

## A SYNOPSIS OF THE LEGAL FRAMEWORK REGULATING THE POWER SECTOR IN TURKEY

by Emine Başcı DEVRES\* & Begüm DURUKAN\*\*

### I. Introduction

The power sector in Turkey is a significant field that has generated rapid and pioneering developments in several areas of law. The scarcity of the energy supply vis-à-vis the energy demand in Turkey has particularly obliged the sector to develop in the last two decades. Owing to the needs of and developments in this sector, Turkey has witnessed new legal and financial structures, feverish legal discussions, constitutional and administrative challenges, organisational restructurings and legislative amendments leading to a totally new legal environment regulating the energy market. This Article aims to walk the reader through the evolution steps of the legal framework regarding the power sector.

Accordingly, the Article will first discuss, in the next section, the pieces of legislation put into force since 1984 together with any amendments made to and challenges initiated against such legislation. In the third section, recent legal developments including the constitutional amendments affecting the power sector shall be analysed. The forth section shall examine the new Electricity Market Law (“EML”) currently being discussed at the Parliament. The Conclusion shall summarise the nature of the innovation achieved through such legislative developments.

### II. Chronological Analysis of the Main Legislation Governing the Power Sector in Turkey

#### *A. Act No. 3096 concerning the Assignment to Entities other than Turkish Electricity Authority of the Generation, Transmission, Distribution and Trade of Electrical Energy (“Act No. 3096”)<sup>1</sup>*

Until the enactment of Act No. 3096, the main activities of the power sector, namely, the generation, transmission and distribution of electricity energy were under the monopoly of Turkish Electricity Authority (“TEK”), a state economic enterprise

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\* Attorney at Law, Partner, Birsal Law Offices.

\*\* Attorney at Law, Birsal Law Offices.

<sup>1</sup> Act No. 3096 published in the Official Gazette No. 18610, dated December 19, 1984.

subject to Decree in the Force of Law No. 232<sup>2</sup>. and owned in its entirety by the Turkish State. Private law companies with domestic and/or foreign capital have become eligible to operate in electricity-related activities through Act No. 3096.

This Act, in general, governs the main principles of the participation of private companies in energy activities, the agreements to be entered into, as well as the term and termination of the authorization. The scope of the activities private law companies may carry out under Act No. 3096 falls under one of three categories<sup>3</sup>. The first category of activities pertains to the assignment of private law companies for the establishment and operation of generation, transmission and distribution facilities and the trade of electricity energy in regions to be determined by a regulation<sup>4</sup>. The second category permits private law companies established for the sole purpose of generating electricity energy to establish and operate generation facilities through an authorization to be obtained and to sell the electricity energy generated in these facilities to either TEAS or the assigned company operating in the relevant region. As the third category, the operation rights of generation, distribution and transmission facilities established or to be established by public institutions in authorization regions may be transferred to public law entities. The procedures to be followed for all three categories are regulated in Act No. 3096.

Another innovation introduces by Act No. 3096 which is significant for the financing of the projects carried out under Act No. 3096 has been the establishment of the Electrical Energy Fund, a public entity the function of which is, *inter alia*, the financial support of the facilities to be established and the provision of consistency in the energy price.

In 1993, through the unbundling of TEK, Turkish Electricity Generation and Transmission Company (“TEAS”) and Turkish Electricity Distribution Company (“TEDAS”) were established<sup>5</sup>. Following this restructuring, within the context of Act No. 3096, TEAS has become the party to and bound by the energy sale agreements previously executed between TEK and private law companies<sup>6</sup>.

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<sup>2</sup> Decree in Force of Law No. 232 concerning State Economic Enterprises published in the Official Gazette No. 18435, dated June 18, 1984.

<sup>3</sup> These categories are set forth in Articles 3, 4 and 5 of Act. No. 3096.

<sup>4</sup> The authorization regions are determined by the Regulation regarding the Regions of Authorization of Institutions other than TEK, published in the Official Gazette No. 18858, dated September 4, 1985.

<sup>5</sup> The unbundling of TEK has been achieved through the Council of Ministers Decree No. 93/4789 published in the Official Gazette No. 21699, dated September 15, 1993 (“TEK Decree”). Please note that currently, TEAS is also being restructured as mentioned in Section IV of this Article.

<sup>6</sup> TEAS and TEDAS established as a result of the unbundling of TEK are the legal successors to TEK. This relationship is revealed by Article 6 of the TEK Decree and Article 4 of the Articles of Association of both TEAS and TEDAS.

