Global tax guide to doing business in Turkey

Overview

The Turkish direct taxation system consists of income tax and corporate income tax, which are enacted in the Income Tax Law number 193 and the Corporate Income Tax Law number 5520.

Turkish residents are subject to income tax on their worldwide income. An individual whose domicile is in Turkey or any person who remains in Turkey more than six months in one calendar year is deemed to be a resident of Turkey.

Companies whose legal or business headquarters are located in Turkey are subject to corporate tax on their worldwide income; described as full liability taxpayers in the legislation. Limited liability taxpayers whose legal and business headquarters are not located in Turkey are taxed on their income derived in Turkey.

Turkey also imposes 15% withholding tax on dividends, 20% on professional services and royalty payments made to non-residents. Turkey has an extensive double taxation treaty (DTT) network that will reduce local withholding tax rate on such types of income.

Turkey is a signatory to the Multilateral Convention to Implement Tax Treaty Related Measurs to Prevent Base Erosion and Profit Shifting (MLI) and has agreed to adopt the minimum standards as well as certain optional provisions. The ratification process has not yet been completed.

In addition to direct taxes, the Turkish taxation system includes indirect taxes such as value added tax, special consumption tax, banking and insurance transactions tax, special communication tax, stamp tax, customs tariff and fees.

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Legal system

Turkey operates under a civil law legal system, which is largely based on continental European models. The legal framework of Turkey is based on the dual separation of public and private law. The sole authority to enact laws belongs to the Grand National Assembly of Turkey. The judicial system of Turkey is a three-tier system that includes First Instance Courts, Regional Courts of Appeal and the Supreme Court.

Taxation authorities

In Turkey, taxation authorities are separated into two main heads as Revenue Administration and Tax Inspection Board. These two authorities are placed under the Turkish Republic Ministry of Treasury and Finance in the organizational chart of Turkey's administrative system. The Tax Inspection Board has the responsibility for carrying out inspections by its tax inspectors for the taxpayers, whereas the Revenue Administration is responsible for levying and collecting taxes through tax offices.

Business vehicles

According to Foreign Direct Investment Law No. 4875 and in line with Turkish Commercial Code No. 6102, foreign investors are entitled to establish joint stock companies, limited liability companies as well as branches and liaison offices in Turkey.

Joint stock companies & limited liability companies

A minimum of one (1) shareholder and TL 50,000 of capital is required to establish a joint stock company. Limited liability companies shall also have minimum one (1) shareholder but shall be established with a minimum capital of TL 10,000.

Both entities are corporate taxpayers in Turkey.

Due to the favorable position concerning the liabilities borne by shareholders, joint stock companies and limited liability companies are the business vehicles in Turkey most commonly chosen by foreign investors, along with the other business setup forms of branch offices and liaison offices. These two types of companies, joint stock companies and limited liability companies are the ones, for which the shareholders are not held liable for the debts of the company in terms of their personal assets.

For limited liability companies, if the tax receivables cannot be wholly or partially collected from the company itself, or it is apparent that the public receivables will not be collected from company, the liability of the shareholders and/or legal representative arises.

Branch

Foreign investors are also entitled to establish a branch in Turkey in order to engage in activities within Turkey, as per the Turkish Commercial Code and the Trade Registry Regulation. Unlike joint stock companies and limited liability companies, branches may be incorporated only for the same purposes as the parent company; therefore branches shall not have a separate Articles of Association. There is no minimum capital requirement for branches but branches may have a separate capital, which may be allocated by the parent company. Turkish citizen and foreigners can be appointed as branch managers; however, it is required that they reside in Turkey.

Branches are liable for all taxes such as corporate income tax, value added tax, withholding tax and stamp duty once they are registered for tax purposes in Turkey. Branches are treated as non-resident limited liability companies for tax purposes and only profits generated in Turkey are subject to corporate tax at the rate of 22%. The branch profit transferred to headquarters is subject to dividend withholding tax at a rate of 15%, which might be reduced if there is an available DTT between Turkey and the country of which the principal is a resident for income tax purposes.

Liaison office

Foreign entities may prefer to establish a liaison office in Turkey to represent parent companies' business activities and to gather necessary information on the related sector and the country on behalf of the parent company, which is a practical way to enter the Turkish market. The Ministry of Trade is authorized to permit foreign companies established under the laws of foreign countries to establish liaison offices to carry out the activities indicated under the Regulation of the Implementation of Foreign Direct Investment Law, provided that they do not engage in commercial activities in

Turkey. The Ministry must be convinced with supporting documents that the operations of the prospective liaison office actually fall under the accepted categories. These activities are as follows: market research, promotion of the goods and services of the parent company, representation and hosting, control of the suppliers in Turkey, technical support, communication and information transfer and regional management center etc. In addition, there is no foreign capital requirement in establishing a liaison office.

