

FREEDOM OF PRIVATE ENTERPRISE AND INVESTMENT INCENTIVES IN TURKEY

Asis. Dr. Tayfun AKGÜNER (*)

I. This work, as indicated by its title "*Freedom of Private Enterprise and Investment Incentives*", covers both the freedom of private enterprise and measures to encourage investments in the private sector. Falling under Public Law, the study referring to two seemingly dissimilar unrelated topics, will first attempt to determine the Constitutional bases for freedom of private enterprise and then to analyze the investment incentives. I acknowledge that investment incentives limit the freedom of private enterprise. Private enterprises which agree to invest in accordance with the principles outlined in the Five Year Development Plans and the Annual Programs and which thus pass up the opportunity to invest freely as they should choose are rewarded with certain financial benefits by the State. In addition, investment incentives and the system accompanying them acquire meaning only in an economic and legal system wherein private enterprise is found. Therefore, there exists a close relationship between "*freedom of private enterprise*" and "*investment incentives*".

II. The descriptive method is used here. The reason is that the basic law is found and enforced through various and scattered legal acts, ministerial regulations and government circulars.

(*) Dr. Tayfun Akgüner, is an assistant professor at the Institute of Administrative Law and Administrative Sciences of the Istanbul University Law School. This is the English Summary of his doctorate thesis called "*Freedom of Private Enterprise and Investment Incentives*".

III. After determining that Article 40 of the Turkish Constitution provides for freedom of private enterprise, I will look at the limitations placed on this freedom by Paragraphs two and three of the same Article and the relationship of the freedom to Article 41 of the Constitution. I will then review the investment incentives.

IV. Tracing the situation back before the 1961 Constitution, private enterprise during the Ottoman Empire was in the hands of Turks and minorities. European industry, which developed after the sixteenth century, influenced Ottoman Industry. The nineteenth century Commercial Agreement provided that the Ottoman economy would sell raw material and food to developed European economies and would in turn buy manufactured goods from them. It should be emphasized here that until the sixteenth century the Ottoman Empire, along with the Italians, completely controlled trade in the Near East. In 1913, "*the Temporary Law for Encouraging Industry*", aiming at promoting industry, was put into effect. In 1915, there was the "*Industrial Survey*". At that period, private enterprise was financially lacking in technology and organization.

V. From 1923 to 1950, upon the urging of the founder of the Republic, Atatürk, the "*Turkish Economic Congress*" gathered in Izmir. This Congress gave great importance to private enterprise as opposed to public enterprise; however with the World Depression of the 1930's, the Turkish State began to intervene in the economic life. The new politics was called "*State-ism*". The Stateism principle is not a socialist movement; rather it assumes that the State should accomplish what private enterprise can not. This principle was added in 1937 to the 1924 Constitution. At that time, several public institutions came into being and nationalization of enterprise was practiced. In 1934, Turkey drew up its "*First Five-Year Industrial Plan*". The second plan was never put into effect because of the outbreak of the Second World War. In 1945, the "*Third Five - Year Industrial Plan*" was prepared.

VI. In the period between 1950 and 1960, the Democratic Party then in power, under the influence of the "*Marshall Plan*", followed a policy that emphasized private enterprise and agriculture. Investments were made in the areas of electrical energy, irrigation, flood control, highway and railroad construction, and harbor improve

ments. At the same time, there were obvious advances made by the public sector as well. In 1954, the "*Law to Encourage Foreign Investment*" passed. From 1955 to 1960 due to the increased inflation rate, strict price controls and stabilization measures went into effect.

VII. The Constitution prepared by the Constituent Assembly following the Revolution on May 27, 1960 was approved by a public referendum on July 9, 1961. That Constitution known as the "*1961 Constitution*" is the "*Constitution of the Turkish Republic*" still in force.

Article 40 of this Constitution states, "Everyone has the right to work and to enter into contracts in any field. Private enterprises may be freely established.

"Law can limit these freedoms only in the public interest.

