

## ‘The Stabilization Clause’ of The Baku-Tbilisi-Ceyhan Pipeline Agreements: A Legal Review

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Article Info	ABSTRACT
<p><b>Article History</b></p> <p><b>Received: 31.05.2022</b> <b>Accepted: 30.08.2022</b> <b>Published: 02.09.2022</b></p> <p><b>Keywords:</b> Stabilization Clause, Foreign Direct Investment, International Investment Contract, Baku-Tbilisi-Ceyhan (BTC) Pipeline Agreement, Pipeline Investment.</p>	<p>International investment contracts usually involve stabilization clauses that are prevalently used in infrastructure, telecommunication, and energy sectors, especially in the oil and gas extraction industries. In the petroleum industry, foreign investors providing advanced technology and substantial financial capital for oil development often face political risks in developing countries such as expropriation of pipeline investments, increased taxes, and other fees for projects throughout the contractual performance. These stabilization provisions disincentive host states from enacting new laws or enhancing their laws and regulations on environmental, public health, labor, and human rights standards. The stabilization clause of the Baku-Tbilisi-Ceyhan (BTC) Pipeline Agreement was criticized as a great obstacle to Turkey’s regulatory ability to enhance environmental, health, labor, and human rights standards. Indeed, the BTC’s stabilization clause neutralizes Turkey’s laws and regulations for forty years. This paper proposes some important legal tools to alleviate these concerns over stabilization clauses in pipeline investment contracts.</p>

### Bakü-Tiflis-Ceyhan Boru Hattı Projesi Kapsamında İmzalanan Anlaşmalardaki ‘İstikrar Şartı’: Hukuki Bir Değerlendirme

Makale Bilgileri	ÖZ
<p><b>Makale Geçmişi</b></p> <p><b>Geliş: 31.05.2022</b> <b>Kabul: 30.08.2022</b> <b>Yayın: 02.09.2022</b></p> <p><b>Anahtar Kelimeler:</b> İstikrar Şartı, Doğrudan Yabancı Yatırım, Uluslararası Yatırım Sözleşmesi, Bakü- Tiflis-Ceyhan (BTC) Boru Hattı Anlaşması, Boru Hattı Yatırımı.</p>	<p>Uluslararası yatırım sözleşmeleri genellikle altyapı, telekomünikasyon ve enerji sektörlerinde, özellikle petrol ve gaz arama/çıkarma endüstrilerinde yaygın olarak kullanılan ‘istikrar şartı’ nı içerir. Petrol endüstrisinde, petrol geliştirme için ileri teknoloji ve önemli finansal sermaye sağlayan yabancı yatırımcılar, gelişmekte olan ülkelerde boru hattı yatırımlarının kamulaştırılması, artan vergiler ve sözleşmenin ifası boyunca projeler için gündeme gelen diğer ücretler gibi siyasi risklerle karşı karşıya kalmaktadır. İstikrar şartı, yatırıma ev sahibi devletleri çevre, halk sağlığı, çalışma ve insan hakları standartları ile ilgili yeni yasalar çıkarmaktan veya yasalarını ve regülasyon temelli düzenlemelerini geliştirmekten alıkoyar. Bakü-Tiflis-Ceyhan (BTC) Boru Hattı Anlaşması'nda yer alan istikrar şartı; Türkiye'nin çevre, sağlık, çalışma ve insan hakları standartlarının iyileştirilmesine ilişkin düzenleyici işlemler yapabilmesine engel teşkil ettiği için eleştirildi. Hakikaten de BTC'deki istikrar şartı, Türkiye'nin idare hukukunu ve regülasyon hukuku temelli düzenlemelerini kırk yıl sürecek şekilde etkisiz hale getirmektedir. Bu çalışma, boru hattı yatırım sözleşmesinde yer alan istikrar şartına ilişkin bu endişeleri hafifletmek için bazı önemli hukuki enstrümanlar önermektedir.</p>

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## INTRODUCTION

BTC pipeline project that has been carrying Caspian oil across Azerbaijan, Georgia, and Turkey to the Mediterranean Sea since 2006 was one of the most outstanding investments of British Petroleum (BP) in Central Asia.<sup>1</sup> This mega project was arranged financially<sup>2</sup> and has been operated by the BTC Consortium, which consists of nine corporations, which are called MEP Participants. BP has been conducting the design and construction phases as the largest stakeholder since the project was commenced.<sup>3</sup>

Turkey, unique geography providing a bridge between Europe and Asia, rested two main goals of the BTC pipeline project. The first goal is to eliminate the risk of danger in the Istanbul Strait that was being overused by heavy oil tankers. Possible accidents in the Istanbul Strait would harm not only approximately eighteen million people’s physical security but also Istanbul’s unique environmental heritage as well.<sup>4</sup> The second goal was that Turkey desired the infusion of Caspian natural gas into the Turkish national energy market whilst Turkey would benefit from the lucrative Western market to decrease dependence on Russia.<sup>5</sup> As a result of these goals of Turkey and BP in the so-called region – Turkey, Georgia and Azerbaijan signed the BTC pipeline agreement in Istanbul on November 18, 1999.<sup>6</sup> The legal structure of the agreement was based on the “Intergovernmental Agreement (IGA) among Turkey, Azerbaijan, and Georgia” that also supervised three Annexes: “Host Government Agreement (HGA),” “The Turnkey Agreement,” and “The Government Guarantee.”<sup>7</sup>

This complex legal structure of the BTC pipeline project is undoubtedly associated with some significant legal problems. In particular, the important principles of Turkish laws and regulations, have been diminished since the project commenced to be operated. This paper discusses how the BTC pipeline project’s legal structure on the IGA and HGA between Turkey and the BTC Consortium trumps the applicable Turkish national legislation enacted on behalf of the BTC Consortium.

