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# Screening of Foreign Investment in the Context of Turkmenistan's FDI (Foreign Direct Investment) Regime

## Türkmenistan Doğrudan Yabancı Yatırım Rejimi Kapsamında Yabancı Yatırımların Taranması

Farruhbek Muminov\* , Alp Emre Varol\*\*

### Abstract

Since the fall of the USSR, Turkmenistan has made some progress in the development of its national economy and its ability to attract foreign investment. Although Turkmenistan is considered an attractive destination due to its rich natural resources, the country's FDI regime, including its admission procedures, lacks transparency and predictability. From the perspective of foreign investors, the host state's FDI regime plays a crucial role. Without considering a host state's FDI regime, foreign investors may be at risk of losing their investment due to lack of transparency or an unpredictable legal environment. Requirements related to the admission of foreign investment may differ between countries. Unlike most countries, which usually limit the scope of admission requirements (national security concerns), Turkmenistan's FDI regime imposes stricter requirements on foreign investors during the entry process. It is understandable that Turkmenistan may expect to maximize the benefit of foreign investment while minimizing its negative effects on the national economy. However, a lack of clear and transparent admission requirements leaves a large amount of discretion with various administrative bodies. This makes admission requirements unpredictable and dissuades foreign investors from investing in the host country. This article scrutinizes the admission requirements related to foreign investment in the entry stage in the Turkmenistan FDI regime.

### Keywords

Foreign investment, Admission requirement, Lack transparency and predictable legal environment

### Öz

Sovyetler Birliği'nin parçalanmasından sonra Türkmenistan'ın ulusal ekonomisinin kalkınması ve yabancı yatırım çekme konusunda belirli bir ilerleme kaydettiği söylenebilir. Her ne kadar Türkmenistan; doğal zenginlikler bakımından zengin ülke konumunda olsa da ülkenin doğrudan yabancı yatırıma ilişkin yasal rejimi özellikle yabancı yatırımların kabulüne ilişkin şartlar şeffaf ve öngörülebilir değildir. Günümüzde birçok ev sahibi ülke yabancı yatırımların kabulünde ancak ulusal güvenlik endişelerinden dolayı kısıtlarken Türkmenistan yabancı yatırımların kabulü aşmasında daha sıkı koşullar getirmektedir. Türkmenistan'ın; yabancı yatırımlardan beklenen yararı maksimize ederken, yatırımların ulusal ekonomi üzerindeki olumsuz etkilerini en aza indirmek istemesi anlaşılabilir bir durumdur. Ancak ev sahibi ülkenin yabancı yatırımların kabulüne ilişkin şartların açık olmaması ve şeffaflıktan yoksun olması yabancı yatırımların kabulünü idari makamların takdir yetkisine bırakmaktadır. Bu durum ev sahibi ülkenin yabancı yatırım kabulüne ilişkin şartlarını öngörülemez hâle getirmekte ve yabancı yatırımcıları ev sahibi ülkeye yatırım yapmaktan caydırabilmektedir. Bu makale Türkmenistan DYY rejimi bağlamında yabancı yatırımların kabulüne ilişkin koşullar incelenmektedir.

### Anahtar Kelimeler

Yabancı yatırım, Yatırımların kabulüne ilişkin şartlar, Şeffaf ve öngörülebilir yasal ortam

\* Correspondence to: Farruhbek Muminov (Ph.D. Candidate), Anadolu University, Faculty of Law, Department of Private Law, Eskişehir, Turkey. E-mail: f.muminov@hotmail.com ORCID: 0000-0002-1559-3879

\*\* Alp Emre Varol (Ph.D. Candidate), Anadolu University, Faculty of Law, Department of Private Law, Eskişehir, Turkey. E-mail: aevarol@gmail.com ORCID: 0000-0002-4306-0607

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## Introduction

It is generally recognized that host countries are better able to attract foreign investment with a combination of investment, technology, and know-how. The race to attract foreign investment pressures host countries to liberalize their foreign investment frameworks. A dramatic process of liberalization has motivated countries to replace the screening and authorization requirements related to the admission of foreign investment with more flexible provisions, including freedom of entry and sectoral exceptions<sup>1</sup>. Currently, most host countries (such as South Korea, Turkey<sup>2</sup>, and Japan) have no admission requirement for foreign investors while a few host countries (Tajikistan, Turkmenistan) impose strict admission requirements because of national security concerns and, environmental and health regulations. In the case of Turkmenistan, Turkmenistan's Foreign Investment Law contains strict admission requirements. According to Article 7 of Turkmenistan's Foreign Investment Law, "*Investment projects with foreign investment shall be subject to mandatory state examination, including the observance of standards of earthquake resistance, fire, explosion, environmental and sanitary requirements*"<sup>3</sup>. The main difficulty with such requirements is a lack of certainty and transparency. Among host countries, the common problem with certainty and transparency in the general legal framework, including bureaucrats and protectionists, is that it will likely be used as a Trojan horse<sup>4</sup> against foreign investors due to uncertainty regarding environmental or other requirements. While high standards do not discourage foreign investors from investing in host countries, uncertainty and frequent changes in regulatory frameworks may

