

Preliminary Analysis of the Implications of the Host Government Agreement between Turkey and the BTC Consortium

October 2002

This analysis is an update of the findings of an International Fact-Finding Mission to Turkey in July/August 2002. The Fact Finding Mission consisted of representatives from the following NGOs: Campagna per la Riforma della Banca Mondiale, Kurdish Human Rights Project, The Corner House, Ilisu Dam campaign, Platform.

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The FFM would like to indicate that this is a preliminary analysis pending detailed review of the IGA and other relevant Project Agreements.

The BTC project is to be designed, built and operated in a manner intended to conform with a number of legislative measures, the main categories of which are listed hierarchically below:

1. The Constitution of the Republic of Turkey;
2. The Inter-Government Agreement (IGA);
3. The Host Government Agreement (HGA);
4. Turkish domestic law not superseded by the IGA or HGA;
5. Other regulatory requirements such as Governmental Decrees, Regulations, Communiqués, Ministerial Orders, Instructions, to the extent that they do not conflict with the IGA or HGA.

Upon publication in Turkey's Official Gazette on 10th September 2000 (No 24166),¹ the IGA and HGA for Turkey constitute binding international law and are part of the Turkish legal system; they constitute the prevailing domestic law of Turkey governing the BTC project. These Agreements define the capital and resources that each signatory is to provide to the project, the timetable by which it would be developed and the standards that it must meet.

The IGA is an international agreement signed by the three transit countries (the Azerbaijan Republic, Georgia and the Republic of Turkey) and thus is binding only on these three countries. The HGA is defined as a private law contract signed by the Republic of Turkey and the oil companies² ("the Consortium").

Under the HGA, the Turkish Government has exempted the consortium seeking to build the pipeline from any obligations under Turkish law, aside from the Constitution which conflict with the terms of the HGA/IGA.³ In doing so, the FFM finds, it has effectively abrogated its executive and legislative powers to protect Turkish citizens from potential environmental damage and associated health and safety hazards or to improve the regulatory regime should changes in our understanding of the risks require it.

Under the HGA, the Turkish Government has also effectively granted BP exemption from the financial impacts of any new environmental, social or any other laws affecting the pipeline that Turkey may introduce in the next forty years, the lifetime of the Agreement. In addition, it has undertaken to compensate the BTC consortium if new taxes or health or safety or environment laws adversely affect the finances of the project.

Once the project is underway, only BP and its partners have the power to terminate the HGA, except in extraordinary circumstances. The Turkish Government is thus not in a position to regulate or ensure *de facto* oversight of the operation or construction of the pipeline. This inevitably limits the ability of the World Bank to place compliance conditions on the project.

Even a future Turkish Government committed to human rights would not have the ability to invoke its executive powers to amend the agreement so as to afford its citizens greater protection..

The FFM has made a preliminary attempt to assess the project's compliance with international private and public laws. It would appear that the HGA places the project in potential violation of the European Convention on Human Rights, European Union laws and other international law instruments. Certain of the HGA's most relevant provisions are briefly analysed in this report.

¹ Environmental Impact Assessment, June 2002, Appendix A3-13.

² The State Oil Company of the Azerbaijan Republic, BP Exploration (Caspian Sea) Ltd, Statoil BTC Caspian AS, Ramco Hazar Energy Limited, Turkiye Petrolleri A.O., Unocal BTC Pipeline LTD, Itochu Oil Exploration (Azerbaijan) Inc., Delta Hess (BTC) Limited.

³ The Agreement has the same legal standing as any domestic law and prevails "over all Turkish law (other than the Constitution)".

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The FFM is deeply concerned about the human rights, environmental and developmental implications of the HGA and recommends that these are analysed in detail – and publicly discussed – before any public funding is given for the project.

BOX: THE TURKISH CONSTITUTION AND THE HGA

The Turkish Constitution does not directly address environmental matters. But Section III of the Turkish Constitution establishes an "environment right" as one of the Social and Economical Rights and Duties. Under Article 56 "*Everyone has the right to live in a healthy and stable environment. It is the duty of the State and the citizens to develop the environment, to protect environmental health and to prevent environmental pollution*". Under this Article, it is one of the functions of the State to develop the environment, to protect environmental health and to prevent environmental pollution.⁴

The most relevant parts of the HGA are reproduced below in bold, together with commentaries on their implications.