The second section describes the significant clauses that pertain to both the IGA and the HGA respectively. The BTC pipeline agreement emphasized that both the IGA and HGA cannot

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<sup>1</sup> Robert, Peachey. “Petroleum Investment Contracts after the Baku-Tbilisi-Ceyhan (BTC) Pipeline”, *Northwestern International Law & Business*, Vol. 31, No. 3, 2011, pp. 739-740.

<sup>2</sup> British Petrol. *Baku-Tbilisi-Ceyhan (BTC) Pipeline*, [http://www.bp.com/en\\_ge/bp-georgia/about-bp/bp-in-georgia/baku-tbilisi-ceyhan-btc-pipeline.html](http://www.bp.com/en_ge/bp-georgia/about-bp/bp-in-georgia/baku-tbilisi-ceyhan-btc-pipeline.html), Accessed 1 May 2022.

<sup>3</sup> Amnesty International, *Human Rights on the line Baku Tbilisi Ceyhan Pipeline Project*, 2003, [http://bankwatch.org/documents/report\\_btc\\_hrighs\\_amnesty\\_05\\_03.pdf](http://bankwatch.org/documents/report_btc_hrighs_amnesty_05_03.pdf), Accessed 1 May 22. Peachey, p. 741, Starr, S. Frederick and Cornel, Svante E. *The Baku-Tbilisi-Ceyhan Pipeline: Oil Window to the West*, 2005 Central Asia-Caucasus Institute Silk Road Studies Program, p. 106, [https://www.silkroadstudies.org/resources/pdf/Monographs/2005\\_01\\_MONO\\_Starr-Cornell\\_BTC-Pipeline.pdf](https://www.silkroadstudies.org/resources/pdf/Monographs/2005_01_MONO_Starr-Cornell_BTC-Pipeline.pdf), Accessed 01 May 22.

<sup>4</sup> Starr, S. Frederick and Cornel, Svante E. Cornel, p. 105-106.

<sup>5</sup> Peachey, p.750.

<sup>6</sup> BAKU-TBILISI-CEYHAN COPL PROJECT DIRECTORATE, <http://www.btc.com.tr/eng/project.html>, Accessed 22 April 22.

<sup>7</sup> *Id.*

be interpreted as an international private concession contract. The IGA including the HGA as its appendix was an intergovernmental treaty under international law. Furthermore, the IGA created the agreement’s prevailing legal regime that afterward was used to illustrate the stabilization clause in the HGA. The third section begins by explaining the stabilization clauses’ legal status under international customary law. Secondly, it examines the stabilization clause of the HGA agreement between Turkey and the BTC Consortium. Stabilization clauses as very significant protection to foreign investors are used to avoid or decrease the political risks related to multinational projects in international investment agreements.<sup>8</sup> The fourth section consists of a summary of proposals for those complex contractual relationships and prospective pipeline agreements as well. Turkey proposes to enhance its role as a reliable energy transfer country whilst Turkey had harmonized its domestic legislation with the European Union (EU) directives as a candidate country of EU for years.<sup>9</sup> In addition, Turkey ought to improve its national environmental law and regulations to mitigate greenhouse gas emissions because of the ratification of the Paris Agreement on 11 October 2021.<sup>10</sup> Therefore, the BTC pipeline agreements should be evaluated very carefully to meet those three goals’ requirements in the future. Finally, this paper concludes by highlighting the effects of this multifaceted legal framework of the BTC legal agreements.

## I. BACKGROUND

The BTC pipeline is 1768 kilometers in total length and transports oil from the Azeri-Chirag-Deepwater Gunashli (ACG) field and across Azerbaijan, Georgia, and Turkey.<sup>11</sup> The pipeline pumped the planned volume of petrol across the channel at the beginning of June 2006 and has transported approximately 2 billion barrels of oil from the Caspian Region to the Ceyhan terminal in Turkey for nine years.<sup>12</sup> As a result of that, not only did BP enjoy this well-design investment opportunity<sup>13</sup> but also did Turkey declare to earn twelve billion dollars from the BTC pipeline investment in March 2014.<sup>14</sup> This section of this paper explains some specific clauses firstly on the IGA, and secondly on the HGA of the BTC oil pipeline agreement.

<sup>8</sup> Westlaw Practical Law. *Stabilization Clause*, <http://us.practicallaw.com/1-501-6477>. Accessed 05 May 22. See also Potesta, Michele. “Legitimate Expectations in Investment Treaty Law: Understanding the Roots and Limits of a Controversial Concept”, *ICSID Review*, Vol: 28, No: 1, 2013, pp. 88-122. Fauchald, Ole Kristian. “International Investment Law and Environmental Protection”, *Yearbook of International Environmental Law*, Vol: 17, No: 1, 2007, pp. 27-29.

<sup>9</sup> REPUBLIC OF TURKEY MINISTRY OF FOREIGN AFFAIRS. *Turkey’s Energy Strategy*, <http://www.mfa.gov.tr/turkeys-energy-strategy.en.mfa>. Accessed 07 May 22.

<sup>10</sup> “The Paris Agreement was adopted on 12 December 2015 at the twenty-first session of the Conference of the Parties to the United Nations Framework Convention on Climate Change.” See United Nations Treaty Collection, [https://treaties.un.org/Pages/ViewDetails.aspx?src=IND&mtdsg\\_no=XXVII-7-d&chapter=27&clang=en](https://treaties.un.org/Pages/ViewDetails.aspx?src=IND&mtdsg_no=XXVII-7-d&chapter=27&clang=en), Accessed 05 May 2022.

