one of the priorities of legal improvements, has not been established as of yet. On 30 November 2012, the Turkish Union of Chambers and Commodity Exchanges (the **"UCCE"**) organized a conference on the Istanbul Arbitration Center. We attended this conference expecting that

[1] www.ifm.gov.tr/SitePages/ifmgiris.aspx
[2] The Prague Trade and Agriculture Chamber's Arbitration Court, the Singapore Arbitration Center and the Dubai Arbitration Center.

the draft rules of Istanbul Arbitration Center would be made public. However, we unfortunately realized that the draft rules had not yet been prepared.

When drafting the rules, the Turkish arbitration community should be well aware that in order to be able to take part in the very competitive world of international arbitration, the Istanbul Arbitration Center must ensure that these rules be in the same direction with the time-tested institutions such as the ICC, Zurich Arbitration Association and London Court of International Arbitration. Further, the rules that will be adopted must be based on the principles of neutrality and impartiality, principles that contract makers seek when deciding on the clauses of resolution of disputes in international contracts. If the Istanbul Arbitration Center's objective is to be a competitive international center for the resolution of disputes, it must attract the target audience with well drafted rules, and must provide neutrality and impartiality, experienced arbitrators and secretariat as well as competitive costs, as emphasized by almost all of the speakers from all around the world in the UCCE's conference.

The Prime Ministry finished its examination on the Draft LIAC in March 2013, and accordingly, the Draft LIAC was submitted to Presidency of the Grand National Assembly of Turkey (the **"Parliament"**) on 25 March 2013.

Under the Draft LIAC, the Istanbul Arbitration Center will determine the rules of arbitration, as well as other alternative dispute resolution mechanisms, within six months following the enactment of the LIAC. The Center will have one Local Arbitration Court and one International Arbitration Court, thereby separating the monitoring of proceedings in local disputes from those with an international element. Several Turkish scholars and practitioners have taken an active role in promoting the establishment and development of the arbitration center. As per Article 17 of the Draft LIAC, it will enter into force on 1 April 2014 (if approved by the Parliament before that date).

II. Improvements in Turkish Legislation in the Field of Arbitration

In the past few years, significant changes in legislation in the field of arbitration have been passed in Turkey. This has resulted in arbitration becoming more popular and common. The International Arbitration Law (the "**IAL**") has been in force since 5 July 2001, which is mostly based on the UNCITRAL Model Law on International Arbitration. The IAL governs international arbitration proceedings conducted in Turkey, while the Civil Procedure Code applies only domestic arbitration with no foreign element.

1. Scope of Application and Implementation of the IAL

The IAL is a law of procedure and governs the rules in arbitrations where there is a "foreign element" and the place of arbitration is in Turkey.[3] Even if the place of arbitration is not in Turkey, the IAL is applicable if the parties agree on or the arbitrators decide on its applicability. Under the IAL, a foreign element exists if:

(i) the parties to an arbitration agreement have their domiciles or habitual residences or places of business in different countries;

[3] Decision of the 15th Civil Chamber of the Court of Appeals dated 15 November 2007, numbered 2007/3708 E., 2007/7216 K.

(ii) one of the following places is situated outside the country in which the parties have their domiciles or habitual residences or places of business:

- the place of arbitration; or

- a place where a substantial part of the obligations arising from the underlying contract to the arbitration agreement is performed or a place where the dispute has the closest connection;

(iii) a shareholder of a company that is a party to the underlying contract brings foreign capital into Turkey or where loan and/or guarantee agreements need to be signed in order for the execution of that contract; or

(iv) in accordance with the underlying contract, capital or goods move from one country to another.

If one of the above circumstances exists, the IAL will be applied to arbitrations in Turkey.

As to whether the dispute is subject to arbitration, Article 1 of the IAL excludes two types of disputes. These are disputes arising from or related to rights *in rem* on immovable properties in Turkey and disputes the subject of which cannot be disposed of by the parties, such as disputes in connection with criminal or public law.

An arbitral award where the IAL has been applied is considered a local arbitral award. For this reason, such arbitral awards are directly enforceable and are not required to be subject to an enforcement lawsuit in Turkey. On the other hand, the party who wishes to prevent its enforceability can file a lawsuit in a court of first instance requesting that the arbitral award be set aside. Under this Article:

> *"The application for setting aside an award may be made within thirty days from the date of notification of an award or a decision on correction or interpretation or an additional award. This application will automatically suspend the execution of the arbitral award".*

An arbitral award rendered within the scope of the IAL may be set aside only on the grounds set forth in Article 15 of the IAL. This Article specifically excludes the possibility to appeal an arbitral award. However, the decision rendered by the court in the lawsuit for setting aside can be appealed.