- 1 Giorgio Sacerdoti, 'Admission and Treatment of Foreign Investment Recent Bilateral and Regional Treaties' (2000) 1(1) *The Journal of World Investment and Trade* 106; Sornarajah Muthucumaraswamy, *the International Law on Foreign Investment* (3th edn, Cambridge University Press 2010) 105; Peter Muchlinski, Federico Ortino and Christoph Schreuer, *the Oxford Handbook of International Investment Law* (1th edn, Oxford University Press 2008) 229; Andrew Newcombe and Lluís Paradell 'Law and Practice of Investment Treaties: Standards of Treatment' (Kluwer Law International 2009) 132; Amokura Kawharu, 'The Admission of Foreign Investment under TPP and RCEP', (2015) 16(2) *The Journal of World Investment and Trade*, 1058, 1061; Salacuse Jeswald "BIT by BIT: the Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries" (1990) 24 *The International Lawyer* 3, 666; August Reinisch, *Standards of Investment Protection* (Oxford University Press 2008) 11; Jean-Yves Steyt, 'Comparative Foreign Direct Investment Law: Determinants of the Legal Framework and the Level of Openness and Attractiveness of Host Economy', LLM Graduate Research Paper, 76(2006); OECD, 'Foreign Direct Investment Restriction in OECD Countries' (2015) <<https://www.oecd.org/eco/reform/2956455.pdf>> accessed 4 February 2019; OECD, 'FDI Regulatory Restrictiveness Index'(2018)<[https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX&\\_ga=2.175271777.298301915.1549266976-167128608.1541492600#](https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX&_ga=2.175271777.298301915.1549266976-167128608.1541492600#)> accessed 4 February 2019.
- 2 See in more detail, in accordance with Article 3/a of Turkey's Foreign Direct Investment Law, Law number: 25205; Date of acceptance: 17.06.2003; Article 4/1 of Korea's Foreign Investment Act, Law number: 5559; Date of acceptance: 16.09.1998.
- 3 See also in accordance with Article 4/3 of Law of Turkmenistan on Foreign Concessions "*Concession projects and programs as well as feasibility studies shall be subject to the state expert examination including their environmental, sanitary and hygienic qualifications*", Law of the Republic of Uzbekistan on Foreign Concessions, 1993, No.386-V, *Journal of Majlis of Republic of Turkmenistan*, 1993, No.9-10, Art.54; According to Article 8/1 of Law of Turkmenistan Investment Activities in Turkmenistan "*In cases and orders established by Turkmenistan legislation an investor is obliged to obtain to obtain the results of the State Expertise on investment projects concerning observance of standards and rules of seismic, fire, explosive, sanitary-hygienic, ecological and city-building requirements*". Law of Turkmenistan Investment Activities in Turkmenistan, 1993, No.184-111, *Journal of Majlis of Republic of Turkmenistan*, 1993, No.4, Art.34. It can access all Turkmenistan's legislations <[http://minjust.gov.tj/ru/mmerkezi/doc\\_view.php?doc\\_id=6116](http://minjust.gov.tj/ru/mmerkezi/doc_view.php?doc_id=6116)> accessed 21 November 2019.
- 4 Thomas Waelde and Abba Kolo, 'Environmental Regulation, Investment Protection and "Regulatory Taking" in International Law' (2001) 50(4) *The International and Comparative Law Quarterly* 812.

be problematic<sup>5</sup>. From this point of view, there is no guidance to define admission requirements in the context of Turkmenistan's Foreign Investment Law. On the other hand, it is common practice for host countries to take measures to protect domestic investors and maximize the benefits of foreign investment during the entry of that foreign investment. In the process of state examination, host countries have the opportunity to evaluate potential negative effects that investment projects may have on environmental or public health. At this stage, it is possible to reject an investment project or to accept it on the condition that additional requirements will be fulfilled to minimize the project's negative effects. However, as stated above, the effectiveness of state expertise depends on the certainty and transparency of the guidelines that are regulated throughout the whole process by the state's examination.

The motives of Foreign Direct Investment screening procedures differ among countries (such as control of strategic sectors or granting foreign investment incentives). Most countries often apply screening procedures to control the entry and establishment of foreign investment. These screening procedures may create unnecessary barriers for foreign investors. Generally, a special government authority carries out screening and approval procedures. Foreign investors often complain that such screening procedures and approval processes are highly discretionary, and lack transparency and effective juridical review. There are three primary scenarios for the application of FDI screening procedures. In the first scenario, all foreign investment established in the host country is subject to a screening procedure. In the second scenario, only specific or strategic sectors are subject to a screening procedure. In the third scenario, foreign investment in some host countries (Jordan, Egypt, and Bahrain) is subject to a screening procedure to grant certain investment incentives<sup>6</sup>.

This article scrutinizes the screening grounds at the entry of foreign investors in the context of Turkmenistan's Foreign Investment Law. Part I reviews comparative analyses of the admission of foreign investment in investment laws and recent developments. Part II provides a comprehensive review of the grounds given by state expertise for the entry of foreign investors. Part III examines provisions related to the admission of foreign investment in Turkmenistan BITs. Part IV considers non-discrimination treatments at the stage of entry in light of Turkmenistan's Foreign Investment Law and BITs.

## **I. Comparative Analyses of Admission of Foreign Investment**

It is generally accepted that understanding the restrictions on foreign investment (approval mechanisms, sectoral restrictions, performance requirements, local content

5 Gaetan Verhoose, 'Foreign Direct Investment and Legal Constrains on Domestic Environmental Policies: Striking Reasonable Balance Stability and Change' (1998) 29 *Law and Policy in International Business* 453.

6 OECD, 'Investment Climate and Regulation of International Investment in MENA Countries: Assessment of Available Information and General Recommendations' (2005) 14.

rules, etc.) is crucial to evaluate the attractiveness of a host country. By removing screening procedures, host countries send a positive message to foreign investors. Moreover, the removal of screening procedures is considered an important step toward the liberalization of a host country's national economy<sup>7</sup>.