<sup>11</sup> British Petrol. *Baku-Tbilisi-Ceyhan Pipeline*.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> HURRIYET DAILY NEWS. *Turkey Earns 12 Billion \$ from Baku Pipeline*, 2014, <http://www.hurriyetdailynews.com/turkey-earns-12-billion-from-baku-pipeline.aspx?pageID=238&nID=64023&NewsCatID=348>. Accessed 07 May 22. Reyes, S. Abigail. “Protecting the

## A. IGA of the BTC Pipeline Agreements

The method of using an intergovernmental treaty in the petroleum industry has been observed in the last decade for giant cross-border projects.<sup>15</sup> For the mega-development projects, the BTC consortium has been taking advantage of an intergovernmental treaty to be positive about the principle of freedom of transit of petroleum.<sup>16</sup> The Turkish scholar Sedat Çal emphasizes that the agreement among Georgia, Azerbaijani, and Turkey was also valid for the Turkish domestic law since the parties of IGA exercised their sovereign power to be binding with a treaty under international law.<sup>17</sup>

The IGA of the BTC project contains eleven articles in which specific details purport to protect the BTC Consortium unilaterally with the benefit of a tremendous variety of rights.<sup>18</sup> Article 2(1) of IGA<sup>19</sup>, the most considerable provision of this treaty, creates the project's prevailing legal system. Turkey also guaranteed that the treaty would be adopted into Turkish legislation under the Turkish Constitution within the shortest time frame as a binding obligation under international law.<sup>20</sup> The Turkish Government guaranteed the enactment of a Turkish domestic statute to make the IGA of the BTC applicable to the Turkish legal regime.<sup>21</sup> Thus, first, the Turkish National Grand Assembly ratified the agreement package on June 22, 2000.<sup>22</sup> Secondly, upon publication in Turkey's Official Gazette on 10th September 2000 (No. 24166), the IGA for Turkey was now part of the Turkish legislation system.<sup>23</sup>

Immediately after the prevailing legal regime provisions, under Article 2.2<sup>24</sup>, Turkey approved the attached appendices of IGA which are the between and among Turkey and the Project Investors (attached as Appendix 2), the Turnkey Agreement between and among the turnkey contractor, and the Project Investors (attached as Appendix 3), the Government Guaranty as a contract by which Turkey guarantees the payment and performance obligations of the turnkey contractor under the Turnkey Agreement (attached hereto as Appendix 4), and the HGA between

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Freedom of Transit of Petroleum: Transnational Lawyers Making (up) International Law in the Caspian" *Berkeley Journal of International Law*, Vol. 24, No.3, 2006, pp. 842-844.

<sup>15</sup> Reyes, p. 845.

<sup>16</sup> *Id.* p. 844.

<sup>17</sup> Çal, Sedat. "Bakü-Tiflis-Ceyhan Boru Hattı Projesi Kapsamındaki Anlaşmaların Hukuki Yönden Değerlendirilmesi" *Ankara Üniversitesi Sosyal Bilimler Dergisi*, Vol. 63, No. 4, 2008, pp. 90-95.

<sup>18</sup> *Id.* pp. 96-97

<sup>19</sup> The Transportation of Petroleum Via the Territories of The Azerbaijan Republic, Georgia and The Republic of Turkey Through the Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement, Turkey-Azerbaijani-Georgia, (18.11.1999), [http://www.bp.com/content/dam/bp-country/en\\_az/pdf/legalagreements/BTC\\_eng\\_agmt4\\_agmt4.pdf](http://www.bp.com/content/dam/bp-country/en_az/pdf/legalagreements/BTC_eng_agmt4_agmt4.pdf). Accessed 01 May 22. (*The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999))

<sup>20</sup> Çal, p. 97.

<sup>21</sup> *Id.*

<sup>22</sup> BAKU-TBILISI-CEYHAN COPL PROJECT DIRECTORATE.

<sup>23</sup> The Corner House. *Issues Arising From Legal Regime For BTC Project*, 2003, <http://www.thecornerhouse.org.uk/sites/thecornerhouse.org.uk/files/Chapter%20%20-%20LEGAL%20REGIME-1.pdf>. Accessed 22 April 22.

<sup>24</sup> *The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999)

and among the Azerbaijan Republic and the Project Investors (attached as Appendix 5) as being part of the treaty.<sup>25</sup>

Within this context, BP took advantage of the treaty that not only trumps all the Turkish domestic legislation but also was unlikely to be modified by a new Turkish Government in case of any political instability since BP had already learned its lessons not to use an international private concession agreement in Iran.<sup>26</sup> That’s how the Turkish administrative law and principles were frozen to protect the interests of BP. On the other hand, the concept of using the HGA as a part of the treaty was criticized since not only did the HGA’s provisions connote a typical international private concession agreement<sup>27</sup>, but also that concept was against the sovereignty of the Turkish state under international customary law and the Turkish domestic law.<sup>28</sup>

The power of the BTC legal agreement’s prevailing legal regime was expounded under Article 2. 7 in depth.<sup>29</sup> According to this sweeping clause, “Turkey warrants to Azerbaijan and Georgia that it is not subject to any regional or international treaty or domestic law that conflicts with the implementation of or value of the pipeline project.”<sup>30</sup> The conspicuous point of this clause is that the BTC consortium lawyer reminded the parties of IGA that the HGA and Project Agreements were somehow part of this IGA.<sup>31</sup> On the other hand, this approach does not neatly comport with the Turkish Constitutional Court’s rulings, since the BTC legal agreements were adopted into the Turkish legal system as statutes. As long as the specific statutes of BTC do not include international fundamental rights and freedoms under Article 90 of the Turkish Constitution, the Turkish government has the sovereign power to enact a new regime that may prevail over the previous BTC domestic statutes.<sup>32</sup>

According to another unequivocal provision of the IGA, Article 2. 8<sup>33</sup>, Turkey cannot expect any service of public benefit for those who live in its territory from the BTC oil pipeline project.<sup>34</sup> The BTC consortium claims that this clause is aimed at preventing any further discussion about whether HGA can be interpreted such as a concession agreement since the BTC consortium has no public utility interest in this project.<sup>35</sup> However, that provision has taken considerable heat since the project was being funded by the World Bank’s private lending arm, the International Finance Corporation (IFC), the European Bank for Reconstruction and Development (EBRD), and

<sup>25</sup> Çal, p. 97.