Act No. 3096 and its implementing Regulation<sup>7</sup> constitute the foundation for all power projects carried out by private law companies and opens up the way for all further legal regulations put into effect regarding the power sector.

***B. Build-Operate-Transfer (“BOT”) Model- BOT Law concerning the Realization of Certain Investments under the BOT Model (“BOT Law”)***<sup>8</sup>

Following Act No. 3096, the BOT Law was put into effect setting forth a specific scheme under which private law companies can carry out certain investments and services including the generation, transmission, distribution and the sale of electricity energy. This section shall examine the BOT Law with its amendments made prior to the legislative amendments of 1999<sup>9</sup>.

*1. Scope of the Act*

The BOT Law consists of a specific provision that Act No. 3096 shall continue to be applied<sup>10</sup> demonstrating that the Turkish legislature has aimed to keep both pieces of legislation in force to be applied depending on the special needs and characteristics of the projects.

The original form of BOT Law covers, *inter alia*, projects concerning the generation, transmission and distribution of electricity energy. In its originally enacted form, the BOT Law provides that agreements to be entered into under the BOT Model are subject to private law and are of non-concessionary nature<sup>11</sup>. In addition, the BOT Law specifically stipulates that Act on Concessions<sup>12</sup> shall not be applicable to projects realized under the BOT Law.<sup>13</sup>

Another important feature of the BOT projects has been the issuance of state guarantees under Article 11 of the BOT Law which is subsequently amended by Law No. 4180<sup>14</sup>. Under this Article, the Minister in charge of the Undersecretariat of Treasury (“UT”) is authorized to guarantee the payment of sale proceeds for electrical energy, as well as any other goods or services acquired by public institutions from private law companies within the framework of the BOT Model. Additionally, all

<sup>7</sup> Regulation on the Principles to be applied to the Assignment to Entities other than Turkish Electricity Authority of the Generation, Transmission, Distribution and Trade of Electrical Energy, published in the Official Gazette No. 18858, dated September 4, 1985.

<sup>8</sup> BOT Law published in the Official Gazette No. 21959 dated June 13, 1994.

<sup>9</sup> The legislative amendments comprising the constitutional amendment and implementing legislation also affecting the BOT Law is analysed in Section III of this Article.

<sup>10</sup> Article 13 of the BOT Law.

<sup>11</sup> Article 5 of the BOT Law.

<sup>12</sup> Act No. 2025 on Concessions published in the Official Gazette No. 2139, dated July 2, 1932.

<sup>13</sup> Article 14 of the BOT Law.

<sup>14</sup> Act No. 4180 published in the Official Gazette No. 22747, dated September 4, 1996.

agreements to be concluded, as well as all acts and things to be done by and between the administration and the private law company concerned are exempted from stamp tax and other fees<sup>15</sup>.

Whereas Act No. 3096 enables private law companies to operate in the power sector for the first time, the BOT Model constitutes the first piece of legislation which explicitly determines the nature of the power sector activities as non-concessionary. The determination of the nature of the power sector activities shall form the main point of legal discussion in this field, resolution of which will demand constitutional amendments.

## *2. Amendments to BOT Law*

### **a)** Act No. 4047<sup>16</sup>

By Act No. 4047, power projects are excluded from the coverage of the BOT Law. However, a second sub-section is inserted in Article 13 whereby it is stipulated that power projects subject to Act No. 3096 may benefit from the provisions of Articles 5 (specifying contracts as private law, non-concessionary contracts), 11 (UT Guarantees), 12 (tax exemptions) and 14 (inapplicability of the Act on Concessions) of the BOT Law upon the request of the Ministry of Energy and Natural Resources ("MENR"). Thus, if and when MENR so requests, projects governed by Act No. 3096 will be specified as "private-law projects," and they will enjoy state guarantees and tax exemptions, just as the projects governed by the BOT Law.

### **b)** Act No. 4180

Article 11 of BOT Law governing UT Guarantees has been subject to an amendment by Act No. 4180. Such amendment has enlarged the scope of the UT Guarantees from the sale prices of goods or services received by public institutions involved in BOT projects to all payment obligations of public institutions which may arise out of a failure in the supply of generation inputs undertaken to be provided to private law companies under the relevant contracts.

## *3. Challenges Against the BOT Law before the Turkish Constitutional Court*

### **a)** Cancellation of Certain Parts of Articles 5 and 14

The Turkish Constitutional Court cancelled certain parts of Articles 5 and 14 of the BOT Law<sup>17</sup>. The ruling of the Court became effective upon its publication in the

<sup>15</sup> Article 12 of the BOT Law.