Many countries, especially developing countries, have introduced special laws to regulate the treatment of foreign investment in their territory. These laws are called investment laws, and they cover domestic and foreign investors. The admission of foreign investment is one of the main provisions of these laws. Most investment laws contain sector-specific limitations (defense, extractive industries, energy, etc.). It is also common for investment laws to include some provisions regarding general safeguards (in the case of, for instance, national security, public order, environmental protection, and public health). However, although these general safeguard requirements of the host country are crucial in the registration and screening procedures for foreign investment, detailed guidelines about them are rarely provided<sup>8</sup>. In this regard host countries have a broad policy space to apply such general safeguards due to their flexibility and uncertainty. Traditionally, there are two models related to the admission of foreign investment in investment treaties. The controlled entry model keeps policy space for host countries to regulate the admission of foreign investment into their territory. From this perspective, foreign investment projects in the context of some host countries' FDI regime are subject to screening and approval by government authorities. In contrast, the full liberalization model contains no requirements for the admission of foreign investment<sup>9</sup>. In the process of massive liberalization, most host countries have removed their foreign investment restrictions, including their screening procedures. For example, Turkey introduced a new Foreign Investment Law in 2003, which changed their process from a screening system to a notification system. Some degree of restriction on foreign investment<sup>10</sup> is common practice in many FDI regimes, with particular focus on both national security and cultural factors<sup>11</sup>. The latest trends in international foreign investment law indicate that host countries have started to be more restrictive of foreign investments, especially with regard to state-owned enterprises (SOEs). There is a fear that, in some cases, foreign investors

7 OECD, 'Foreign Direct Investment and Economic Developments: Lesson from Six Emerging Economies' (1998) 38.

8 UNCTAD, 'Investment Laws: A Widespread Tool for the Promotion and Regulation of Foreign Investment, Investment Policy Monitor' (2016) <[https://unctad.org/en/PublicationsLibrary/webdiaepcb2016d5\\_en.pdf](https://unctad.org/en/PublicationsLibrary/webdiaepcb2016d5_en.pdf)> accessed 10 February 2019.

9 Ignacio Gomez-Palacio and Peter Muchlinski, 'Admission and Establishment' in Peter Muchlinski, Federico Ortino and Christopher Shreuer (eds), *The Oxford Handbook of International Investment Law* (1th edn, OUP 2008)10.

10 UNCTAD, Measuring Restrictions on FDI in Services in Developing Countries and Transition Economies <[https://unctad.org/en/Docs/iteiia20061\\_en.pdf](https://unctad.org/en/Docs/iteiia20061_en.pdf)> accessed 25 February 2019.

Golub Stephen, 'Measuring of Restrictions on Inward Foreign Direct Investment for OECD countries' OECD Economic Department Working Papers <<https://www.oecd.org/eco/reform/2956455.pdf>> accessed 25 February 2019.

11 OECD, 'Freedom of Investment, National Security and Strategic Industries' <<https://www.oecd.org/investment/investment-policy/40473798.pdf>>; OECD, 'Guidelines for Recipient Country Investment Policies Relating to National Security' <<https://www.oecd.org/daf/inv/investment-policy/43384486>> accessed 25 February 2019.

could be controlled directly or indirectly by foreign governments, and thus, used as political tools against the host country. To prevent these cases, most host states take measures to bar certain types of foreign investment. The inevitable consequence of such reviews of foreign investment is a lack of transparency and consistency<sup>12</sup>. Concerns over foreign investment, especially that of state-owned enterprises, often create pressure in host states to adopt laws to restrict foreign investments. Several states (notably Australia, the United States, Japan, Canada, China, and Russia)<sup>13</sup> have already implemented review systems in which foreign investment in areas of critical infrastructure is subject to review. For example, the U.S.'s Committee on Foreign Investment (under the purview of the U.S. Treasury Department) has broad authority over foreign investment in the country and can restrict such investment due to national security<sup>14</sup> or other concerns. Likewise, in 2017, Russia adopted new rules related to restrictions on foreign investments. According to these amendments, the Governmental Commission may demand prior approval of transactions related to any Russian company (not only companies that are considered to be strategic).

## II. Admission of Foreign Investment

### A. Sectoral Restrictions for Foreign Investment

Generally, sector-specific restrictions on foreign investment are the most common although the current trend suggests a significant reduction in formal investment restrictions, which are usually limited to industrial policies. In the case of Korea and Taiwan, it is usually applied to liberal policies in order to attract foreign investment in labor-intensive sectors, whereas technological industries are subject to strict requirements. The investment policy of these countries is to be building local technological capabilities<sup>15</sup>. These restrictions often target transportation, media, and utility sectors due to their political sensitivity<sup>16</sup>. Restrictions on foreign investment are a widely used technique to control foreign investment. These restrictions often take the form of a share of a company's equity capital or the restriction of ownership in certain sectors. It is considered as a sectoral restriction for foreign investment even

12 Justin O'Brien, 'Barriers to Enter: Foreign Direct Investment and the Regulation of Sovereign Wealth Funds' (2008) 42 *The International Lawyer* 1231.

13 See, for more detail, comparative study of restriction of foreign investment regulations: Laura Fraedrich, Chase Kaniecki and Sara Rafferty, 'Foreign Investment Control Heats Up: A Global Survey of Existing Regimes and Potential Significant Changes on the Horizon' (2018) 13 *Global Trade and Customs Journal* 141; Pim Jansen, 'Industrial Policy and in the Context of Merger and Foreign Investment Control' (2018) 24 *Columbia Journal of European Law* 157; Fabio Bassan, 'Host States and Sovereign Wealth Funds' (2010) 5 *EBLR* 165; Jackie Van Der Meulen and Michael J. Trebilcock, 'Canada's Response to Foreign Sovereign Investment: Operationalizing National Security Exceptions' (2009) 47 *Canadian Business Law Review* 392.