<sup>26</sup> Hildyard, Nicholas and Muttitt, Greg. *Turbo-Charging Investor Sovereignty Investment Agreements and Corporate Colonialism*, 2004, <http://www.thecornerhouse.org.uk/sites/thecornerhouse.org.uk/files/HGAPSA.pdf>. Accessed 01 May 22.

<sup>27</sup> *Id.*

<sup>28</sup> Çal, p. 97.

<sup>29</sup> *The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999)

<sup>30</sup> Amnesty International, 2003.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999)

<sup>34</sup> Çal, p. 97.

<sup>35</sup> Center for International Environmental Law. *Comments to the IFC Baku-Tbilisi-Ceyhan Pipeline Project*, [http://www.ciel.org/Publications/BTC\\_Comments\\_10Oct03.pdf](http://www.ciel.org/Publications/BTC_Comments_10Oct03.pdf). Accessed 1 May 22.

several Export Credit Agencies with public funding (what BP itself has named free public money).<sup>36</sup> There was a big dilemma within this context since public money would not be used for public benefit under this provision.<sup>37</sup>

Under Article 3 of IGA<sup>38</sup>, Turkey guaranteed to secure all the egresses and ingresses in and out of Turkish territory during the construction of this project.<sup>39</sup> The Turkish Government has taken a major responsibility by itself even though Turkey was not entitled to get any specific payments.<sup>40</sup> Article 4 of IGA<sup>41</sup>, entitled " Technical, Safety, and Environmental Standards," stipulates that international standards and practices within the Petroleum industry cannot furnish less protection than the EU legal regime furnished under the Turkish domestic legislation on technical, safety, and environmental fields.<sup>42</sup>

BP asserted the applicable international standards mentioned in the BTC pipeline agreements stating they provide more protection than Turkish national law.<sup>43</sup> The definition and boundaries of the EU law were very ambiguous and thereafter BP declared EU Directives specifically applied to the EU law on the IGA.<sup>44</sup> However, the EU directives were still very broad to interpret that clause even though BP has no authority to specify any terms under the IGA of the BTC pipeline project.<sup>45</sup> The standards clause was also criticized by the NGOs which alleged the parties of IGA would have to negotiate with each other to put a specific definition with giving priorities to international human rights law, since the current version of the standard clauses may cause tremendous human rights violations under the European Convention on Human Rights that has a great application area in Turkey.<sup>46</sup>

The NGOs inquired about the third parties' claims for exceeding industry standards.<sup>47</sup> Especially, the local people living throughout the pipelines' construction must have faced a lot of human rights violations whilst ambiguous types of industrial standards were being applied.<sup>48</sup> Similarly, the Turkish scholars emphasized that the undefined standards would not be interpreted by the Turkish Courts under the domestic Turkish legislation either and that there are tremendous

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<sup>36</sup>The Corner House. Environmental Impact Assessment of BTC Oil Pipeline, <http://www.thecornerhouse.org.uk/resource/environmental-impact-assessment-btc-oil-pipeline>. Accessed 23 April 2022.

<sup>37</sup> Çal, p. 98.

<sup>38</sup> *The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999)

<sup>39</sup> Çal, p. 98.

<sup>40</sup> *Id.* p. 97.

<sup>40</sup> *Id.*

<sup>41</sup> *The Baku-Tbilisi-Ceyhan Main Export Pipeline Agreement* (18.11.1999)

<sup>42</sup> Hildyard, Nicholas and Muttitt, Greg, 2004.

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> *Id.*

<sup>47</sup> Amnesty International, 2003.

<sup>48</sup> *Id.*

legal issues under the Turkish national law.<sup>49</sup> The most influential comment on that clause is that the industry’s pipeline standards on the guidelines that can be considered as a part of soft law were reinserted into the IGA. In this way, the petroleum industry would be able to create unilateral standards that may be binding on the Turkish Government for the implementation of agreements.<sup>50</sup>

## B. HGA of the BTC Pipeline Agreements

The HGA is an important appendix of the IGA that regulates the relationship and obligations between Turkey and the BTC Consortium in detail. The existence of the pipeline is expected to be at least 40 years under Article 3.1<sup>51</sup> The parties may also expand the life of the agreement ten more years or twice.<sup>52</sup> Turkey’s obligations can be explained under three titles<sup>53</sup>. Under the first one, entitled Turkey guarantees to freeze any amendments of the Turkish domestic law under HGA 21.2.<sup>54</sup> In addition, the HGA specifically neutralizes any type of new international obligation that will be part of Turkey’s national legal system after the HGA was signed under Article 7.2.6.<sup>55</sup> In the same provision, any interpretation of existing national and international law of the Turkish court is also avoided if the economic equilibrium of the project is affected disadvantageously.<sup>56</sup>

According to the second obligations category, entitled “obligations to refrain from applying existing law,” the HGA furnishes Turkey guarantees not to either act or fail in any approach that might exclude or delay any project activity or otherwise negatively affect the project in Article 5.2.3 of HGA.<sup>57</sup> This broad prohibition applies to any type of Turkish security, health, safety, and environmental regulations.<sup>58</sup> On the other hand, this provision has an important exception: Turkey may intervene in response to an “imminent and material threat” to protect such interests.<sup>59</sup> Under the third obligation category, Turkey has guaranteed to not only make its territory secure and convenient for the construction of the BTC pipelines but also to keep the pipelines stable throughout the project’s lifetime within the expropriated land provision and police protection clauses.<sup>60</sup> Turkey might violate tremendous human rights that are protected by European Convention on Human Rights whilst the project is being implemented as Turkey is binding some specific obligations with the European Human Right Court’s decision.<sup>61</sup>

<sup>49</sup> Çal, p. 98.