<sup>16</sup> Act No. 4047 published in the Official Gazette No. 22130, dated December 3, 1994.

<sup>17</sup> Constitutional Court Decision No. E. 1994/71, K. 1995/23 published in the Official Gazette No. 22586, dated March 20, 1996.

Official Gazette<sup>18</sup>. According to this ruling, the provisions of Article 5 specifying BOT contracts as “non-concessionary contracts subject to private law,” and the part of Article 14 providing for the inapplicability of the Act on Concessions to BOT contracts were unconstitutional.

The reasoning of the Court was that contracts governed by the BOT Law involve the renderence of public services and are strictly related to public interest. According to the Court, where the administration enters into a contract with a private law company for the performance of a public service, such contract is and should be construed as “concession”. The Court also found that the legislator’s actual goal in specifying BOT contracts as non-concessionary contracts was to exclude such contracts from the jurisdiction of the Supreme Administrative Court, and to have any disputes that may arise out of such contracts settled before judicial courts or through arbitration<sup>19</sup>. Accordingly, the Turkish Constitutional Court took the position that contracts concluded under BOT Law were concessions and thus their execution must be made subject to the approval of, and the disputes arising thereof must be resolved before, the Supreme Administrative Court.

**b) Challenge against Article 11 as amended by Act No. 4180**

The constitutionality of Article 11 of the BOT Law, as amended by Act No. 4180 has also been challenged on two grounds. The first challenge pertains to the inconsistency between the Council of Minister’s Decree setting forth the Rules for the Implementation of the BOT Law (the “BOT Decree”)<sup>20</sup> and the BOT Law. Despite the determination of the Constitutional Court that BOT projects are in the nature of concessions, the BOT Decree remained to define BOT contracts as private law contracts. Thus, the reference in Article 11 to the BOT Decree constituted the subject matter of the constitutional challenge<sup>21</sup> and has been subject to an intermediary injunction decision of the Constitutional Court, suspending the application thereof<sup>22</sup>.

The second challenge requesting the suspension of the application of the entire Article 11 on the UT Guarantee has been rejected by the Constitution Court.

<sup>18</sup> According to Article 153(3) of the Turkish Constitution, laws, decree laws or the by-laws of the National Assembly shall be repealed on the date of publication of the cancellation ruling of the Constitutional Court if not decided otherwise by the Constitutional Court.

<sup>19</sup> According to Article 155(2) of the Turkish Constitution, the conclusion of a concession contract is subject to the prior approval of the Supreme Administrative Court.

<sup>20</sup> BOT Decree published in the Official Gazette No. 22068, dated October 1, 1994.

<sup>21</sup> The part of Article 11 constituting the subject matter of the challenge reads as follows “*those contracts which are concluded pursuant to the rules and procedures set forth in the Council of Ministers’ Decree put into force on the basis of the authority conferred by Article 4 of this Law...*”

<sup>22</sup> Following the injunction decision, this part of Article 11 has also been cancelled by the Constitutional Court. The cancellation decision has not yet been published.

#### *4. Challenges against the BOT Projects at the level of the Supreme Administrative Court*

Apart from the constitutional challenges against the BOT Law, the contracts of specific projects executed between the administration and the private law companies under the BOT Model have also been subject to challenges. These challenges have been initiated before the Supreme Administrative Court as the contracts have been deemed as concession contracts falling under the jurisdiction of the administrative courts. Chamber of Electrical Engineers (“CEE”) filed a lawsuit for the cancellation of two power projects implemented under the BOT scheme, the contracts of which have already been executed in 1996. CEE, in this lawsuit, claimed that such projects were, in fact, concessions, and that the parties, by specifying them as private law-governed projects, have tried to avoid the jurisdiction of the Supreme Administrative Court. The Supreme Administrative Court dismissed one of the lawsuits on the ground that the sixty-day time period had elapsed to file the lawsuit<sup>23</sup> and accepted the review of the second challenge.

Regarding this second challenge, 10<sup>th</sup> Chamber of the Supreme Administrative Court rejected the lawsuit on grounds that the statute of limitations had run<sup>24</sup>. 10th Chamber of the Supreme Administrative Court found that the extensive press coverage and the press releases in the claimant's own publication indicated that the CEE had knowledge of the projects and thus the argument that CEE has abided by the rules of the statute of limitations was not acceptable. Following the CEE appeal with the General Assembly of Administrative Litigation Chambers, the Supreme Administrative Court's decision was upheld<sup>25</sup>.