PREAMBLE

"WHEREAS, in connection therewith, the Intergovernmental Agreement shall become effective as law of the Republic of Turkey and (with respect to the subject matter thereof) prevailing over all other Turkish Law (other than the Constitution) and the terms of such agreement shall be the binding obligation of the Republic of Turkey under international law; this Agreement shall gain legal effect following publication in the *Official Gazette* as a part of the appropriate Decree of the Council of Ministers of the Republic of Turkey; the Government Guaranty and the Turnkey Agreement shall become effective and shall be binding and enforceable in accordance with their terms; and any other Project Agreements shall be binding instruments, enforceable in accordance with their respective terms."

Implications

- The agreement (together with the IGA) seeks to establish a legal regime that prevails over all other current or future domestic law that may conflict with the Project Agreement or otherwise prejudice the economic interests of the consortium.
- Accordingly, the Turkish Government has limited its powers to protect Turkish citizens from potential environmental damage and associated health and safety hazards to the extent that they are not protected by the HGA.
- Any conflict between the HGA and other current or future Turkish law would be resolved in favour of the HGA as otherwise the Turkish Government would be in breach of contract and a claim for damages would be open to the consortium.

ARTICLE 3 - Agreement, Term and Duration

Para 3.2

"Notwithstanding the foregoing Section 3.1, this Agreement may be terminated at any time by the MEP [Main Export Pipeline] Participants giving their written notice of termination to the Government and shall be of no further force or effect for any purpose as of the date specified by the MEP Participants in said notice."

⁴ Environmental Impact Assessment June 2002, Appendix D-2.1.1

Para 3.3

"If the MEP Participants have not taken steps to commence the construction phase respecting the Facilities (by, for example, giving notice to the Turnkey Contractor under the Turnkey Agreement to commence such activity) by not later than thirty-six (36) months after the Effective Date, then for a period of one hundred twenty (120) days thereafter the Government shall have the right to give written notice to the MEP Participants of the termination of this Agreement."

Para 3.4

"If the Government concludes that the MEP Participants have committed a material breach of any of their joint and several obligations (as those obligations are set forth in Section 11.3), then the Government shall have the right to give written notice to the MEP Participants of such breach in detail sufficient for the MEP Participants to undertake cure. During the pendency of any discussions to attempt resolution and/or any subsequent arbitral proceedings, the MEP Participants may, but shall have no obligation to, undertake to address and/or cure the alleged breach; provided, however, in the event the MEP Participants do not commence efforts to effect cure of a disputed breach, the Government may undertake cure."

Implications

- The consortium has the power to terminate the contract at any time and thus the Turkish Government would not be able to demand compliance with new regulations or to ensure *de facto* oversight of the operation or construction of the pipeline. Accordingly, the World Bank's ability to place compliance conditions on the project may be severely limited.
- In the case of a material breach of contract by the consortium, the consortium has no obligation to address and/or cure that breach unless and until the time the Government has proven knowing and persistent failure or frustration of contract. The latter requirements would be difficult to satisfy and hence it is unclear who would be liable to remedy the breaches whilst the dispute in being resolved. Such an extended delay would potentially have severe consequences for the environment and those affected.

ARTICLE 4 - Grant of Rights

Para 4.1(iii)

"For purposes of the Project, the State Authorities hereby grant pursuant to the Project Agreements:

"to each of the MEP Participants, the exclusive and unrestricted property right (other than ownership) to use, possess, control and construct upon and/or under the Permanent Land, and to restrict or allow (at the MEP Participants' sole discretion) the use, occupation, possession and control of, and construction upon and/or under, the Permanent Land by any other Persons."

Implication

- The consortium is granted an effective right to restrict the geographical development of villages, without compensation. It would be for the consortium to decide whether it can build structures over the buried pipeline regardless of how severely those structures interfere with the use of the adjacent land (for example, by blocking movements of livestock). In essence, a strip of Turkey a thousand kilometres long is transferred to the legal control of BP and other oil companies.

Para 4.1(vi)

[. . .] "to the MEP Participants and their designated Contractors free of charge, readily available water of sufficient quality and quantity located proximate to the Facilities in order to

perform hydrostatic and other testing of the Facilities, together with the right to dispose of same at location(s) proximate to said Facilities upon completion of such testing."