The grounds for setting arbitral awards aside are listed in Article 15 in a *numerus clausus* manner, under two main titles. These are (a) causes to be taken into consideration by the judge *ex-officio* and (b) causes to be proved by the requesting party.

Although more than ten years has passed since the IAL's entry into force, only 24 decisions of the Court of Appeals relating to set aside proceedings are publicly available.[4] Some of these decisions will be examined below.

[4] Three of them were rendered in 2002, one of them was rendered in 2005, eight of them were rendered in 2006, six of them were rendered in 2007, one of them was rendered in 2008, two of them were rendered in 2009, and the last two decisions were rendered in 2011 and 2012.

(a) Grounds that Must Be Considered "Ex-Officio" by the Court of First Instance

Under Article 15 of the IAL, an arbitral award may be set aside if the court finds that (i) the subject matter of the dispute is not capable of settlement by arbitration under Turkish law; or (ii) the award is in conflict with the public policy.

(b) Grounds to be Proved by the Requesting Party

Article 15 further provides the causes of setting aside an arbitral award that must be proved by the requesting party. If the party requesting the court to set aside the arbitral award proves that:

(i) a party to the arbitration agreement was under some incapacity; or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication regarding the law applicable, the arbitration agreement is invalid under Turkish law;
(ii) the composition of the arbitral tribunal is not in accordance with the parties' agreement;
(iii) the arbitral award was not rendered within the term of arbitration;
(iv) the arbitral tribunal unlawfully found itself competent or incompetent;
(v) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration;
(vi) the arbitral proceedings were not in compliance with the parties' agreement or, failing such agreement, with the IAL, and such non-compliance affected the substance of the award; and
(vii) the parties were not treated with equality,

the court of first instance will set aside the arbitral award.

As an example of reasons for setting aside an arbitral award in accordance with Article 15 of the IAL, the Court of Appeals has held that the arbitrators cannot render a decision exceeding the defendant's responses raised in its responsive petition, as the arbitrators are bound by the responses of the defendant.[5] The Court of Appeals has adopted a liberal approach when determining whether or not a dispute is covered by the arbitration agreement. In a dispute related to a roaming agreement, the tribunal decided that it lacked jurisdiction to hear the dispute. Upon the claimant's request to set aside the tribunal's decision, the court of first instance dismissed the claimant's request on the ground that the subject matter of the roaming agreement did not fall within the scope of the arbitration agreement. Upon appeal, the Court of Appeals held that, as the dispute was directly related to the performance of the roaming agreement, it fell within the scope of the arbitration agreement. For this reason, the Court of Appeals reversed the court of first instance's decision.[6]

In another decision of the Court of Appeals, it was held that the arbitrators were competent to render decisions regarding their own competence as well as the validity of the arbitration

[5] Decision of the 15th Civil Chamber of the Court of Appeals dated 11 May 2011, numbered 2010/7197 E., 2011/2857 K.
[6] Decision of the 11th Civil Chamber of the Court of Appeals dated 8 March 2007, numbered 2005/12747 E., 2007/4160 K.

agreement. If this competence was used in contradiction with the arbitration agreement or the law, this issue should be considered in a lawsuit to set aside an arbitral award.[7]

The Court of Appeals recently rendered a decision regarding the determination of the competent court. The defendant of the arbitration was a joint stock corporation established in France. The claimant filed the setting aside proceedings in the 2nd Civil Court of First Instance of Kadıköy. The defendant objected to the court's competence, but this objection was rejected by the Court. The defendant then appealed the decision and the Court of Appeals held that the defendant did not have a place of business in Turkey and, thus, in accordance with Article 15 of the IAL, the lawsuit for setting aside the arbitral award should have been filed before the civil court of first instances of Istanbul (not the civil court of first instance of Kadıköy).[8]

2. Domestic Arbitration Rules under the New Civil Procedure Law

From 5 July 2001, when the IAL entered into force, until late 2011, Turkish international arbitration procedures were governed by the IAL while domestic arbitration procedures were governed by the Civil Procedure Law No. 1086 of 1927 (the **"Former CPL"**). However, the Former CPL was replaced in October 2011 by the New Civil Procedure Law No. 6100 (the **"New CPL"**). Unlike the Former CPL, the New CPL is more aligned with the IAL in that it better reflects international legal and procedural principles even though it applies only to domestic arbitration proceedings.