#### ***C. Build-Operate (“BO”) Model***

##### *1. Council of Ministers’ Decree No. 96/8269 (the “BO Decree”)*<sup>26</sup>

Following the constitutional cancellations of certain parts of the BOT Law, the BO scheme was introduced as an alternative in order to enable private companies to operate in the power sector. The BO Model provides the licensing system being one of the methods of administrative law through which the administration may assign a private company to perform a certain public service. Unlike concession, which

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<sup>23</sup> Supreme Administrative Court Decision, dated June 19, 1997 and numbered E. 1997/1107 and K. 1997/2496.

<sup>24</sup> Supreme Administrative Court Decision, dated June 24, 1998 and numbered E. 1997/774 and K. 1998/3013.

<sup>25</sup> General Assembly of Administrative Litigation Chambers Decision, dated November 4, 1999 and numbered E.1998/560 and K. 1999/982.

<sup>26</sup> Decree No. 96/8269 of the Council of Ministers concerning the Construction and Operation of Electricity Generation Facilities published in the Official Gazette No. 22660, dated June 8, 1996.

requires the execution of a bilateral agreement between the administration (or its agent) and the concessionaire; licensing is a unilateral administrative act. The BO Decree constitutes the first governmental attempt to introduce such system which was challenged before the Supreme Administrative Court and cancelled because of deficiencies in its promulgation technique<sup>27</sup>.

## 2. The BO Law No. 4283 (the “BO Law”)<sup>28</sup>

Following the challenge regarding the BO Decree, the Turkish legislature passed the BO Law in 1997 and the Regulation No. 97/9853 detailing the implementation of the BO Law (“BO Regulation”)<sup>29</sup>.

The BO Law provides for the licensing of private sector entities for the construction and operation of thermal power plants, however, it does not regulate the transmission and distribution of electricity energy. Another limitation on the scope of the BO Model is that it only covers thermal power projects excluding hydro, nuclear and geothermal plants.

Pursuant to the Transitional Article 1 of the BO Law, the bids received during the effectiveness of the BO Decree with respect to thermal power plants would continue to be evaluated according to the principles set forth in the BO Law.

## 3. Challenges to the BO Law and the Energy Sales Agreements (“ESA”s) executed under the BO Model

CEE and Kamu Isletmeciligi Gelistirme Merkezi Vakfi (“KIGEM”) have brought challenges against the BO Decree and the BO Law. CEE's challenge on the BO Law was part of the lawsuit concerning the BO Decree and KIGEM's challenge on the BO Law was part of the lawsuits regarding the ESAs of the BO projects in Turkey.

### a) CEE Challenge

CEE has initially requested the cancellation of the BO Decree before the Supreme Administrative Court. This lawsuit, instituted on July 10, 1996, requested the annulment of the BO Decree on grounds that it regulates a subject which falls within the scope of issues required to be regulated by law. The Court, in its interim decision dated February 19, 1997, upheld the CEE's request and issued an injunction

<sup>27</sup> See Section II.C.3.a. below for more detail on the challenge regarding the BO Decree.

<sup>28</sup> Law No. 4283 concerning the Regulation of Establishment and Operation of Electricity Energy Generation Facilities and Sale of Energy under the BO Build-Operate Model, published in the Official Gazette No. 23054, dated July 19, 1997.

<sup>29</sup> Regulation No. 97/9853 on the Establishment and Operation of Electricity Energy Generation Facilities and the Sale of Energy under the Build-Operate Model. published in the Official Gazette No. 23095, dated August 29, 1997.

decision suspending the application of the Decree. After the promulgation of the BO Law, the CEE filed a supplementary petition requesting the referral to the Constitutional Court of the BO Law on grounds that it aims to circumvent the injunction decision regarding the BO Decree and the concession issue.

The Supreme Administrative Court cancelled the BO Decree on grounds that it governs an area which should be regulated by law, however, rejected the request to refer the BO Law to the Constitutional Court<sup>30</sup>.

#### **b) The KIGEM Challenge**

The BO Law has been challenged on December 7, 1998, by KIGEM in the lawsuits filed before administrative courts for the cancellation of the ESAs of the ongoing BO Projects in Turkey. KIGEM, requested an injunction decision for the suspension of the implementations of the ESAs and at the same time, made an indirect constitutional challenge for the cancellation of the BO Law.