<sup>50</sup> Hildyard, Nicholas and Muttitt, Greg, 2004, Law Gazette. *Dispute Resolution (Arbitration) Clauses – Pathologies and Pitfalls*, <http://www.lawgazette.com.sg/2013-10/867.htm>. Accessed 23 April 2022.

<sup>51</sup> Amnesty International, 2003.

<sup>52</sup> Amnesty International, 2003.

<sup>53</sup> *Id.*

<sup>54</sup> *See id.* Host Government Agreement Between and Among The Government of the Republic of Turkey and MEP PARTICIPANTS [Turkey-MEP]

<sup>55</sup> *Id.*

<sup>56</sup> *Id.*

<sup>57</sup> *Id.* *See also*, Article 5.2.3 [Turkey-MEP]

<sup>58</sup> *Id.*

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> *Id.*

Turkey's additional obligations are crowned with an intense stabilization clause for the welfare of the BTC consortium under Article 7.2.11 of HGA.<sup>62</sup> According to this article, if the economic equilibrium that is established under the Project Agreements is disrupted or negatively affected directly or indirectly after either the effective date or the date that the Turkish Government has fulfilled its obligations under section 7.2 or 7.2(1) because of either specific change or a general application change of Turkish laws including taxes, health, safety and environment regulations that are interpreted and exercised by any Turkish judicial body, the Turkish Republic will be subject to all kind of actions to restore the economic equilibrium of the Project Agreements.<sup>63</sup> BP asserted that having stabilization clauses for mega-devolvement projects is very common in that region and aimed to keep their three billion dollar investment safe from any type of prospective nationalization.<sup>64</sup> On the other hand, the concept of the BTC's stabilization clause meets the standards of neither the OECD nor the United Nations Commission on International Trade Law (UNCITRAL), whilst the BTC Consortium enjoys an extensive stabilization clause avoiding any the Turkish legislation change on the domestic and international level as well.<sup>65</sup>

In addition, scholars claimed that the conception of the stabilization clause might have a chilling effect on Turkey's domestic law obligations to human rights standards. Within this clause, Turkey would not able to implement not only new human rights obligations, but also, obey current and prospective human rights obligations governed predominantly by European Convention Human Right Court.<sup>66</sup> In parallel, the Turkish scholars expounded that the apprehensive stabilization clause would affect the development of Turkish environmental law that is based on the EU Directives, negatively because of fear of compensation obligations under that clause would make the Turkish Government reluctant to harmonize the Turkish national law with the EU and international laws as well.<sup>67</sup>

Due to international communities' concern about the legal concept of BTC legal agreements, the BTC Consortium promulgated a Deed Poll, entitled The BTC Human Rights Undertaking that promises not to apply the stabilization clause for compensation whilst states (Turkey, Georgia, and Azerbaijani) enact new laws on human rights and environment as well.<sup>68</sup> However, this document cannot be considered as a part of BTC legal agreements as the document was only signed by the BTC Consortium unilaterally, and this guideline cannot be interpreted as a part of hard law by international arbitration tribunals.<sup>69</sup> The arbitration mechanism on the HGA is as inequitably disadvantageous as the stabilization clause for the Turkish Government since any dispute originating from the terms of projects will be determined by international arbitration organizations such as either ICSID or the ICC under Article 18 of the HGA.<sup>70</sup> The English law

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<sup>62</sup> Çal, p. 123.

<sup>63</sup> *Id.*

<sup>64</sup> Reyes, pp. 858-859.

<sup>65</sup> Hildyard, Nicholas and Muttitt, Greg, 2004.

<sup>66</sup> *Id.*

<sup>67</sup> Çal, pp. 126-127.

<sup>68</sup> Hildyard, Nicholas and Muttitt, Greg, 2004.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*



system was chosen as substantive law and the English language has taken primacy within any legal dispute regarding the interpretation of project agreements’ provisions between Turkish and English for future arbitration cases.<sup>71</sup>

The non-profit organizations point out that under the arbitration clause of HGA, any legal disputes either between Turkey and the BTC Consortium or third parties such as people living in the Turkish territory and the BTC Consortium will be solved by the ICSID, which is linked to World Bank for funding.<sup>72</sup> The Turkish courts’ jurisdiction is neutralized by the international arbitration mechanism, where the English law will be followed, accordingly.<sup>73</sup>

## II. ANALYSIS

Foreign direct investments, as an important key to trade’s liberalization, are warmly welcomed by undeveloped and developing countries that would like to captivate mega projects for great economic benefits whilst multinational corporations aim to embark on stable regions and truly protect their investments from a type of host states’ interferences such as regulatory amendments, domestic courts’ orders, nationalization, etc.<sup>74</sup> In particular, oil-producing countries usually cooperate with foreign companies that provide the required technologies and stable financial budgets to extract and transport oil as a significant type of foreign direct investment.<sup>75</sup>

Within this context, stabilization clauses have been applied as a substantial legal instrument for years in oil concession contracts.<sup>76</sup> This part of the paper gives a quick review of stabilization clauses under international law. Second, the concept stabilization clause of the BTC pipeline legal agreement on the HGA between Turkey and the BTC Consortium will be examined in detail.