Even if the Law and Communiqué prohibit liaison offices from engaging in any profit or expense-generating activities, tax liability of the liaison office will arise in case liaison office performs commercial activities contrarily to the permission. In case of engaging in commercial activities, the liaison office will be taxed in accordance with legislation on the limited liability taxpayer.

Financing a corporate subsidiary

Equity financing

Capital increase

The share capital of joint stock companies/limited companies may be increased either by issuing new shares or by increasing the value of each share.

“Notional interest deduction” has been in effect for cash capital increases effective since July 1, 2015. Turkish capital corporations (except for those that operate in finance, banking and insurance sectors) will be able to deduct 50% of the interest to be calculated over cash capital increase amounts which are registered in the Turkish Trade Registry or the interest calculated over the cash capital contributions of the newly established corporations, from their taxable income.

Debt financing

Thin capitalization

If the ratio of the borrowings from the shareholders or from the persons related to the shareholders exceeds three times the shareholders’ equity of the borrower company at any time within the relevant year, the exceeding portion of the borrowing will be considered as disguised capital. For borrowings from related parties that are banks or financial institutions, half of the borrowings are taken into consideration in the calculation for disguised capital.

Interest paid or accounted for and foreign-exchange differences related to disguised capital are regarded as non-deductible expenses in determining the corporate tax base. Interest related to disguised capital is treated as a dividend distribution and is subject to dividend withholding tax.

Withholding tax implications

Interest payments made to non-resident entities are subject to withholding tax at rates 0%-10%. The withholding tax rates might be reduced under an applicable DTT.

Resource utilization support fund (RUSF)

Foreign exchange and gold borrowings provided to Turkish residents (banks and financing institutions are exempt) from abroad are subject to RUSF depending on the maturity.

RUSF rates on foreign currency denominated loans are as follows:

Average Maturity	Rate
Up to 1 year	0%
1 year (including 1 year) to 2 years	0.5%
2 years (including 2 years) to 3 years	1%
3 years (including 3 years) and above	3%

RUSF rates on Turkish lira (TL) denominated loans are as follows:

Average Maturity	Rate

Average Maturity	Rate
Up to 1 year	1%
1 year (including 1 year) and above	0%

Stamp tax

Documents in relation to the loans extended by banks, foreign credit institutions and international institutions, their securities, repayments, transfers and assignment of the receivables that stem from the loan and the annotations established on these documents (excluding the use of the loans) are exempt from stamp tax.

Corporate income tax

Income tax rate

Companies whose legal or business headquarters are located in Turkey or whose operations are centered and managed in Turkey are subject to corporate tax on their worldwide income.

The corporate tax rate is 22% for 2020.

Capital gains

Capital gains derived by all companies are included in ordinary income and subject to corporate tax.

75% of capital gains derived by corporate taxpayers from the sale of shares and 50% of capital gains derived by corporate taxpayers from the sale of immovable property owned by for at least two (2) years are exempt from corporate tax provided that the gains from the sale are kept in a special account until the end of the fifth year following the year of sale.

Capital gains derived from the sale of foreign participations that have been held for at least two years by a holding company resident in Turkey are exempt from corporate tax subject to certain conditions.

Branch tax

Branches are taxed solely on the income derived from activities in Turkey since they are regarded as non-resident entities for Turkish purposes. Branch profits are subject to Turkish corporate income tax at the rate of 22% for 2020.

The branch profit transferred to headquarters is subject to dividend withholding tax at a rate of 15%, which might be reduced under an applicable DTT.

Computation of taxable income

Taxable base

The corporate tax base is determined by deducting expenses from the revenue of a company.

Deductions

All business related expenses are deductible. Some of the exceptions listed in the legislation are:

i. Interest on shareholders' equity or on advances from shareholders
ii. Interest, foreign-exchange differences or similar expenses calculated or paid on disguised capital
iii. Disguised profit distribution through transfer pricing
iv. Reserves set aside from profits
v. Corporate tax, all fines, tax loss penalties and interest imposed on such tax
vi. Discounts or other losses arising from selling the company's own securities for less than par value

Income tax reporting

Resident and non-resident entities having a permanent establishment in Turkey are obliged to file annual corporate income tax and quarterly advance corporate income tax returns (on a calendar year basis unless permission to the contrary is specifically obtained from the Ministry of Treasury and Finance). The last date of submission of the corporate income tax return is the 25th of the fourth month following the fiscal year end. The advance tax return should be submitted at the latest by the 14th of the second month following the quarter period. Advance corporate tax is offset against the final corporate tax calculated in the annual tax return.