"The State shall take measures to ensure that private enterprise complies with national economic needs and social goals and to enable it to function in security and stability."

This Article, which reflects contemporary economic and social views, is far from a "*laissez faire*" policy, demanding instead state intervention. The Turkish Constitution has an economic philosophy based on a "*Mixed Economy*" principle.

The "*everyone*" of Article 40 should be taken to mean everyone possessing and using civil rights. The expression "*in any field*" can be viewed positively or negatively. In the positive sense, it can be understood to refer to a person's right to choose freely the area wherein he wishes to invest. In the negative sense, it can be understood to mean that private enterprise need not handle and can not be forced to handle any specific area. This form of interpretation is a result of the "*indicative*" and "*flexible*" nature of the Turkish Plan application.

Article 40 assures the freedoms to work, enter into contracts and establish private enterprise.

Again it is Article 40 that places limitations on the freedom of private enterprise. Paragraph 2 of Article 40 states, "*Law can limit these freedoms only in the public interest*". Again the third Paragraph

stipulates, "The State shall take measures to ensure that private enterprise complies with national economic needs and social goals and to enable it to function in security and stability". These limitations, like the freedoms they limit, can be divided into positive and negative groups. The positive ones are those which stress that the State will assure that private enterprise can function in security and stability; The negative ones are those that attempt to restrict the activity of private enterprise, to narrow its sphere of activity. The freedom of private enterprise can be limited only by a law passed by the legislature and the limitation should be for the purpose of attaining a public good. The "public interest", in its broad sense, is a concept that changes with the political and ideological understandings of the time and that is revealed in judicial decisions and that is consistent with the political and social principles of the Constitution. The Constitutional Court in numerous decisions has interpreted the "public interest" of Article 40 in the economic life as "economic public interest".

According to Article 11 of the Constitution "basic rights and freedoms can not be altered in their essence even by law". This Article is a general restrictive article for all rights and freedoms in that it states that the essence of basic rights and freedoms is not to be infringed. Outside reasons mentioned in other articles of the Constitution, they can be limited. There are many interpretations of what "the essence of a basic right or freedom" is. I think that for every freedom the essence is different and must be separately determined. Considering freedom of private enterprise, its essence is different from that of the other freedoms. It has the following characteristics:

1. Freedom of private enterprise is a direct outgrowth of the principles of a social state and the rule of law found in Article 2 of the Constitution. For social and economic reasons, it can be restricted by act, but the restriction can not infringe the essence.

2. As there is a natural extension of this freedom to the right of ownership and the freedom to work and enter into contracts, it is also protected by the 1931 Constitution's Article 14 which covers these matters. Even in this respect, the freedom of private enterprise bears a distinctive quality. On the condition that a private entre-

preneur stay within the legal and constitutional limits, even should a specific area of enterprise he had planned to enter be closed by the State, the essence of the freedom would not have been infringed; the same entrepreneur could enter another field that he wanted to, invest his money and use his freedom.

The limitations placed on the freedom of private enterprise by Turkish laws can be categorized in the following ways:

1. *The State Monopoly* : The State, to acquire income, can monopolize certain areas of enterprise where there is public benefit to be accrued by such a legal arrangement. An example is the Tobacco and the Tobacco Monopoly Law.

2. *Social Importance* : Some services and activities because of their social importance are entrusted to the State and therefore closed to private enterprise. For example : The Postal Act.

3. *Intervention of Police Power - Control Mechanism* : Police powers have authority, as specified by law, to limit the freedom of private enterprise. From such intervention, the public benefits and the essence of the freedom is not affected. For example, according to Article 14 of the Police Duties and Authority Act, the police are to prevent any person for any reason from making noise after 12 midnight that would disturb the peace and quiet of the neighborhood.

4. *Permits and Licensing* : The State, by law, can require permits or licences for certain activities of private enterprise or can determine the form that activity is to take; however, limitations on the freedom of private enterprise placed by an administrative act based on administrative discretion, do affect the essence of the freedom.