14 The Foreign Investment and National Security Act of 2007, (P.L 110-49, 121, Stat 246).

15 Rajneesh Narula and Sanjaya Lall 'Understanding FDI-Assisted Economic Development' (1th edn, Routledge 2006), 261.

16 UNCTAD, 'World Investment Report' (2018) 177 < [https://unctad.org/en/PublicationsLibrary/wir2018\\_en.pdf](https://unctad.org/en/PublicationsLibrary/wir2018_en.pdf) > accessed 26 February 2019.

though statutory state monopoly is not targeted to restrict on foreign investment<sup>17</sup>. From a Central Asian state's perspective, Kazakhstan<sup>18</sup>, Kyrgyzstan<sup>19</sup>, Tajikistan<sup>20</sup>, and Uzbekistan<sup>21</sup> do not apply strict procedures to the admission of foreign investment, while Turkmenistan<sup>22</sup> does. However, it is common practice in Central Asian states to remain absolute or quasi-monopolies in certain economic sectors. In the case of Uzbekistan, for example, the list of state assets that cannot be privatized includes oil transportation, oil production, gas and gas pipelines, the production and transportation of electricity, rail, public mail service, water and sewer servicing, air navigation services, and ports and airports<sup>23</sup>. Similar laws and regulations exist in the legal frameworks of Kazakhstan<sup>24</sup>, Kyrgyzstan<sup>25</sup>, Tajikistan<sup>26</sup>, and Turkmenistan<sup>27</sup>. Although there is no entry barrier for foreign investment in Tajikistan's legal framework, some economic sectors are de facto closed to FDI. Restrictions on formal ownership by foreign investors are not present, apart from the existence of some requirements in the financial sector. However, a lack of transparency in the registration of entities (a single - window system) may be seen as an informal restriction on foreign investors. Tajikistan has no comprehensive plan to abolish the majority of the state monopoly in the foreseeable future<sup>28</sup>.

The case of Turkmenistan shows that some sectors, for example, energy and extraction sectors, are a state monopoly. It is known that the oil and gas extraction sector is more open for foreign investment, whereas the energy sector is strictly

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- 17 OECD, 'Foreign Investment Restriction in OECD Countries' (2004) 2 <[https://www.oecd-ilibrary.org/economics/oecd-economic-outlook-volume-2003-issue-1/foreign-direct-investment-restrictions-in-oecd-countries\\_eco\\_outlook-v2003-1-38-en](https://www.oecd-ilibrary.org/economics/oecd-economic-outlook-volume-2003-issue-1/foreign-direct-investment-restrictions-in-oecd-countries_eco_outlook-v2003-1-38-en)> accessed 26 February 2019.
- 18 Law of the Republic of Kazakhstan on Investment, 08.01.2003, No.373, Journal of Parliament of the Republic of Kazakhstan, 2003, No.14, Art.274.
- 19 Law of the Republic of Kyrgyzstan on Investments in the Kyrgyz Republic, 27.03.2003, No.66, Journal of Jogorku Kenesha of the Republic of Kyrgyzstan, 2003, No.7, Art.252.
- 20 Law of the Republic of Tajikistan on Investments, 12.05.2007, No.260 Mazhlisi Oli of the Republic of Tajikistan Collection of Legislation, 2007, No.5, Art.65.
- 21 Law of the Republic of Uzbekistan on Foreign Investments, 30.04.1998, No.609-I, Journal of Olii Majlis of Republic of Uzbekistan, 1998, No.5-6, Art.91.
- 22 Law of the Republic of Uzbekistan on Foreign Investments, 2008, No.184-111, Journal of Majlis of Republic of Turkmenistan, 2008, No.1, Art.17.
- 23 Law of the Republic of Uzbekistan about Natural Monopolies, 1999, No.9, Journal of Olii Majlis of Republic of Uzbekistan, 1999, No.9, Art.212.
- 24 Law of the Republic of Kazakhstan On Natural Monopolies and Regulated Markets, 1998, No.272-I, Journal of Parliament of the Republic of Kazakhstan, 1998, No.16, Art.214.
- 25 Law of the Republic of Kyrgyzstan about Natural Monopolies in the Kyrgyzstan Republic 2017, No.126, Journal of Jogorku Kenesha of the Republic of Kyrgyzstan, 2011, No.7, Art.1052.
- 26 Law of the Republic of Tajikistan about Natural Monopolies, 2007, No.235, Mazhlisi Oli of the Republic of Tajikistan Collection of Legislation, 2007, No.3, Art.168.
- 27 Turkmenistan does not have a specific law to regulate competition. Fair competition is regulated by Article 17 of the Law on State Support to Small and Medium Enterprises. See: Закон Туркменистана О Государственной Поддержке Малого и Среднего Предпринимательства, 2009, №57-IV, Ведомости Меджлиса Туркменистана, 2009, № 3, ст.59 [Law of the Republic of Turkmenistan on State Support to Small and Medium Enterprises, 2009, No.57, Journal of Majlis of Republic of Turkmenistan, 2009, No.3, Art.59].
- 28 UNCTAD, Investment Policy Review, 6 (2016) (Oct.25, 2018) <[https://unctad.org/en/PublicationsLibrary/diaepcb2016d1\\_en.pdf](https://unctad.org/en/PublicationsLibrary/diaepcb2016d1_en.pdf)> accessed 20 March 2019.



to manage the political, economic, financial, legal, industry, regional, and natural risks that may arise in connection with certain situations. First, it is common to take measures against foreign investment. In this case, those include the Sovereign Wealth Fund or foreign investments that have close connections with foreign countries. However, the transparency and predictability of the Agency is crucial from a foreign investor perspective. The case of Turkmenistan indicates that the Agency for the Protection from Economic Risks has no clear guidelines to follow when analyzing public investment projects. This could dissuade foreign investors from investing in Turkmenistan. Second, after a few foreign investors started investment cases against Turkmenistan that ended up in international investment arbitration, Turkmenistan has started carefully analyzing public investment projects on a case-by-case basis<sup>36</sup>. Most of these investment cases are public investment projects and the foreign investor's claim is based on unlawful expropriation, violation of non-discrimination, delayed payments, and other provisions of Turkmenistan BITs.