### A. The Short Review of Stabilization Clauses’ Legal Status Under International Law

This short section examines firstly a brief history of stabilization clauses’ legal status under international customary law. Secondly, contemporary stabilization clauses’ types will be presented.

Oil agreements are usually interpreted under property rights that may be the object of an expropriation entity by international arbitration tribunals.<sup>77</sup> As a matter of fact, “conditions of lawfulness of expropriations under international law<sup>78</sup>” arise from the regulatory taking doctrine

<sup>71</sup> *Id.*

<sup>72</sup> “The ICSID (International Centre for Settlement of Investment Disputes) Convention is a treaty ratified by 157 Contracting States... authorizes arbitration.” See ICSID Convention, <https://icsid.worldbank.org/resources/rules-and-regulations/convention/overview>, Accessed 07 May 22.

<sup>73</sup> Amnesty International, 2003.

<sup>74</sup> Cotula, Lorenzo. *Regulatory Takings, Stabilization Clauses and Sustainable Development*, OECD Global Forum on International Investment OECD Investment Division, 2008, <http://www.oecd.org/investment/globalforum/40311122.pdf>. Accessed 1 May 22.

<sup>75</sup> Walter, André von. *Oil Concession Disputes Arbitration on*, Max Planck Encyclopedia of Public International Law, 2008, <http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e187?rskey=EqJq7w&result=2&prd=EPIL>. Accessed 1 May 22.

<sup>76</sup> Cotula, 2008.

<sup>77</sup> Walter, André von Walter, 2008.

<sup>78</sup> *Id.*

within which each state has a sovereign right to nationalize assets and to regulate activities of natural sources on its territory.<sup>79</sup> This principle, as being a respected principle of international customary law, was affirmed by the UN General Assembly Resolutions 1803 and 1902.<sup>80</sup> If host countries that have their natural resources work with either other states or companies as foreign investors they need to exercise their sovereign rights such as expropriating assets and regulating foreign investors’ activities within their domains, they must meet four conditions to make the prospect expropriation lawful under international law.<sup>81</sup>

For those obligations, firstly, the nationalization of foreign investors’ assets must be based on public purpose, not on arbitrary states’ activities.<sup>82</sup> Under the *BP v. Libya* case, the tribunal ruled that the purpose of expropriation was based on political reasons. Thus, the Libyan government that had sufficient knowledge about the UN’s public purpose criteria could not meet the necessity of proving legally sufficient.<sup>83</sup> Second, taking foreign investors’ assets must be founded on nondiscriminatory grounds.<sup>84</sup> In a specific example, even though in *BP v. Libya*, it was held that the expropriation was made in a discriminatory way, the tribunal of *Texcoco-Calasiatic v. Libya* ruled that “ expropriation measures were also taken against other companies.<sup>85</sup>” Third, there must be a due process under host states’ domestic frameworks. Fourthly, states must pay appropriate compensation against foreign investors for any takings.<sup>86</sup> Within this context, under the *BP v. Libya* case, for example, the Libyan government neither offered an appropriate offer of compensation nor followed the due process for the unlawful expropriation.<sup>87</sup>

Even though foreign investors have some protections such as an appropriate compensation against a lawful expropriation under international customary law for their energy investments, foreign corporations aim to keep their projects safe and stable against any type of expropriations and regulations that may affect negatively economic values of projects.<sup>88</sup> These heavy cash flow investment projects need to be protected with better remedies beyond the unlikely attachment of a regulatory taking doctrine.<sup>89</sup> The stabilization clauses are one of the most important legal instruments to achieve those foreign investors’ goals since host governments are legally and theoretically bound by a contractual commitment whilst they guarantee not to change the regulatory framework against the economic equilibrium of projects.<sup>90</sup> If any change adversely

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<sup>79</sup> Cotula, 2008.

<sup>80</sup> *Id.*

<sup>81</sup> *Id.* See also Walter, Andre von, 2008.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> *Id.*

<sup>87</sup> *Id.*

<sup>88</sup> Ong, Sheldon Leader-David. *Global Project Finance, Human Rights and Sustainable Development*. Cambridge University Press, 2013, p. 147.

<sup>89</sup> *Id.* p. 147.

<sup>90</sup> See Harten, Gus Van. “The Public-Private Distinction in the International Arbitration of Individual Claims against the State”, *International and Comparative Law Quarterly*, Vol: 56, 2007, pp. 371- 394.

affecting projects’ economic value is made, host states must pay the required compensation to restore the economic equilibrium<sup>91</sup>.

Under international customary law, stabilization clauses have been discussed and stabilization clauses that restrict the host states’ sovereignty have been discussed as well.<sup>92</sup> The legal question is still left unanswered.<sup>93</sup> The *Texoco v. Libya* tribunal held that ‘the stabilization clause limits the host state’s sovereignty as the host state in exercising its sovereignty committed to its waiving.’<sup>94</sup> In the tribunal’s decision, the U.N. General Assembly Resolution 1803 on the Permanent Sovereignty of States over Natural Resources as expressing customary international law and the principle pact sunt servanda was referred to, to illustrate the arguments.<sup>95</sup> However, the tribunal in *LETCO v. Liberia* upheld that a stabilization clause aimed to protect against the host state’s arbitrary action but could not weaken fully the sovereign power of states.<sup>96</sup> Therefore, host states’ sovereignty rights are never been overridden by this concept.<sup>97</sup>