In limiting this freedom for the sake of public interest, the legislative body has the discretionary power to determine by an Act where the public interest lies.

VIII. The third paragraph of Article 40, (quite separate from the limitations placed on it by the second paragraph) subjects the freedom of private enterprise to a new series of limitations and brings a new obligation to the State. In the third paragraph of the Article; the terms "*national economic needs*" and "*Social goals*" are used.

The limitations in Article 40 have a parallel in Article 41 of the Constitution. Article 41 is entitled "*The Order of Economic and Social Life*" and provides, "*The economic and social life shall be organized so as to ensure the goals of social justice, full employment and a standard of living in keeping with human dignity.*" The Article also shows the State how to accomplish these obligations. The second paragraph of Article 41 stating, "*It is the duty of the State to increase national savings, to direct investments toward priorities that will enhance the public welfare and to draw up development plans so as to promote economic, social and cultural development along democratic lines*", points out the way. "*Social goals*" is clarified by the principle of the "*social state*" in Article 2. According to this article, "*The Republic of Turkey is a national, democratic, secular and social state under the rule of law, based on human rights and the fundamental principles set forth in the Preamble.*"

Another principle of Paragraph 3 of Article 40 is that, "*The State should take positive measures to assure that private enterprise can function in security and stability.*" This principle is an essential provision considering that the Constitution not only accepts private enterprise but financially supports and encourages it, along with the public sector to increase the national development rate. This stability and security principle, as interpreted by judicial decisions, is to ensure that economic acts and regulations shall not be retroactive, shall comply with previously vested rights, shall not controvert the principle of a social state under the rule of law, and shall not be a tool of mere politics.

Political parties, in their platforms regarding the freedom of private enterprise and consequently the economic and social order, have ranged from democratic left or socialist views to those liberal, nationalistic, or national socialistic ones.

IX. The Constitutional basis of investment incentives is the second paragraph of Article 41. As we discussed earlier, the State is given four obligations that are covered in this Article: "*to promote development, to increase national savings, to direct investments, and to prepare development plans.*" The State is to direct investments by democratic means through "*encouragement and support*". In addition, Article 129 of the Constitution providing that "*Economic, so-*

cial and cultural development shall be tied to a plan. The development shall be realized through this plan." — strengthens the provision. In practice, a State Planning Organization was formed by law; and laws have passed concerning the preparation of the Plan, its adoption and application.

X. Law number 933 entitled, *"The Law Concerning the Application of Development Plans"* has played an important role in Turkish Investment Incentives. Certain of its more important provisions were repealed by the Constitutional Court in 1969. Thus today's investment incentives completely rest on annual programs, certain scattered and frequently changed regulations as prepared by the Council of Ministers in accordance With Development Plans.

The *"Decree Concerning the Application, Coordination and Follow-Up of the 1977 Program"* (or, in short, *the 1977 Program*) contains incentives listed in the following order:

1. Incentives related to Investments:

- a. Income tax and corporation tax reductions,
- b. Exemptions from construction tax,
- c. Exemptions from Custom Duties and Fees,
- d. Installments of up to 5 years on Custom Duties and Fees.
- e. Revisions in Tariff Notes and Percentage Rates and of Goods Listed in Custom Tariff Tables,
- f. Loans:
 - aa. Domestic loans :
 - aaa. Reduced Interest on Medium-range loans.
 - bbb. Tax and Service fee exemptions on export-guaranteed investment loans.
 - bb. Special foreign loans.
- g. Investment quotas.

2. Export Incentives :

- a. Refund of export tax,
- b. Exemption from export taxes and fees,
- c. Export on credit,
- d. Special Export Fund,
- e. Allocations for foreign exchange to be used in exporting.

I have covered only investment incentives here.