### **B. Grounds for Screening Foreign Investment**

Recent developments<sup>37</sup> among developed and developing countries indicate that the scope of national investment screening mechanisms has been expanding. The main reason for such restrictions is to control the planned acquisition of strategic firms, through which foreign investors may take control of critical infrastructure and technologies. Beyond that, these infrastructure and technologies can be seen as crucial for the long-term competitiveness of the national economy<sup>38</sup>.

As a rule in the context of Turkmenistan legislation, state expertise takes place in the process of registering a foreign investment. In this process, the state makes sure that the foreign investment is consistent with the standards and rules of seismic, fire, explosive, sanitary-hygienic, ecological, and city-building requirements. These is only an illustrative list of standards; the state also assesses the social and economic benefits of foreign investment. Most developing countries employ lower health, environment, and safety and labor standards as regulatory incentives<sup>39</sup>. Unlike other developing countries, Turkmenistan imposes high health, safety, and environmental standards for foreign investment during the process of admission. This phenomenon can be explained in two ways. On the one hand, Turkmenistan is more aware of protecting the environment and public interest than other developing nations. Therefore,

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36 Seven out of ten investment cases are requested by Turkish investors. See in more detail, Investment Policy <<https://investmentpolicyhub.unctad.org/ISDS/CountryCases/215?partyRole=2>> accessed 10 May 2019.

37 In particular, recent international investment agreements impose foreign investors for certain requirements related to protection of environment.

38 UNCTAD (n 16) 179.

39 Ibid 110; Sarianna M. Lundan, 'Definitions, Motivations and Locational Determinants of Foreign Direct Investment, Rethinking Investment Incentives: Trends and Policy Options' 56 (Ana Teresa Tavares-Lehmann, Perrine Toledano, Lose Johnson, and Lisa Sachs ed., 2016).

Turkmenistan establishes strict environmental and other standards related to public interest for foreign investment at the point entry. In this regard, Turkmenistan considers the benefits of foreign investment to national economy as well as public interest. On the other hand, there is some doubt regarding Turkmenistan's introduction of these standards for foreign investors in terms of admission. It is not common practice for foreign investors to complain about high environmental standards. Most empirical research indicates that foreign investors do not change their operations to take advantage of lower environmental standards provided by some host countries<sup>40</sup>. One of the main issues related to environmental requirements in the context of national laws is the absence of stability, certainty and transparency. In Turkmenistan, several of the environmental laws and amendments are not accessible to the public. Only some laws and regulations are available via the online newspaper *Turkmenistan: Golden Age*, and such laws are not updated often<sup>41</sup>. The Ministry of Nature Protection (MNP) is the main environmental enforcement authority. Inspectors of five regional departments of MNP scrutinize enterprises and impose sanctions that are in violation of environmental requirements.

The United Nations Economic Commissions for Europe reviewed Turkmenistan's environmental regulations and concluded a lack of consistency and certainty with international standards. According to this review, "Environmental laws contain only brief provisions on administrative, criminal, and civil liability for noncompliance. The assurance of compliance with environmental requirements is based, first of all, on the use of the command-and-control approach, since possibilities for the use of economic incentives for enterprises are very limited. The influence of administrative sanctions on the behavior of polluters (most of which are SoEs) is negligible. During the review mission, it was not possible to comprehend the link between the law enforcement activities of MoNP and decision-making on the allocation of appropriate funding for environmental protection at enterprises that do not comply with environmental requirements. The decision-making in Turkmenistan depends to a large extent on the Government". As can be seen Turkmenistan's environmental regulation is undetectable at the entry of foreign investment. Furthermore, although there are some laws<sup>42</sup> to regulate the registration of foreign investment, they provide no guidelines related to state expertise, including environmental standards. When guidelines are non-existent or very broad, it leaves broad discretion in the hands of the authorities to make evaluations. This phenomenon may compromise the transparency and predictability of

40 OECD, 'Foreign Direct Investment and Environment: An Overview of Literature (1998) 3.

41 United Nations Economic Commissions for Europe, 'Turkmenistan: Environmental Performance Reviews' (2012) 22 < [http://www.unece.org/fileadmin/DAM/env/epr/epr\\_studies/Turkmenistan.pdf](http://www.unece.org/fileadmin/DAM/env/epr/epr_studies/Turkmenistan.pdf) > accessed 20 October 2019.

42 See in more detail, Decree No.8054 (2006) of the president of Turkmenistan "On the Improvement of State Registration of Legal Entities and Investment Projects"; Resolution 5105 (2001) of the President of Turkmenistan "On measures to improve the state registration of legal entities".

state expertise<sup>43</sup>. Because of the non-existence of guidelines related to state expertise, there is no objective criteria for the government officials to follow.