Under host states’ national law, the legality of stabilization clauses is a significant key for legal issues arising from the stabilization clauses.<sup>98</sup> Within this context, domestic constitutional principles are exercised to determine which law is applicable in the analysis, by the law of stabilization clauses.<sup>99</sup> Multifaceted stabilization clauses encourage transnational lawyers not only to specialize in more than one legal field but also to focus on the comparative legal study of host government national legislation such as constitutional and administrative legal custom. On the other hand, the national courts’ ruling on legal issues arising from the stabilization clauses is unlikely legitimate if viewed under international arbitration mechanisms.<sup>100</sup> Such a specific example, in the *Revere Copper v. OPIC* case, the Jamaican Supreme Court ruled that the stabilization clause freezing the Jamaican Government’s legislative power not to impose a new increasing taxation obligation was void ab initio.<sup>101</sup> The arbitral tribunal held that the application of domestic law by the Jamaican Supreme Court does not trump the application of principles of public international law that require States to govern their activities in good faith for aliens whose investments must not be affected by States’ arbitrary actions. Therefore, the stabilization clause was not voidable in that case.<sup>102</sup>

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<sup>91</sup> Ong, 2013, p. 148.

<sup>92</sup> Gehne, Katja and Brillo, Romulo, *Stabilization Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment*, Swiss National Center of Competence in Research, 2014, [http://www.wti.org/fileadmin/user\\_upload/nccr-trade.ch/wp2/Stab\\_clauses\\_final\\_final.pdf](http://www.wti.org/fileadmin/user_upload/nccr-trade.ch/wp2/Stab_clauses_final_final.pdf). Accessed 1 May 22.

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *Id.*

<sup>96</sup> *Id.*

<sup>97</sup> *Id.*

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> Gehne and Brillo, 2014.

The types of stabilization clauses have been formulated in different ways for years.<sup>103</sup> There are three categories of stabilization clauses concepts that parties on internationalized contracts apply due to their interests.<sup>104</sup> The first one, freezing clauses, freezes fully both fiscal and non-fiscal legislation about investment for the duration of the project.<sup>105</sup> Investors have used this specific clause to freeze national legislation from the effective date of agreements to the conclusion of agreements as a classical approach.<sup>106</sup> Especially, freezing clauses are usually preferred to freeze any prospective tax regulations, statutes, guidelines, etc.<sup>107</sup> The most important criticism of the freezing clause is that even though the host state guarantees not to enact any legislation against the economic value of projects negatively, states can still exercise sovereign authority in the public interest.<sup>108</sup>

The second one, the economic equilibrium clause, provides legal protection against any type of change of domestic legislation impacting negatively upon the economic value of the project, as a modern approach.<sup>109</sup> In other words, if any change of law occurs against the economic value of the project negatively, the host states are required to pay adequate compensation to investors.<sup>110</sup> The economic equilibrium clause method provides more flexibility than the freezing clause method because the parties are usually required to negotiate on the legalities before the parties apply to the international arbitration tribunals.<sup>111</sup> The Swiss author Gene posited that because economic equilibrium clauses do not avoid host states' regulation power as long as the economic value project is restored,<sup>112</sup> freezing clauses give no room for host states to regulate any type of activities that are linked to the project.<sup>113</sup>

The third one, hybrid clauses, creates their concept for the parties that will decide upon whether economic equilibrium is needed to regulate legal frameworks as part of altering law against the investment without paying compensation.<sup>114</sup> This model is unlikely to fit well the rationale behind having a stabilization clause in the international contract since parties are unlikely can agree on whether economic equilibrium is met to neutralize the stabilization clauses' legal status.<sup>115</sup> The OECD report criticized that even though foreign investors would seek to protect their investments with stabilization clauses under international law, the host states are pressured not to regulate their national legislations with new international social and environmental standards that are growing very rapidly because of globalization and new technologies' necessities. Even

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<sup>103</sup> Cernic, Jernej Letnar, "Corporate Human Rights Obligations Under Stabilization Clauses", *German Law Journal*, Vol: 11, No: 2, 2010, pp. 210-214.

<sup>104</sup> *Id.*

<sup>105</sup> *Id.*

<sup>106</sup> Gehne and Brillo, 2014.

<sup>107</sup> *Id.*

<sup>108</sup> *Id.*

<sup>109</sup> *Id.*

<sup>110</sup> Cernic, pp. 210-218.

<sup>111</sup> Gehne and Brillo, 2014.

<sup>112</sup> *Id.*

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> Gehne and Brillo, 2014.

worse, the international standards adopted into national legislation of host states may often not be exercised because of fear of acting against the project's economic equilibrium.<sup>116</sup>

The OECD report further premised that stabilization clauses may make host states reluctant to enhance their environmental and social standards. In other words, host states would be pressured by the compensation’ fear and concerns about the long-term projects. Thus, not only would the legislative branches be discouraged from enacting new social and environmental regulations. The executive branches would be unwilling to implement international standards that are already adopted in their national legislations because of the menace of contractual sanctions under the chilling effect context.<sup>117</sup> In particular, poor countries may be affected by the chilling effect to keep international investments stable in their territories.<sup>118</sup>

Consequently, even though stabilization clauses provide tremendous advantages to multinational energy companies, host states may struggle to harmonize their domestic social and environmental regulations and agreements with international standards because of the contractual obligations’ compensation threat and concern.