The KIGEM challenges were mainly based on the concept of public service and thus alleged that the contracts have a concession nature. KIGEM argued that the BO Law, by putting such contracts under the scope of private law, is unconstitutional taking into account the Constitutional Court decisions where electricity generation, transmission and distribution are considered as typical and standard public services and the carrying out of such services by private persons are made possible only through concession contracts. KIGEM claimed that the contracts are not executed in the proper form set forth for concession contracts. Injunction was also requested on grounds that the effectiveness of the contract and the transfer of natural resources shall result in losses that cannot be compensated.

The KIGEM challenges have been rejected by the administrative courts on grounds that KIGEM lacks standing required to file such a lawsuit.<sup>31</sup> KIGEM appealed before the Supreme Administrative Court in connection with certain projects requesting the reversal of the administrative court decisions and also injunction. The Supreme Administrative Court, in its interim decisions, rejected the requests of injunction, however, the merits have not yet been investigated<sup>32</sup>.

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<sup>30</sup> Supreme Administrative Court Decision dated December 28, 1998 and numbered E. 1996/8792, K. 1998/7213.

<sup>31</sup> Certain of these decisions are: 9<sup>th</sup> Administrative Court of Ankara Decision dated November 25, 1999 and numbered E. 1998/1275, K. 1999/1277, 8<sup>th</sup> Administrative Court of Ankara Decision dated May 10, 1999 and numbered E. 1998/1203, K. 1999/428.

<sup>32</sup> Certain of these decisions are: Supreme Administrative Court Decision dated July 20, 1999 and numbered E. 1999/2543, Supreme Administrative Court Decision dated July 8 1999 and numbered E. 1999/2407.



### III. Recent Legislative Developments effecting the Status of the Power Sector Legislation

#### A. Law No. 4446 Amending the Turkish Constitution (Constitutional Amendment)<sup>33</sup>

The Constitutional Amendment of August 1999 gave relief to all parties involved in internationally financed power projects in Turkey. Proposed by the members of the coalition parties and accepted by Parliament's qualified majority, the Constitutional Amendment constitutes a major novelty especially within the context of the above-explained challenges to the BOT and the BO Models.

Under the Constitutional Amendment, Article 47 pertaining to nationalization and privatization, Article 125 regarding recourse to judicial review and Article 155 regulating the authorities of the Supreme Administrative Court have been revised. Article 47, which previously only regulated nationalization, as amended, enables the designation of private law companies to carry out public services by private law contracts on condition that such designation is explicitly indicated by law. The amended Article 125 adopts domestic and international arbitration as an alternative in the settlement of disputes having a foreign element arising out of public services and concessions. In parallel to this change, the jurisdiction of the Supreme Administrative Court, regulated in Article 155, which formerly provided for the review of the concession contracts by the Supreme Administrative Court has been amended. The amendment removes the review of the Supreme Administrative Court over concession contracts, limiting the Supreme Administrative Court supervision to granting its opinion prior to the execution of concession contracts within two months.

#### B. Implementation Laws

The Constitutional Amendment constituted the outset of the necessary reform in the power sector and certain addenda and amendments to relevant domestic legislation were required for the implementation thereof.

##### 1. Law No. 4493 amending the BOT Law ("Law No. 4493")<sup>34</sup>

Law No. 4493 includes "the generation, transmission, distribution and sale of electricity" within the scope of the investments that may be carried out under the BOT Model with the aim of broadening the extent of energy investment projects. The Law, in accordance with the amended Article 47 of the Constitution, also stipulates that

<sup>33</sup> Law No. 4446 regarding the Amendment of Certain Provisions of the Constitution of the Republic of Turkey, published in the Official Gazette No. 23786, dated August 14, 1999.

<sup>34</sup> Law No. 4493 relating to the Amendment of certain Provisions of Law No. 3996 concerning the Realization of Some Investments and Services under the Build-Operate-Transfer Model published in the Official Gazette No. 23914, dated December 22, 1999.

contracts executed between an administration which is specified by the Higher Planning Committee, and a private law company under the BOT Model shall be governed by private law provisions.

*2. Law No. 4492 amending the Supreme Administrative Court Law and Administrative Procedure Law ("Law No. 4492")<sup>35</sup>*

Law No. 4492, reflecting the amendment to Article 155 of the Constitution, removes the Supreme Administrative Court review on concession contracts relating to public services and requires the Supreme Administrative Court to express its opinion within two months of the date of receipt thereof. It also restricts its jurisdiction to administrative lawsuits arising out of concession specifications and concession contracts relating to public services whereby arbitration has not been stipulated.