It is common practice in Turkmenistan legislation that Turkmenistan's Foreign Investment Law, as well as other investment regulations, reference "their environmental, sanitary, and hygienic qualifications". These standards provide enough discretion to the authorities to evaluate the activity of foreign investment because of uncertain standards. From this point of view, Turkmenistan's state expertise (their environmental, sanitary, and hygienic standards) includes no precise criteria. Turkmenistan's legal framework for foreign investment is often seen as a complex and diverse set of barriers to the inflow of foreign investment into the country. International experience demonstrates that subjecting specific sectors to screening procedures that are clearly described in national legislation is a better approach than subjecting all foreign investment to the same screening procedures. This approach makes national legislation more predictable for foreign investors. According to this approach, non-listed sectors are not subject to review. The national legislation of host countries often excludes utilities, telecommunications, transportation, and media from their screening procedures<sup>44</sup>. It is generally recognized that all regulatory standards, such as environmental, public health, and labor standards, would positively impact a host country's income level. These standards also create policy space for host countries to regulate these matters and balance the interests of foreign investors with those of the host country. However, it should be noted that small countries could be in a weaker position to negotiate with large companies and large neighboring countries. As previously mentioned, the regulatory standards of a host country are not the main concern of foreign investors. The main concern is the predictability of a host country's legal framework. The predictability of a host country's current and future regulatory framework could decrease uncertainty and increase the attractiveness of investment<sup>45</sup>.

The foreign investor expects the host country to behave in a transparent and consistent manner without uncertainty. The fact that the legislation is foreseeable ensures that foreign investors comply with the legislation by planning their investments in advance. The inability of the host country to comply with its own manner of conduct with respect to foreign investors or investments and to the extent that it cannot provide protection to the extent that the country undertakes the investment agreements affects the ability of the foreign investor<sup>46</sup>. On the other hand, the principle of stability and predictability should not be interpreted as the fact that foreign investment legislation

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43 OECD, 'Transparency and Predictability for Investment Policies Addressing National Security Concerns: A Survey of Practices' (2008) 3 < <https://www.oecd.org/daf/inv/investment-policy/40700254.pdf> > accessed 2 November 2019.

44 UNCTAD (n 16)180.

45 OECD, 'Regulatory investment incentives' < <https://pdfs.semanticscholar.org/767d/afb28173d00395740bf7b9910b09ec7214ba.pdf> > accessed 10 May 2019.

46 *Tecnicas Medioambientales Tecmed S.A v. Mexican*, ICSID Case No: ARB/00/02, Award, para. 154.

and investment agreements can never be changed. In other words, states can often change their laws and regulations by using their own regulatory powers, taking into account the changing economic conditions or developments in the political, economic, and social fields. These changes may lead to less profitable and even unprofitable activities in certain cases<sup>47</sup>.

### **C. Do Turkmenistan's Bits Contain Any Special Provisions Related to the Admission of Foreign Investment?**

Traditionally, there is consensus that the state has the full right to allow foreign investors to enter its territory. However, over the past two decades, several countries have liberalized their investment climate and abolished entry barriers for foreign investment. Without a doubt, open and transparent admission rules for the entry of foreign investment is a crucial contributor to the inflow of foreign investment into a host country. From the point of view of the predictability and stability of a host country's investment framework, investment treaties create more secure, transparent, and predictable environments for foreign investors at the international level. Simultaneously, host countries preserve certain rights to control the entry of foreign investment to protect national and public interests (security, national economic policy, public health, and environment)<sup>48</sup>. For that reason, host countries often maintain certain provisions to create space for regulatory policy.

Generally speaking, based on the controlled entry model, a host country's BIT often includes an admission clause. In the scope of such clause, the host country has no obligation to revise its domestic legislation or preserve regulatory power during the pre-entry stage<sup>49</sup>. It should be noted that strict admission rules dissuade foreign investors from investing in host countries. In this sense, pre-established commitments could be considered a strong message to potential investors while limiting the regulatory power of a host country to admit foreign investment in its territory. Nearly all of Turkmenistan's BITs contain special provisions related to the admission of foreign investment. For example, Article 2 of the Turkmenistan-India BIT states "This agreement shall apply to all investments made by investors of either Contracting Party in the territory of the other Contracting Party, accepted as such in accordance with its laws and regulations, whether made before or after coming into the force of this Agreement". Although the language of such provisions ("admit"<sup>50</sup>, "permit"<sup>51</sup>) in the context of Turkmenistan's BIT is different, all provisions related to admission make reference to national laws. In this regard, such provisions play a role

47 Feldman v. Mexico, ICSID Case No.ARB/99/1, para 112.

48 WTO, 'Concept paper on modalities of pre-establishment, Working Group on Relationship Trade and Investment' (2002) 3.

49 Shan Wenhua, 'The Legal Protection of Foreign Investment: A Comparative Study' (Hart Publishing 2012) 30.

50 Article 2/1 of Turkmenistan-UAE BIT.

51 Article 2/1 of Turkmenistan-Uzbekistan BIT.

at two levels<sup>52</sup>. First, these provisions allow the host country to apply its admission and screening procedure in the scope of national legislation. In the case of Turkmenistan, admission and screening procedures are carried out through state expertise. In this process, Turkmenistan evaluates the consistency of foreign investment projects with general safeguard standards (environmental, sanitary, and hygienic qualification), as well as the contribution of foreign investment to the national economy. Second, these provisions allow Turkmenistan to apply discriminatory provisions to foreign investors in the context of national legislation at the entry stage. In other words, it is not possible to apply national treatment and a most favored nation clause at the stage of entry.