### **B. Overview of the BTC Legal Agreements’ Stabilization Clause for Turkey**

This section of the paper examines the stabilization clause on the HGA between Turkey and the BTC consortium under customary international law and Turkish domestic law. The unique HGA stabilization clauses comprise two parts. The first part of the clause provides that if any change of law affects the project’s economic value, Turkey must restore the economic equilibrium of the project.<sup>119</sup> The second part of the stabilization clause provides that the HGA retains a unilateral right to compensation to the BTC consortium if Turkey enacts any type of legislation affecting the value of the project.<sup>120 121</sup>

The IGA’s prevailing legal system successfully aided the BTC consortium, whose projects would unlikely be affected by Turkey’s prospect amendments to domestic law within the stabilization concept.<sup>122</sup> However, it is uncertain and disputed what “change of law” means under the BTC legal agreements, and it would be questionable until Turkey enacts any type of law affecting the project’s economic values.<sup>123</sup> Similarly, the Turkish scholars posited that both “change in law” and “economic equilibrium” terms will be interpreted and ultimately applied by international arbitration tribunals, not by the Turkish courts. Furthermore, the Turkish government would not exercise its sovereign rights in some specific areas such as tax, social, environmental regulations, etc.<sup>124</sup>

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<sup>116</sup> Cotula, 2008.

<sup>117</sup> *Id.* pp. 11-12.

<sup>118</sup> *Id.*

<sup>119</sup> Cernic, 2010.

<sup>120</sup> *Id.*

<sup>121</sup> *Id.*

<sup>122</sup> Cernic, 2010, p. 221.

<sup>123</sup> *Id.*

<sup>124</sup> Çal, pp. 96-102.

The unique stabilization clause of HGA is broader than many typical international investment agreements for the BTC pipeline project since firstly within this context the treaty was used instead of using a state contract.<sup>125</sup> Secondly, behind the traditional stabilization technique for freezing any present and future law, the HGA’’ [contains] economic stabilization provisions as an additional safeguard for the stability of parties’ contracts.<sup>126</sup>’ The BTC’s stabilization clause has both freezing and economic equilibrium functions as a combined stabilization clause.<sup>127</sup> The concept of changes of law may conflict with Turkey’s prospective fundamental human rights obligations that are based on not only new international treaties but also European Human Right Court’s obligations.<sup>128</sup>

The Model Investment Agreement drafted by the United Nations Commission on International Trade Law (UNCITRAL) advises on projects’ rules. Basically, ‘‘change of law’’ is an inevitable consequence of democracy for host states. Thus, corporations ought to expect possible amendments instead of freezing host states’ legal frameworks.<sup>129</sup> For being more beneficiary, stabilization clauses’ scope should be constricted by specific legislation that interferes with project economic values.<sup>130</sup> Similarly, the OECD suggested that the restriction of legislation should be specified for any unnecessary compensation claims that also cause unnecessary financial costs.<sup>131</sup> Consequently, a hybrid type of the BTC’s stabilization clause neither fits the UNCITRAL nor OECD models. Turkey is under the pressure of compensation threat for at least forty more years under the unprecedented stabilization clause.<sup>132</sup>

### III. PROPOSED SOLUTIONS

This part of the paper advises some proposals for the Republic of Turkey for the BTC and prospective pipeline projects’ legal agreements. As an important trade partner and official candidate of the EU, Turkey aims to enjoy its unique geography to attract more oil and natural gas pipeline projects to its territory whilst Turkey strives to diversify its energy sources and follow a consistent energy policy that conforms to the EU energy policy.<sup>133</sup>

Under the stabilization clause, the BTC pipeline projects’ prevailing legal regime probably does not conform with the EU social, environmental, and labor directives. Therefore, Turkey should not only negotiate with the BTC Consortium to specify what change in law means, but also freezing the Turkish national legislation system for forty years against the value of projects will

<sup>125</sup> Maniruzzaman, A.F.M. ‘‘International Energy Contracts and Cross-Border Pipeline Projects: Stabilization, Renegotiation and Economic Balancing in Changed Circumstances - Some Recent Trends’’, *OGEL*, Vol:1, No:12, 2006, <http://www.ogel.org/article.asp?key=2289>. Accessed 1 May 2022.

<sup>126</sup> *See id.*

<sup>127</sup> Cotula, 2008.

<sup>128</sup> Cernic, 2010, pp. 210-221.

<sup>129</sup> Hildyard, Nicholas and Muttitt, Greg, 2004.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* (The author also underlined that the Indian’s model of stabilization clause provides more flexibility in order to negotiate for the amendments.)

<sup>132</sup> *Id.*

<sup>133</sup> *Turkey’s Energy Strategy*, 2015. (The Turkish Foreign Affairs Ministry indicates that there are three current oil pipelines projects and four current natural gas pipeline projects that are based on the Turkish territory.)

be replaced with a more flexible stabilization clause that meets the OECD and UNCITRAL criteria. Turkey and the BTC consortium should review problematic clauses such as the EU law and international standards in the BTC legal agreements. Specific terms should be used to avoid the risk of legal discussion for not only the Turkish Government's interests but also the BTC Consortium's economic goal as well.

## CONCLUSION

BP as an important shareholder of the consortium of Azerbaijan International Operating Company had enjoyed the discovery of extracting and transporting Azerbaijani oil from the late 1990s and 2020s to Western markets. The most inexpensive commercial way of Caspian oil transportation was that the Caspian oil was supposed to be carried out oils by shipping tankers throughout the Turkish Straits to energy-hungry EU countries. BP aimed to operate the new BTC Consortium to construct a 1780 kilometer Transcaucasian pipeline to secure their long-term economic goals in that region.

The IGA of the BTC pipeline project was used to neutralize the Turkish national legislation whilst the IGA creates its own unique prevailing legal regime that is also an essential key element to establishing the stabilization clause on the behalf of the BTC Consortium. The stabilization clause of HGA attached to the IGA to make the international private concession of the treaty has two different functions: freezing out the Turkish legislation system, especially the Turkish domestic law and regulations, and offering even restitution of economic equilibrium. Any type of claims, especially compensation demands will be evaluated and ruled by international arbitration tribunals according to the English substantive law for the next forty years.

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