*3. Law No. 4501 enabling Arbitration in disputes arising out of concession contracts relating to public services ("Law No. 4501")<sup>36</sup>*

Law No. 4501 enables, *inter alia*, the retroactive application of international arbitration to current concession projects, excluding those which have been cancelled by a finalized court holding, through a Counsel of Ministers decree to be issued upon the application of the assigned company within one month of the promulgation date of Law No. 4501 and upon the application of the relevant administration. Law No. 4501 also comprises a "foreign element" definition which refers to any one of the cases where at least one of the shareholders of the company party to the contract is of foreign origin pursuant to the provisions of encouragement of foreign investments legislation, or where it is required to execute a foreign originated capital or loan or guarantee agreement for the application of the contract. Law No. 4501 further provides for arbitration in Turkey and abroad pursuant to Turkish law or foreign law as well as before an international arbitration institution [such as ICSID, UNCITRAL or ICC] having its own procedure for arbitration.

Article 7 of Law No. 4501 also amends the provisional Article 1 of the BOT Law to provide that, private law companies that have executed concession contracts with the administration regarding projects falling under Act No. 3096 may apply to the Counsel of Ministers within one month of the promulgation date of Law No.

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<sup>35</sup> Law No. 4492 concerning the Amendment of Some Provisions of Supreme Administrative Court Law and Administrative Procedure Law, published in the Official Gazette No. 23913, dated December 21, 1999.

<sup>36</sup> Law No. 4501 on the Principles to be Applied in the event of Submission to Arbitration of Disputes arising out of Concession Specifications and Contracts relating to Public Services, published in the Official Gazette No. 23941, dated January 22, 2000.

4501, for the application of the amended Article 5 of the BOT Law<sup>37</sup>. In such case, the contract executed between the administration and the private law company shall be revised within three months (unless a longer period has been agreed upon by the parties) of the promulgation date of the decision of the Counsel of Ministers, subject to private law provisions.

It should be noted that this law has been made subject to a constitutional challenge by one of the opposition parties in the Parliament. The challenge heard before the Constitutional Court referred to the request to cancel Articles 2c and 7 as well as Provisionary Article 1 of Law No. 4501<sup>38</sup>. The lawsuit has been rejected<sup>39</sup>.

<sup>37</sup> For purposes of clarity, amended Article 5 of the BOT Law provides that contracts executed under the BOT Model are subject to private law.

<sup>38</sup> The Articles made subject to the constitutional challenge read as follows:

**“Definitions**

ARTICLE 2 - The concepts embodied in this Law have the following meanings:

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- c) Foreign element: Any one of the cases where at least one of the shareholders of the company established or to be established that is a party to the contract is of foreign origin pursuant to the provisions of encouragement of foreign investments legislation, or where it is required to execute a foreign originated capital or loan or guarantee agreement for the application of the contract;

ARTICLE 7 - The second paragraph of Provisional Article 1 of Law concerning the Realization of Certain Investments and Services under the Build-Operate-Transfer Model dated June 8, 1994 and numbered 3996 has been amended as follows:

However, it may be decided by the Counsel of Ministers upon the application of the assigned company or the capital company within one month of the promulgation date of this Law and upon the application of the relevant administration, that Article 5 of this Law shall be applied to projects and works indicated in the first paragraph and to the projects and works subject to the Law Concerning the Authorization of Establishments other than the Electricity Institution of Turkey (TEK) for the Generation, Transmission, Distribution and Trading of Electricity, dated December 4, 1984 and numbered 3096, and Law Concerning the Authorization of Establishments other than the General Directorate of Motorways for the Construction, Maintenance and Trading of Controlled Motorways (Highway), dated May 28, 1988 and numbered 3465. In such case, the contract executed between the administration and the assigned company or the capital company shall be revised within three months as from the promulgation date of the decision of the Counsel of Ministers, subject to private law provisions, by taking into consideration the criteria regarding provisions of international financing and similar implementation contracts of the administration which are in force. The said term may be extended for a period of additional three months at most upon the agreement of the parties.

PROVISIONAL ARTICLE 1 - The projects and works initiated in accordance with the concession specifications and concession contracts relating to public services prior to the entry into force of this Law, shall be concluded in accordance with the procedures and principles to which they have been subjected.