Implications

- Local populations will be able to demand access to water of sufficient quality and quantity only to the extent that their demands do not conflict with demands of the project as stated by the consortium.
- The polluted water resulting from hydrostatic and other testing may be disposed of at the same location without any determination of responsibility and liability.

ARTICLE 5 - Government Guarantees

Para 5.2(iii)

"Without limiting the breadth and scope of the foregoing, the Government hereby commits the State Authorities to perform and guarantee to each of the MEP Participants:

"that the State Authorities shall not act or fail to act in any manner that could hinder or delay any Project Activity or otherwise negatively affect the Project or impair any rights granted under any Project Agreement (including any such action or inaction predicated on security, health, environmental or safety considerations that, directly or indirectly, could interrupt, impede or limit the flow of Petroleum in or through the Facilities, except under circumstances in which continued operation of the Facilities without immediate corrective action creates an imminent, material threat to public security, health, safety or the environment that renders it reasonable to take or fail to take, as the case may be, such action and, then, only to the extent and for the period of time necessary to remove that threat)."

Implications

- The preservation of the stability of the project prevails over any other considerations except where there is an imminent, material threat to public security, health and the environment. Thus the project has power over the state in the relevant area.
- It is unclear as to what would be allowed as constituting an "imminent and material threat" and who would decide if such a threat existed.
- The high threshold of damage required before action is taken is at odds with any recognised concept of *precaution* in matters of environmental protection.
- Local populations would have no redress where the Government has not acted or has failed to act to protect its interests.

ARTICLE 6 - Representations and Warranties

Para 6.2(v)

"The Government hereby represents and warrants to each of the MEP Participants that as of the Effective Date the Government and throughout the term of this Agreement:

"the State Authorities have not granted and are not obligated to grant to any Person any rights or privileges that are inconsistent or conflict, or that may limit or interfere, with the exercise and enjoyment of the rights and privileges held by any Project Participant under any Project Agreement."

Implication

- Any natural or legal person adversely affected by the project would not be able to demand from the Turkish Government the grant of any rights or privileges that the consortium or the Government consider as against the project.

ARTICLE 7 - Certain Covenants and Consents of the Government

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Paras 7.2 (vi) and (xi)

"The Government hereby covenants and agrees (on its behalf and acting on behalf of and committing the State Authorities) that throughout the term of this Agreement:

"if any domestic or international agreement or treaty; any legislation, promulgation, enactment, decree, accession or allowance; any other form of commitment, policy or pronouncement or permission, has the effect of impairing, conflicting or interfering with the implementation of the Project, or limiting, abridging or adversely affecting the value of the Project or any of the rights, privileges, exemptions, waivers, indemnifications or protections granted or arising under this Agreement or any other Project Agreement it shall be deemed a Change in Law under Article 7.2(xi).

"the State Authorities shall take all actions available to them to restore the Economic Equilibrium established under the Project Agreements if and to the extent the Economic Equilibrium is disrupted or negatively affected, directly or indirectly, as a result of any change (whether the change is specific to the Project or of general application) in Turkish Law (including any Turkish Laws regarding Taxes, health, safety and the environment)."

Implications

- The Turkish Government is bound by the HGA to compensate the consortium for any changes in the law (including changes aimed at improving protection of human rights or the environment) where such changes negatively impact on the value of the consortium's investment. In practice this may prevent Turkey from enacting or acceding to such laws (or from implementing them in the pipeline corridor).
- This has real potential to place Turkey in direct contravention of international and European laws by which Turkey is currently bound or would be bound in the future.
- The Turkish Government is thus put in a position where in practice it is not to be able to regulate or control the construction and operation of the pipeline.
- These provisions must be read in conjunction with Article 16 of the HGA, which binds the state to the agreement notwithstanding any change in the constitution, nature or effect of the state authorities. The present Government has thereby bound all subsequent governments to the HGA.