Principally, BITs and FTAs contain no special provisions in case the host country may have strong regulatory powers (environment and public health)<sup>53</sup>. It is not common in practice that environmental provisions do not constitute a breach of BIT. Compared with the main provisions of BIT (such as national treatment, most favored nation treatment, fair and equitable treatment), these provisions have often seen soft law in the context of IIA. Albeit international investment arbitration practice illustrates that violation of environmental provisions considers in light of general objectives and its content<sup>54</sup>. Several countries (the U.S. Model BIT 2012 and Canadian Model BIT) in recent years have started to introduce environmental and public health provisions in their national legislation as well as their BITs. Some of these provisions are symbolic rather than mandatory, while others impose certain social standards (environmental and public health standards) for foreign investors.

#### **D. Admission of Foreign Investment and “In Accordance with Host State Law”**

As previously noted, several Turkmenistan BITs require foreign investors to establish their investment in accordance with the law<sup>55</sup>. In these examples, “in accordance with host state law” constrains foreign investors to establish their investments in the scope of Turkmenistan law. In this regard, the admission of foreign investment provisions refers to a host country’s legislation. It means that foreign investors are not protected under the BIT if that foreign investor fails to admit in accordance with the host country’s law<sup>56</sup>.

52 Gomez-Palacio and Muchlinski (n 9) 11.

53 Daniel Chudnovsky ‘*Rethinking foreign investment for sustainable development: Lesson from Latin America*’, (Anthem Press 2010), 132.

54 Hoi L.Kong and L. Kinvin Wroth ‘NAFTA and Sustainable Development: History, Experience and Prospects for Reform’(Cambridge University Press 2015); Ralph Tench, William Sun and Brian Jones ‘Communicating Corporate Social Responsibility: Perspective and Practice’ (Emerald 2014), 144.

55 Article 2/1 of Turkmenistan – Switzerland BIT; Article 3/1 of Turkmenistan – India BIT; Article 2/1 of Turkmenistan – United Arab Emirates BIT; Article 2/1 of Turkmenistan – Uzbekistan; Article 2/1 of Turkmenistan – Israel.

56 See in more detail: August Reinisch ‘How to Distinguish ‘In Accordance with Host State Law’ Clauses From Similar International Investment Agreement Provisions?’ (2018) 7 Indian Journal of Arbitration Law 1, 70-83; Sam Luttrell ‘Fall of the Phoenix: New Approach Illegality Objections in Investment Treaty Arbitration’ (2018) 44 University of Western Australia Law Review 2, 121-141; Jarrod Hepburn ‘In Accordance with Which Host State Laws? Restoring the “Defense” of Investor Illegality in Investment Arbitration’ (2014) 5 Journal of International Dispute Settlement 531, 1-25; Rahim Moloo and Alex Khachaturian ‘the Compliance with the Law Requirement in International Investment Law’ (2011) 34 Fordham International Law Journal 6, 1473- 1499.

As the tribunal explained “in accordance with host state law” in this way: “*The only logical and legal sense to support the literal and teleological interpretation of the expression “in accordance with its legislation (legal provisions)” is to refer to the reservation by the Host State of the investment of its sovereignty, within the scope of the regulation of the conditions for admission of an investment made by the other contracting State, as well as regulation of its protection. Thus, a State can limit its discretion the type of investment admissible through its internal laws (for example, in the case of investments in sectors subject to State monopoly), without violating the BIT and establish freely its own internal rules suitable to protect foreign investments. These are measures of an economic nature rather than clauses limiting the consent of the Host State to the jurisdiction of the ICSID*”<sup>57</sup>.

In *Churchill Mining v. Indonesia*, the tribunal defined admission requirements as a jurisdictional issue. The tribunal explained that admission requirements are applied at the time of the entry to the host country and not during the entry of the investment project. Furthermore, the tribunal clarified the scope of “in accordance with host state law”. The tribunal noted that admission requirements in BITs are narrower than traditional legality requirements which it only limited to domestic law and not the general legal framework of the host country. In contrast, investor-state arbitration awards related to admission requirements and “in accordance with host state law” are not consistent. The tribunal in *Mytilineos Holdings SA v. Serbia* found that foreign investment requires an additional approval procedure in accordance with the 1987 ASEAN Agreement even though the BIT did not contain special provisions related to admission. The tribunal said: “*The BIT itself does not require registration of investments; rather, it covers investments made “in accordance with/consistent with the legislation of the host State”*”<sup>58</sup>. The tribunal in *Tokios Tokenles v. Ukraine*<sup>59</sup> adopted a similar approach. According to Ukraine, there were some irregularities in the foreign investor’s’ business and in some documents related to the business registration under Ukrainian law. The tribunal pointed out that foreign investor activity was within the scope of investment under the BIT, and such investment is not illegal under the law of the host state. The tribunal further suggested that minor registration irregularities are acceptable as long as they are considered as legal investment<sup>60</sup>.

As seen in the above cases, “in accordance with host state law” does not refer to the admission of foreign investment under the host country’s law. This provision is only required for the foreign investor to be legal in the scope of the host’s state law. Unlike such provisions, most of Turkmenistan’s BITs contain clear provisions related

57 *Inceysa Vallisoletana S.L v. Republic of El Salvador*, ICSID Case No: ARB/03/26, Award, para.199.

58 *Mytilineos Holdings SA v. The State Union of Serbia & Montenegro and Republic of Serbia*, PCA, Partly Award on Jurisdiction, para.140.

59 *Tokios Tokenles v. Ukraine*, ICSID Case No. ARB/02/18.

60 *Tokios Tokenles v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction, para 74-76.

to admission. In this sense, once foreign investment is approved by Turkmenistan law, the foreign investor is protected within the scope of the BIT.