However, except for those which have been cancelled by a finalized court holding, the application of the provisions of this Law to the projects and works specified in the first paragraph shall be decided by the Counsel of Ministers upon the application of the assigned company within one month as from the date on which this Law is promulgated and upon the application of the relevant administration. ”

4. Law No. 4577<sup>40</sup> and Law No. 4575<sup>41</sup>

The authorities of the Supreme Administrative Court and the administrative courts have been re-regulated to reflect the amendments made to the foregoing legislation by limiting their jurisdiction to disputes arising out of concession contracts which do not provide for arbitration.

**C. Effect of the Developments on the BOT and BO Legislation**

In accordance with the new regulations; after the determination of the public services which may be carried out by private persons by law, the administration shall be able to enter into private law contracts with private law companies. Likewise, the foreign investor shall be able to execute concession contracts without being subject to the Supreme Administrative Court's review of every step of the contract. In both cases, the application of international arbitration shall not carry the danger of being subject to constitutional challenges, and the project shall not face the danger of being invalidated. Such comfort shall create a safe environment for investments and shall accelerate the financing and operation of the projects.

**IV. New Electricity Market Law**

Following the foregoing evolution of the legal framework of the power sector, Turkey is in the verge of changing the operation of the electricity market entirely. The enactment of the EML constitutes the first fold of this reform and also forms part of Turkey's commitments at the level of international institutions, the performance of which has been delayed. The enactment of the EML by the end of January 2001 was set out as a structural performance criterion in the Letter of Intent dated December 18, 2000 delivered to the International Monetary Fund by the Republic of Turkey within the context of the stand-by arrangement. The Accession Partnership Document prepared by the European Union in November 8, 2000 also requires Turkey to put in place a program for the adoption of the European energy *acquis* and the establishment of the internal electricity market.

On the outset, the EML aims to set forth the rules for a competitive, liberal and efficient environment in the power sector. The structure encourages private sector

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<sup>39</sup> The rejection decision has been rendered on July 23, 2000, however, it has not yet been published in the Official Gazette.

<sup>40</sup> Law No. 4577 on the Amendment of the Law regarding the Establishment and Authorisations of the Regional Administrative Courts, Administrative Courts and Tax Courts and the Law on Administrative Procedural Law published in the Official Gazette No. 24080, dated June 2, 2000.

<sup>41</sup> Law No. 4575 on the Amendment of Supreme Administrative Court Law and the Tables Annexed to the Decree in the Force of Law regarding Regular Staff and Procedure published in the Official Gazette No. 24080, dated June 2, 2000.

investments and reduces public involvement in the field, establishes an independent regulatory and supervisory body to secure a financially strong, constant and transparent electricity market and regulates the privatisation of the state owned electricity generation and distribution assets. In order to secure a smooth passage to the newly formed electricity market, the EML provides a transition period of eighteen months starting from the effective date of the EML, which may be extended once by the Council of Ministers for a period of six months. Current participants engaged in several activities are also required to use this period to choose the market activity they desire to operate in and amend their current contracts accordingly. It is aimed to complete the establishment of the Electricity Market Regulatory Agency (“Agency”) and the enactment of regulations stipulating detailed rules regarding the operation of the electricity market in the transition phase.

Within this context, the following may be listed among the main characteristics of the new electricity market.

#### ***A. Organizational Restructuring***

Pursuant to the EML, the public law entities authorized to engage in electricity market activities are the Turkish Electricity Generation Corporation (“Generation Corp.”), Turkish Electricity Transmission Corporation (“Transmission Corp.”) and the Turkish Trade and Undertaking Corporation (Trade Corp.”). These state economic organizations will be established through the unbundling of the current Turkish Electricity Generation and Transmission Company (TEAS) into three separate entities. Being one of the pivotal points of the sector reform, this reorganization is not achieved through the EML but by a separate piece of legislation to be put in effect. The EML provides that TEAS will carry out the activities of the Generation Corp., Transmission Corp and Undertaking Corp. until their formation.

#### ***B. Licenses***

Public and private law companies are permitted to operate in the new electricity energy market by obtaining licenses to be issued by the Agency in consideration of a license fee. In accordance with the EML, licenses may be issued for a minimum term of 10 and a maximum term of 49 years and are required to cover one specific activity. A license shall set forth the scope of the market activity of the participant and shall comprise provisions on, *inter alia*, the tariff formulas and methods of adjustments. Within the transition period, legal entities currently operating in the market are permitted to carry out their activities without a license.

#### ***C. Electricity market activities and market participants***

Pursuant to the EML, market activities may be listed as generation, distribution, transmission, wholesale and retail, import and export of electricity energy. Private legal entities and real persons are allowed to conduct market activities by forming

generation, distribution, retail sale or wholesale companies in the form of joint stock or limited liability companies depending on the nature of their activities. In case of establishment as a joint stock corporation, shares of the company must be registered shares.