ARTICLE 10 - Compensation for Loss of Damage

Para 10.1

"Without prejudice to the right of the MEP Participants to seek full performance by the State Authorities of the State Authorities' obligations under any Project Agreement, the Government shall provide monetary compensation as provided in this Article 10 for any Loss or Damage which is caused by or arises from:

"(i) any failure of the State Authorities, whether as a result of action or inaction, to fully satisfy or perform all of their obligations under all Project Agreements;

"(ii) any misrepresentation by the State Authorities in any Project Agreement;

"(iii) any failure by the State Authorities, whether as a result of action or inaction, to maintain Economic Equilibrium as provided in Section 7.2(xi);

"(iv) any requisitioning by Governmental forces or authorities of the assets of any Project Participant or any damage or destruction by Governmental forces or authorities of the assets of any Project Participant during any event of war (declared or undeclared), armed conflict or similar event in the Territory; or

"any act of Expropriation by the State Authorities.

"The Government shall compensate the MEP Participants for any Loss or Damage set forth in this Article 10 suffered by the MEP Participants and/or another Project Participant."

Implications

- The only specific reference to compensation is to compensation to the consortium. Compensation to the state or to third parties is not specifically provided for.

ARTICLE 11 - Limitation of Liability

Paras 11.2 and 11.4

"The MEP Participants shall be liable to a third party (other than the State Authorities and any Project Participant) for Loss or Damage suffered by such third party as a result of the MEP Participants' breach of the standards of conduct set forth in the Project Agreements; provided, however, that the MEP Participants shall have no liability hereunder if and to the extent the Loss or Damage is caused by or arises from any breach of any Project Agreement and/or breach of duty by any State Authority."

"Except as set forth in Section 3.4 hereof, it is understood and agreed that under no circumstances whatsoever shall the Government or any State Authorities have the right to seek or declare any cancellation or termination of this or any other Project Agreement as a result of any breach by the MEP Participants or any other Project Participants."

Implication

- The consortium is to be liable to third parties only in those instances where it is in 'breach of the standards of conduct set forth in the Project Agreement'. Those standards consist of (and are explicitly limited to) no more than nebulous standards of conduct as are "*generally prevailing in the international Petroleum pipeline industry for comparable projects.*" (e.g., Appendix 5, paras. 3.3 and 4.2).

ARTICLE 12 - Security

Para 12.1

"[...] the State Authorities shall ensure the safety and security of the Rights to Land, the Facilities and all Persons within the Territory involved in Project Activities and shall protect the Rights to Land, the Facilities and those Persons from all Loss or Damage resulting from civil war, sabotage, vandalism, blockade, revolution, riot, insurrection, civil disturbance, terrorism, kidnapping, commercial extortion, organised crime or other destructive events."

Implication

- The inclusion of the broad concept 'civil disturbance' could be used to justify serious human rights breaches at the hands of the state in its attempts to ensure the stability of the project.

ARTICLE 16 - Binding Effect

Para 16.1(i)

"This Agreement and the rights, obligations and other provisions of this Agreement and any other Project Agreement shall bind and apply to the Parties and:

"in the case of the State Authorities, shall continue to bind the Government, all State Entities and all Local Authorities notwithstanding any change in the constitution, control, nature or effect of all or any of them and notwithstanding the insolvency, liquidation, reorganisation, merger or

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other change in the viability, ownership or legal existence of the State Authorities (including the partial or total privatisation of any State Entity)."

Implication

- Turkey will be bound by the terms of this agreement even in the event of the election of a government more committed to protection of human rights and the environment.

ARTICLE 18 - Dispute Resolution and Applicable Law

Para 18.1

"Arbitration pursuant to this Article 18 shall not be subject to the condition of exhaustion of local remedies such as that referred to in Article 26 of the ICSID Convention."

Para 18.4

"An arbitral tribunal constituted pursuant to this Agreement shall consist of three (3) arbitrators, one of which shall be appointed by the Arbitrating Party or Arbitrating Parties first requesting arbitration, and one of which shall be appointed by the opposing Arbitrating Party or Arbitrating Parties. The third arbitrator, who shall be the presiding arbitrator of the arbitral tribunal, shall be appointed by agreement of the first two arbitrators appointed. [...] The Parties agree that, regardless of the payment scales otherwise prescribed by any institution administering an arbitration under this Agreement, the Arbitrating Parties shall compensate the members of the arbitral tribunal at rates sufficient to secure their service as arbitrators."