Article 407 of the New CPL provides that *"the provisions herein [i.e. in the eleventh section of the CPL] are applicable to disputes that do not contain any foreign element in terms of the International Arbitration Law and where the place of arbitration for the settlement is agreed to be Turkey."* Under this article, therefore, in order for the rules of arbitration of the New CPL to apply, (i) a dispute must not have an international element, and (ii) the venue of arbitration must be Turkey.

One novelty of the New CPL is that while it requires arbitration agreements to be in writing, it states that an arbitration agreement contained in an exchange of letters, telegrams, facsimiles, etc. may also be deemed to be "in writing." Although this is much more flexible than the Former CPL, which required a written contract signed by both parties, it is still more stringent than the UNCITRAL Model Law, which provides that *"an arbitration agreement is in writing if its content is recorded in any form, whether or not the arbitration agreement or contract has been concluded orally, by conduct or by other means."* The New CPL also states that if the parties mutually agree during the course of a lawsuit before a national court to refer the dispute to arbitration, the court must send the file to an arbitrator/arbitral tribunal.

Under Article 414 of the New CPL, *"the arbitrator/arbitral tribunal may grant any interim measures it deems necessary in respect of the subject-matter of the dispute at the request of either party, unless otherwise agreed by the parties."* The Former CPL did not give parties the opportunity to request that an arbitral tribunal decide on interim measures, as the sole competent authority to decide on such measures was the national court system.

[7] Decision of the 15th Civil Chamber of the Court of Appeals dated 27 June 2007, numbered 2007/2145 E., 2007/4389 K.
[8] Decision of the 11th Civil Chamber of the Court of Appeals dated 15 March 2012, numbered 2012/2110 E., 2012/3915 K.

Even under the New CPL, parties will still have to rely on national courts to enforce any interim measures granted by the arbitral tribunal.

One of the most significant changes introduced by the New CPL relates to the competence of an arbitral tribunal to rule on jurisdiction and the existence/validity of an arbitration agreement. Under Article 422 of the New CPL, the arbitral tribunal in a domestic arbitration is empowered both to determine its own jurisdiction and to decide on the existence/validity of the arbitration agreement. This effectively establishes a statutory foundation for the competence-competence principle that was not recognized under the Former CPL.

Another novelty found in the New CPL relates to the term of the proceedings. Under the Former CPL, arbitrators had to render their final awards within six months. The New CPL has extended this term to one year, which is much more reasonable in light of the fact that failure to render an award within the statutory term has frequently been used by the Court of Appeals as a ground for nullifying arbitral awards.

The most noteworthy improvement in the New CPL relates to the method of recourse against an arbitral award. Before the New CPL's entry into force, arbitral awards could be appealed on the grounds listed in Article 533 of the Former CPL. However, the Court of Appeals often rendered controversial decisions regarding the legal grounds for appeal, applying a very broad interpretation to the grounds listed in Article 533. In some cases, the Court of Appeals even went so far as to examine the merits of the claim. By contrast, Article 439 of the New CPL seems to be a fundamental change that, hopefully, will bring this problem to an end.

Under Article 439, an arbitral award rendered in a local arbitration is no longer subject to an appeal before the Court of Appeals. In fact, the only legal challenge that can be brought against an arbitral award is a set aside request before the courts of first instance. Article 439 also lists the grounds for which such set asides can be granted. These grounds are much less likely to be interpreted broadly, as, like the IAL's provisions; they are listed in a *numerus clausus* manner. This is expected to prevent judges from intervening in the merits of a claim. As Article 439 was imported from the IAL, the rules for setting aside awards in both local and international arbitrations are now harmonized.

III. Enforcement of Foreign Arbitral Awards

Arbitral awards rendered in accordance with the IAL or the New CPL will be deemed "local arbitral awards". In this regard, such awards will be directly enforceable in Turkey just like a national court's decision (unless set aside). On the other hand, foreign arbitral awards are subject to an enforcement lawsuit in order for them to be enforceable in Turkey. The International Private Procedure Law (the **"IPPL"**) provides the conditions of a foreign arbitral awards' enforceability in Turkey. Furthermore, Turkey is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the **"New York Convention"**).

The grounds for refusal of recognition and enforcement of foreign arbitral awards listed in the IPPL[9] are similar with the grounds of refusal specified in the New York Convention. On the other hand, as the New York Convention does not contain any procedural rules and leaves the procedure of recognition and enforcement lawsuits to the law of the country

[9] The IPPL entered into force on 27 December 2007.

where the recognition and enforcement is sought, the procedural rules for recognition and enforcement lawsuit are the rules provided in the IPPL.