Certain of the market activities elaborated below are especially significant as they reveal the private and public sector shares in the market:

#### *1. Generation Activities*

Generation activity is defined in the EML as the conversion of energy sources into electricity energy at generation plants. Generation Corp. is the public entity entitled to operate in the generation activity and may establish, rent or operate generation facilities in accordance with generation capacity projections approved by the Electricity Market Regulatory Board ("Board").

Private law companies are authorized to operate in generation activities by means of ownership, financial leasing or transfer of operational rights. However, market share of private law companies in generation is limited to 10% of Turkey's total electricity energy generation published for the previous year.

#### *2. Transmission Activities*

Transmission constitutes the only market activity not open to private sector, subject to the monopoly of the Transmission Corp.. Transmission Corp. is responsible for the operation of the national transmission system and its development in line with market needs and new trading methods and purchasing channels for the efficient operation of the market.

The involvement of private companies in this market activity is allowed only in the case of the instalment of private direct transmission lines for the purpose of encouraging the consummation of electricity at the place of generation, subject to transmission control agreements to be entered into between private companies and the Transmission Corp. and provisions of licenses.

#### *3. Distribution Activities*

EML stipulates the distribution activities to be conducted by distribution companies entitled to operate in distribution regions indicated in their licenses. Distribution companies are required to realize the innovation, substitution and capacity increase investments with respect to their distribution facilities and to render distribution and connection services to all system users. Conditional on meeting the criteria set forth in the EML and by obtaining a separate licence, distribution companies may also be engaged in retail sale of energy to consumers.

#### **4. Wholesale of electricity**

Wholesale of electricity is defined in the EML as the sale of electricity energy for the purpose of resale and includes the wholesale, export, import and sale to consumers of electricity energy. Trade Corp. is recognized as the public entity authorised to operate in this market activity. This corporation is furnished with the authority to perform and terminate energy sales agreements taken over from TEAS and execute new energy purchase agreements with generation companies for a maximum term of one year.

The private companies' share in the wholesale activities is limited to 10 % of the total electricity energy consumed in the previous year.

#### ***D. Electricity Market Regulatory Agency***

In conformity with the international commitments of Turkey, EML introduces an independent regulatory authority for the inspection, supervision and regulation of the electricity market. The Agency is an independent public legal entity having administrative and financial autonomy, affiliated with the MENR only with respect to administrative issues.

The Board constitutes the executive and representative body of the Agency and is imposed with significant duties and powers in order to secure the proper functioning of the market, certain of which may be listed as follows:

- regulation and implementation of standards and rules providing competition and coordination in the sector and ensuring equity, transparency and stability among market participants
- establishment and maintenance of the legislative framework for the generation of energy at low costs,
- grant of, amendment to and cancellation of licenses,
- approval of tariffs set forth in the EML and amendments and adjustments thereto,
- application of sanctions and monetary punishments in case of breach of the regulations stipulated in the legislation and the obligations set forth in the licenses.

#### ***E. UT Guarantees***

Another crucial innovation brought by the new electricity market pertains to the removal of the UT Guarantees to be granted in relation to power projects. Considering the major burden such guarantees create on the UT and taking into account that state guarantees will not be of significance for investors in a liberal market, the UT guarantee has been removed in principle. However, in accordance

with the agreement of UT and the World Bank, UT Guarantees will still be provided to certain BOT projects (i.e., 29 projects determined by the Undersecretariat of State Planning Organization and the MENR) which have undertaken to be commissioned by 2002 for the purpose of meeting the country's energy deficit, on condition that these private law companies do not fail to meet this time schedule.

#### **V. Conclusion**

As indicated in the foregoing sections, the need for electricity energy in Turkey has forced the country to often amend and develop the legal framework regarding the energy sector. Changing principles and schemes of the power sector have prepared the current environment which finally permits the launch of the new liberal electricity market regime. With the operation of the new electricity market, many characteristics of the current legal framework regulating the power sector shall be altered immensely. Turkey now faces an entire new phase during which many pieces of innovative legislation governing the new market shall have to be put in place. The enactment and application of such legislation may give rise to certain new issues and implications to be elucidated. At any rate, the power sector remains to constitute a striking example of the advancement Turkey has encountered, by the transformation of the energy market from a field subject to absolute public monopoly to a liberal and competitive market governed by private law principles.

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