Para 18.6

"[...] The language used during any arbitration proceeding shall be the English language and the English language text of this Agreement will be used and relied upon for all purposes by the arbitral tribunal."

Para 18.12

"This Article 18 shall be governed in accordance with the substantive law of England, but excluding any rules or principles of English law that will (i) prevent adjudication upon, or accord presumptive validity to, the transactions of sovereign states or (ii) require the application of the laws of any other jurisdiction to govern this Article 18."

Implications

- The HGA supersedes the International Centre for Settlement of Investment Disputes (ICSID) Convention with regard to exhaustion of local remedies.
- It is not clear how the arbitration tribunal will function.
- The exclusion of any language other than English places the Turkish Government and any other non-English speaking parties at a disadvantage.

APPENDIX 5 - Codes of Practice

Paras 3.3 / 4.2

"If any regional or intergovernmental authority having jurisdiction enacts or promulgates environmental standards relating to areas where Pipeline Activities occur, the MEP Participants and the Government will confer respecting the possible impact thereof on the Project, but in no event shall the Project be subject to any such standards to the extent they are different from or more stringent than the standards and practices generally prevailing in the international Petroleum pipeline industry for comparable projects.

"If any regional or intergovernmental authority having jurisdiction enacts or promulgates social regulations or guidelines applicable to areas where Project Activities occur, the MEP Participants and the Government will confer respecting the possible impact thereof on the Project, but in no event shall the Project be subject to any such standards to the extent they are

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different from or more stringent than the standards and practices generally prevailing in the international Petroleum pipeline industry for comparable projects."

Implications

- Turkey guarantees that the Project will not be bound by any law that creates environmental or social protection standards that are higher than those generally adhered to in the industry even where such laws are enacted by a regional authority with the authority to require such compliance (including potentially the European Union). Serious questions arise about the compatibility of such a provision with Turkey's progress towards accession. This should be read in conjunction with Art. 21.2 (HGA) in which Turkey gives express recognition to its intention that no future law shall abridge or affect adversely the rights granted to the Consortium or take precedence over any part of the Project Agreements.
- Local populations would not be able to seek redress in accordance with regional legislation to the extent that the latter conflicts with the project.

Box: MAI by the Back Door?

The Host Government Agreement signed by BTC and the Government of Turkey has many of the provisions of the now-discredited Multilateral Agreement on Investments (MAI).

Negotiated in secret within the Organisation for Economic Cooperation and Development — a grouping of the world's 29 richest countries, including Turkey [1] — the MAI was roundly rejected by national parliaments and the public after its contents were leaked to non-governmental organisations and broadcast on the internet.

Branded a “corporate charter” by its critics, due to concerns over its social and environmental implications, the MAI provoked demonstrations on the streets of several OECD capitals. Opponents ranged from environment and development NGOs to consumer groups, human rights bodies, trade unions, local governments, parliamentarians and church groups. The MAI negotiations, initiated in 1995, finally fell apart in 1998.

The MAI agreement would have empowered private investors to extract compensation from foreign governments for legislation that adversely affected their investments, regardless of the public interest. The HGA's provisions on Turkey having to compensate BTC if any new social or environmental laws affect the “economic equilibrium” of the BTC pipeline reflect these MAI provisions.

The MAI was also criticised for protecting the interests of the investor without any corresponding attention being paid to establishing legally-binding investor obligations and accountability. Its proposed “investor-state” dispute mechanism, involving secret tribunals, was also seen as biased in favour of companies and lacking in mechanisms which would give effective legal standing for citizens to bring actions. Again, the HGA can be criticised on both counts.

The Fact-Finding Mission is gravely concerned that BP and the other western oil companies that form the BTC consortium have sought to achieve the MAI's provisions via a bilateral agreement when those provisions have been so decisively rejected at the multilateral level by the public in their home countries.

[1] The OECD comprises 29 of the world's richest countries, including European countries, the US, Japan, Australia, New Zealand, Finland, Mexico, the Czech Republic, Hungary, Poland, Turkey and Korea. Based in Paris with an annual budget in excess of \$200 million, the OECD calls itself “a club of like-minded countries”, which believe in market economics and pluralistic democracy. It provides a forum for discussion on economic and social policy, as well as producing research, policy papers and international treaties and agreements. See www.oecd.org.

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