As to the grounds for refusal of recognition and enforcement, the enforcement of a foreign arbitral award may be rejected by the Turkish court, if:

(i) no arbitration agreement was ever been entered into or the underlying contracts do not contain any arbitral clause;
(ii) the arbitral award is against general ethics or public policy;
(iii) if the issue which is the subject of the foreign award is not arbitrable according to Turkish law;
(iv) a party was not been duly represented before the arbitral tribunal and did not afterwards accept the acts and actions in arbitration in clear terms;
(v) the respondent was not been duly informed of the appointment of arbitrators or failed to present or defend its case;
(vi) the arbitration agreement or clause is considered invalid in accordance with the law agreed upon by the parties, or in its absence, with the law where the award was rendered;
(vii) the appointment of arbitrators or the arbitral procedure applied infringes on the parties' agreement, or in the absence of such agreement, the law of the place of arbitration;
(viii) the arbitral award is related to an issue not covered by the arbitration agreement or clause or beyond the border of the coverage of such agreement or clause (in this latter case, only the part that goes beyond the limit of the arbitration agreement or clause shall not be enforced); and
(ix) the arbitral award has not become final, enforceable or binding in accordance with the law applicable to the award, or in its absence, the law of the place of arbitration, or with the applicable procedure to which the award is subject.

Instead of a detailed examination of the enforcement rules stated in the IPPL, it would be better to examine some significant decisions of the Court of Appeals regarding the enforcement of foreign arbitral awards.

As can be seen in all decisions of Court of Appeals regarding the enforcement of foreign judgments or arbitral awards, the examination on "public order" is one of the most invoked grounds for refusal of recognition and enforcement. In a very recent decision of the General Assembly of the Court of Appeals rendered on 8 February 2012, the Court emphasized in its decision that the conformity of the foreign arbitral award to Turkish public order must be taken into consideration by the courts. The dispute was related to tax law and the General Assembly of the Court of Appeals underlined that a taxing issue is an issue related to public order. For this reason, the General Assembly of the Court of Appeals overruled the decision of the court of first instance enforcing the arbitral award related to a dispute of tax law.[10]

As to the exception of public order examination, a notable decision on the unification of conflicting judgments was rendered on 10 February 2012 by the Joint Chambers of the Court of Appeals in Turkey, regarding enforcement of judgments that do not contain a detailed reasoning. In this decision, it was stated that the lack of a written justification in a foreign court decision will not prevent the enforcement of such judgment, as the fact that whether or not the judgment contains a detailed justification is not related to public order. It was

[10] Decision of the General Assembly of the Court of Appeals dated 8 February 2012, numbered 2011/13-568 E., 2012/47 K.

further noted that the Turkish court which hears the enforcement lawsuit cannot review the merits of the dispute as it may only take into consideration the conditions in the IPPL. The flexible notion of "public order", often relied on as a ground for refusal of enforcement, is defined in this decision. According to this decision, the violation of "public order" means the violation of fundamental principles of Turkish Law, its moral sentiment, and sense of justice, general policy, fundamental rights and freedoms in the Turkish Constitution, the rules grounded *"bona fide"* principle in private law, the principles of law and the violation of human rights and freedoms. "Public order in national law" means the rules that the parties must respect. The decision of 10 February 2012 emphasizes that enforcement of foreign judgments without reasoning will not be in conflict with Turkish public order and that, therefore, the court hearing the enforcement lawsuit cannot refuse the enforcement only on the grounds that the decision does not contain reasoning. The court may refuse the enforcement only if the award is clearly incompatible with Turkish public order. Therefore, the reasoning of decisions will not have any effect on enforcement of foreign judgments.[11] Although this decision of the Joint Chambers is related to judgments by foreign courts, it is very important in that it reflects the Turkish courts' point of view regarding the enforcement of both foreign court decisions and foreign arbitral awards.

As is in comparative law, an enforcement lawsuit regarding a foreign court decision or arbitral award is a procedural lawsuit and, although the conditions of refusal are explicitly defined in the applicable laws and conventions, "public order" has always been a broadly interpreted condition and often used as a ground for refusal. In the past, the Court of Appeals often referred to public order in enforcement proceedings, broadly interpreting the "public order" concept and even going so far as to examining the merits of the dispute, on the ground that the decision is against public order. The recent decision of the Joint Chambers will hopefully bring an end to this very broad application of the concept of public order and enable the more effective enforcement of foreign courts' judgments and tribunals' awards in Turkey.

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[11] Decision of the Joint Chambers dated 10 February 2012