Turkey does not allow for tax consolidation; each company in a group must file its own corporate tax return.

Cross border payments

Transfer pricing

The transfer pricing regulations in Turkey that include the arm's length principle and the requirement for documentation of related party transactions are set out in the Corporate Tax Law in parallel with the Organisation for Economic Co-operation and Development (OECD) guidelines. Three-tier transfer pricing documentation including master file, local file and country-by-country reporting was adopted on February 25, 2020.

The main methods that can be used by the taxpayers in the determination of the arm's length price are (i) comparable uncontrolled method, (ii) cost plus method, (iii) resale price method, (iv) profit split method and (v) transactional net margin method.

It is possible to enter into advance pricing agreements with the tax authorities.

Withholding tax on payments made to non-residents

Resident companies in Turkey are obliged to apply withholding tax upon certain types of payments made to non-residents.

Type of Payment	Local Rate
Dividend	15%
Royalty	20%
Professional Fees	20%
Interest on Loans	0%-10%

These rates might be reduced under an applicable DTT.

Withholding tax at 15% on online advertising services provided by non-residents has been effective since January 2019.

Payroll taxes

Income tax

The employer must withhold income tax on salaries at progressive income tax rates ranging from 15% to 35%.

Social security contributions

Social security premiums, which are calculated on salary limits of a minimum of TL 2,943 and an upper limit of TL 22,072.50 monthly between January 1, 2020 and December 31, 2020, are paid monthly by the employer and the employee at rates defined according to labor categories. Premiums are calculated as a percentage of gross salary based on a range and for Turkish nationals, the general rates are 20.5% for the employer and 14% for the employee.

Unemployment insurance

The employer is required to deduct the unemployment premiums and declare these along with the social security premium contributions on a monthly basis. The rates are 2% for the employer and 1% for the employee.

Indirect taxes

Value-added tax (VAT)

The deliveries and services performed in Turkey within the scope of commercial, industrial, agricultural and self-employment activities and importation of goods and services to Turkey are subject to VAT. The general VAT rate is 18%, whereas the reduced rates range from 1% (e.g., newspapers and magazines -except online sales-, houses with a net area of up to 150m2 and livestock) to 8% (e.g., plastic and plastic made products, books (except e-books), cotton, fibers, leather and processed goods) depends on the delivery of certain types of goods and services.

Taxpayers offset input VAT paid for purchases against the output VAT collected through sales. If input VAT exceeds the output VAT, the balance is not refunded (unless there is a special delivery which enables a VAT refund, such as export exemption) but carried forward to the following months to be offset against future output VAT. There is no time limitation for such VAT carry forwards.

Special consumption tax (SCT)

SCT is an expenditure tax levied on certain goods and services. SCT is applied as either an exact value or a certain ratio and charged only once, which is taken at the stage of manufacture, import or first acquisition.

Four main products lists that fall within the scope of SCT are:

i. *List I*: Petroleum products, aviation gasoline, unleaded gasoline, diesel oil, jet fuel, distillate marine fuels, hydraulic oil, etc.
ii. *List II*: Automobiles, motorcycles, tow trucks for semi-trailers, bus, minibus, special purpose motor vehicle, excursion ship, cruise ship, etc.
iii. *List III* : Tobacco products, cigarettes, cigars and alcohol products, cola drink, soft drinks, soda water, fizzy drinks, sparkling wines, alcohol-free beers, etc.
iv. *List IV*: other consumption goods (caviar, furs, cosmetic products, glassware, small home appliances, microphones, speakers, guns, armaments, white goods and other electrical household machines etc.).

Stamp tax

Stamp tax is applied to a wide range of documents, including but not limited to, agreements, deeds of assignment, deeds of undertaking, and payrolls. There are two types of stamp tax, proportional stamp tax and fixed stamp tax. The proportional stamp tax rates vary between 0.189% and 0.948% depending on the type of the document with an overall cap of TL 3,239,556.40 (for 2020).

Real estate tax

Buildings and land owned in Turkey are subject to real estate tax on the tax value of the property at varying rates between 0.1% and 0.6% depending on the classification of the property. The property tax is payable annually, in two installments in March to May and November.

Title deed

The title deed is payable on transfer of immovable and equally paid by the buyer and the seller as 2% of the sale price.

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