XI. Investment incentives in Turkey are offered on the merits of the project. For a specific private enterprise to benefit from investment incentives, the enterprise must be included in that year's "*General Incentives Tables*" that are attached to the Yearly Program. However, an enterprise not listed in this table, may apply to benefit from investment incentives. The application is submitted with three copies of a feasibility report to the Ministry of Industry and Technology. The Ministry, having evaluated and approved a project, will issue an "*Incentive Certificate*" to the investor. This Certificate is a preliminary certificate from the Ministry of Industry and Technology stating that the proposed investment, as long as it adheres to the stated stipulations, will be an asset to the national economy and that it complies with development plans and yearly programs in exchange for which the State promises that the investor may benefit from the investment incentives specified on the certificate.

It is not enough simply to obtain an "Incentive Certificate" to benefit from the investment incentives. An investor, with an Incentive Certificate hoping to take advantage of a particular incentive, must also obtain an "*Application Certificate*" bearing the name of the particular incentive. Certain incentives can not be utilized without an Application Certificate. For example, no goods can be taken out of customs by flashing an Incentive Certificate for a custom exemption; an Application Certificate must also be submitted.

The General Directorate of Incentives and Applications in the Ministry of Industry and Technology is responsible for closely following investments that have been granted an Incentive Certificate.

XII. It can be stated that with the adoption of an incentive system, the idea of public service has changed drastically. At first, the State presented itself as a classic liberal state. Later, however, the state undertook a policy whereby the state was encumbered with a whole series of public services, interventive and corrective in nature. This stage is now closed, it seems to me. The state alone can no longer provide the ever-increasing public services required. The private sector must cooperate to achieve some of these public ser-

vices, that is to say that hereafter a "*partnership state*" has emerged wherein the private and public sectors work together. The important thing is that the planned development the Constitution assigned to the State be achieved. This activity is a public service. Whether it be achieved by the State or by private enterprise does not matter if it is implemented in a harmonious fashion. It is sometimes stated that the Plan is imperative for the public sector, indicative for the private sector; however, where the private sector has agreed to act in accordance with the Plan, it is likewise imperative; that is the Plan commits the private sector which agrees to adhere to the goals therein outlined. This means that private enterprise is burdened with effecting public services and implementing them. It is possible to label the actions of private enterprise in advancing the Plan as a "*Public Service Mission*".

XIII. The legal relationship between the State which grants incentives. The State, relying on its public power, has official authority to make executive decisions and to act on its own accord regarding investment incentives. It has the upper hand in dealing with private enterprise. Therefore, the legal relationship between the person receiving the incentives and the State resembles a *public service concession contract* and is a *mixed administrative contract*.

XIV. Along with the discretionary power found in the application of Turkish investment incentives, sometimes restrictive tendencies in this power are conspicuous. This results from the rather different nature of investment incentives. I am not able to determine the general tendencies of the discretionary power of the Turkish Council of State in handling the application of investment incentives. The Turkish Council of State, however, first determines the validity of the factual and legal events on which an administrative act is based and then studies whether the events have enough legal value to require the act. This second step is legal opportunity control to some

extent. The Council of State in some decisions has examined whether investment incentives are in the public interest. In addition, the principle of equality should be applied in granting investment incentives — that is, if two people are in the same situation, it should not happen that one be allowed to benefit from investment incentives and the other not. Again we can find cases where the Council of State has held the administration subject to pay damages resulting both from negligent or non-negligent applications of investment incentives.

XV. Although Turkey is not a full member of the European Economic Community, since the Ankara Treaty signed in 1963, it has been preparing for full membership in 1995. While Article 222 of the Rome Treaty grants member states some rights to organize their own commercial relations, various other sections of the Treaty forbid free competition. In my opinion, if Turkey becomes a full member of LEC, there will no longer be a chance to apply investment incentives or, at least, the application will be made much more difficult.

XVI. That the Turkish regulations covering investment incentives are so scattered makes it very difficult to apply and to follow up on them. Despite the criticisms that might be made of investment incentives, they are a legal reality. For this reason, there is need of an *Incentives Law* that would incorporate all the diverse regulations. The present scattered regulations have a negative effect on the investor and prevent the investment incentives from achieving their aim.