### **E. Applicability of Non-Discrimination Clause**

The non-discrimination clause is the cornerstone of international investment treaties. In this sense, international investment treaties and national investment legislation often contain national treatment and most-favored nations clauses. National treatment prohibits discrimination between foreign investors and domestic investors, whereas a most-favored nation clause provides a non-discrimination clause among foreign investors and third party investors.

From the point of view of the host country, application of a non-discrimination clause in the pre-entry stage of investment could be problematic<sup>61</sup>. First and foremost, as mentioned before in the case of Turkmenistan, the host country may have closed certain sectors to foreign investment due to concerns of strategic and political reasons. Another problem with application of a non-discrimination clause is that several developing countries provide certain preferences to domestic investors. The main reason is that host countries get worried about domestic investors who have a low chance to compete with foreign investors. In this case, it is easier for the host country to access a most favored nation clause on the entry of foreign investment rather than national treatment.

Generally speaking, international investment treaties regulate and provide protection for foreign investors after the establishment of the investment, although, some investment treaties provide protection beyond the levels of traditional protection of foreign investment and contain non-discrimination clauses for pre-entry investment. This clause requires that the host state does not discriminate against foreign investors in case of permits, licenses, authorization, and other formalities in the context of the host country's legislation. In other words, in the stages of making, acquiring, and expanding their investments, foreign investors are subject to the same applications as domestic investors as well as third-party investors.

In Central Asian states<sup>62</sup> including Turkmenistan foreign direct investment heavily concentrates in just few sectors, in particular natural resource extraction. International experience as well as recent developments indicate that natural resource extraction sectors are open to discriminatory measurements or predatory interference of the host country<sup>63</sup>. For Turkmenistan, prospective poor-quality regulations, as well

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61 Salacuse (n 1) 667.

62 The OECD Central Asia Initiative, Promoting Investments and Job Creation in Central Asia through Business Linkage Programs, 14 (2013) <<https://www.oecd.org/global-relations/BusinessLinkageProgrammes.pdf>> accessed October 20, 2018.

63 Skovgaard Poulsen, *The Importance of BITs for Foreign Direct Investment and Political Risk Insurance: Revisiting Evidence*, Yearbook on International Investment Law and Policy 2009/2010 (Oxford University Press 2010), 547.

as inconsistent interpretation and arbitrary application of laws, continue to be a major problem for the Turkmenistan foreign investment regime. The scope of a non-discrimination clause is often restricted in the process of admission in all of Turkmenistan's BITs. Although the language of non-discrimination varies, all of Turkmenistan's BITs restrict the scope of non-discrimination in accordance with the host country. For example, Article 4/2 of the Turkmenistan-Swiss Federal Council BIT (2008) states, "...*Treatment of investors themselves as regards the management, maintenance, use, enjoyment or disposal of their investments, shall also be not less favorable than that accorded by a Contracting Party to its own investors or to investors of any third State.*" Some of Turkmenistan's BITs reference the scope of the non-discrimination clause that can be applicable once investment is established in accordance with the host state. For example, Article 2/2 of the Turkmenistan-Turkey BIT states "*Each party shall accord to these investments, once established, treatment no less favorable than that accord in similar situations investments of its investors or to investments of investors of any third country, whichever is the most favorable*". In contrast, a recent survey shows that nearly 88 % of PTAs (Preferential Trade Agreements) contain national treatment in the pre-establishment phase of investment. This provision imposes on the host country to remove all discriminatory market access measurements and treat foreign investors the same as domestic investors<sup>64</sup>.

In light of all of Turkmenistan's BITs, a non-discrimination clause in the pre-entry stage is not applicable. That means that foreign investors could be discriminated against in the process of entry. Restricting the scope of a non-discrimination clause not only covers national treatment but also most-favored nation clauses. In this sense, discrimination can occur among different states' investors.

### Conclusion

The admission of foreign investment is a crucial part of a host country's FDI regime. Clear and predictable procedures regarding the entry of foreign investment make for more favorable destinations for foreign investors. In this sense, foreign investors plan their investments based on host countries' legislation. In contrast, a lack of rules and procedures related to admission may negatively affect the inflow of foreign investment into a host country. It is generally accepted that high standards related to the protection of environmental and public health rules is not the main concern of foreign investors. The main concern is a lack of predictability and transparency in a host country's legal framework. In particular, this issue is more problematic in developing countries due to a lack of the rule of law. It is not acceptable for host countries to employ uncertain laws as a shield against foreign investors in case of disputes between a host state and a foreign investor.

64 Jo-Ann Crawford and Barbara Kotschwar "Investment Provisions in Preferential Trade Agreements: Evolution and current Trends, WTO: Economic Research and Statistics Division, ERSD 2018-14, 17.

Turkmenistan's FDI regime is often defined by a lack of transparency and predictable rules for foreign investors, including admission rules. It seems that it is difficult for Turkmenistan to attract massive amounts of foreign investment due to the country's lack of a predictable and transparent FDI regime. Furthermore, all of Turkmenistan's BITs include provisions that grant Turkmenistan the right to control the admission of foreign investment. That means that foreign investment is accepted in accordance with Turkmenistan legislation. Turkmenistan Investment Law contains special provisions to allow the application of state expertise at the point of entry of foreign investment. In other words, these provisions allow Turkmenistan to scrutinize foreign investment case by case at the entry stage. However, there are no guidelines or principles to follow in the process of applying state expertise. In the eyes of foreign investors, this makes state expertise lack transparency and predictability. In this case, Turkmenistan's application of state expertise gives the impression that Turkmenistan uses state expertise to choose foreign investors rather than to protect environmental and public health.

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