



cutting through complexity™

Investment in Turkey

March 2012

kpmg.com.tr

kpmgvergi.com



Contents

1. Preface	5
2. Country Profile	6
2.1 General Information	6
2.2 Economy and Currency	8
2.3 Employment Conditions	10
3. Opportunities for International Investors	11
3.1 Incentives for International Investors	11
3.2. Investment Incentive Regime	11
3.3 Incentives in Distressed Regions	14
3.4 Research and Development Incentives	14
3.5 Incentives for Technology Development Zones	15
3.6 Incentives for Free Trade Zones	16
3.7 Attitudes towards Foreign Investment	16
3.8 Local Banking System and Sources of Finance for Commerce and Industry	17
4. Foreign Trade & Customs	18
4.1 Foreign Trade Legislation	18
4.2 Customs Regimes and Synopsis of Customs Transactions	18
4.3 Turkey and the EU	19
4.4 Turkish Import Regime	20
4.5 Customs Valuation	20
4.6 Anti-Dumping and Anti-Subsidy Practices	20
4.7 Resource Utilization Support Fund (RUSF)	20
5. Company Law Requirements	21
5.1 Available Corporate Structures	21
5.2 Joint Stock Corporations and Limited Liability Companies	21
5.3 Limited Liability Company	22
5.4 Joint Stock Corporation	24
5.5 Other Forms of Doing Business in Turkey	27
5.6 Forms of Doing Business Other Than Through Branches or Subsidiaries	29
5.7 The New Turkish Commercial Code	30

Contents

6. Corporate Taxation	37
6.1 Taxes on Corporate Income	37
6.2 Allowable Deductions	39
6.3 Non-allowable Deductions	41
6.4 Exclusions from Income	42
6.5 Corporate Taxation	45
6.6 Effects of Law No: 6111 (Tax Amnesty Law) from a Corporate Tax Perspective	49
6.7. International Corporate Taxation	49
7. Transfer Pricing Regulations	55
7.1. Arm's Length Principle	55
7.2. Documentation Requirements	56
7.3. Advance Pricing Agreements (APA)	58
8. Indirect Taxation	59
8.1 Value Added Tax	59
8.2. Special Consumption Tax	63
9. Income Tax on Individuals	64
9.1 Taxable Income	64
9.2 Income Tax Rates	66
10. Labour	68
10.1 Labour Legislation	68
10.2 Labour Costs	72
10.3 Social Insurance - Health Insurance	72
10.4 Rules applicable to expatriates	74
10.5 Collective Agreements - Trade Union Rights	75
11. Mergers, Acquisitions and Reorganizations	77
11.1 Mergers	77
11.2 Acquisitions of Companies	78
11.3 Corporate Reorganizations	82
12. Appendicies	84
12.1 Appendix I: Chart of Principal Turkish Taxes	84
12.2 Appendix II: Chart of Withholding Tax	85
12.3 Appendix III: Computation of taxes on the year-end profits	86
12.4 Appendix IV: Turkish Withholding Taxes by Treaty Countries	88

1. Preface



This publication "Investment in Turkey - March 2012", compiled by KPMG Turkey's Tax Practice, aims to provide general outline of the Turkish tax environment in which foreign investors consider investing and doing business in Turkey.

It reflects developments to March 2012 and the information herein is not exhaustive and should be read as indicating one. Therefore, the information should not be perceived as the sole basis for investment decisions in Turkey.

The information contained in this publication is an introduction for the foreign investors that plan to take a look into tax and business environment in Turkey. Detailed advice in tax, accounting, legal and other matters should be sought from professional advisers.

I would like to take this opportunity to thank to KPMG Turkey Tax Professionals as the authors of this booklet.

Abdulkadir Kahraman
Head of Tax,
Tax Partner

2. Country Profile

2.1 General Information

Geography and Climate

Turkey is situated at the junction of Europe and Asia. The European part of the country is called Thrace (Trakya) and the Asian part is named Anatolia (Anadolu). The location on two continents has been a central feature of the Turkish history, culture and politics. The country shares borders with Greece and Bulgaria to the northwest, with Georgia and Armenia, and Iran to the east, Iraq and Syria to the south. The Black Sea to the north, the Aegean Sea to the west, and the Mediterranean Sea to the south are connected by the Bosphorus, the Sea of Marmara and the Dardanelles, a water way known as the Turkish Straits.

The climate of coastal regions shows features of a transition between a Mediterranean and Black Sea climate. Summers tend to be hot and dry except the Black Sea coast. While spring and fall are warm and temperate, winters are cold, but the number of snowy days is few.

The inner land is more snowy and cold in winter. The coldest months are January and February and hottest July and August.

History and Government

The Republic of Turkey was established in 1923. The new Republic looked to the West for industrialization and the establishment of a secular political system under the guidance of the new Republic's first President Mustafa Kemal Atatürk whose reforms constituted the framework for the development of the modern Turkish Republic. Turkey has enjoyed multi-party politics since 1946.

Turkey is a unitary parliamentary republic. The Grand National Assembly has 550 members elected for four years term, by secret ballot. The executive branch is the Government, headed by the Prime Minister. The President is elected by the Parliament for a four years term. The Prime Minister, who is appointed by the President, nominates the other members of the cabinet, which is approved by the President, and is subject to a parliamentary vote of confidence.

The judiciary is independent of both the legislature and the executive. The legal system is largely based on continental European models. A Constitutional Court is also entitled to cancel legislation passed by the Parliament. It can cancel those laws, or parts of them, which it decides to be incompatible with the Constitution.

Foreign Relations of Turkey

Accession Negotiations have been launched on October 3, 2005 with the adoption of the Negotiation Framework by the Council of the European Union. Turkey and European Union's relations are covering with 3 elements. These are; application of Copenhagen Criteria's, application of EU acquis and strengthen of civil society dialogue¹. According to the basis, negotiations are keeping up with European Union.

Population and Language

The population of Turkey

According to the Population Services Law No. 5490 acted in 2006, new population registration system, which will be the main data source of population censuses, was established in the country. The results of the census states that the population is approximately 74.724.269 as of 31.12.2011².

Proportion of population living in cities is 76,8%

City population (population living in province and district centers) is 57.385.706 and village population (population living in sub-districts and villages) is 17.338.563. The proportion of city population is the highest with 99 % in Istanbul and it is the lowest with 35 % in Ardahan².

Proportion of the population living in Istanbul is 18,2 %

The number of people living in Istanbul is 13.624.240. Most populated provinces are Ankara with 6,6 %, Izmir with 5,3 %, Bursa with 3,6 % and Adana with 2,8 %, respectively. Population size of Bayburt as the least populated province in Turkey is 76.724².

¹ www.abgs.gov.tr

² www.tuik.gov.tr

The half of population is below age 29,7 in Turkey

The median age of the population in Turkey is 29,7. While the median age is 29,1 for males, it is 30,3 for females. The median age of the city population is 29,5, that of the village population is 30,5².

Proportion of the population at ages between 15 and 64 is 67,4 %

Persons at 15-64 age groups which are the working ages constitute 67,4 % of the total population. Proportion of population of Turkey for age group 0-14 is 25, 3 % and it is 7,3% for age group 65 and over².

Language

The official language of Turkey is Turkish. Besides Turkish, a significant part of young generation speaks English or German as a foreign language.

2.2 Economy and Currency

Economy

Turkey experienced a remarkable rate of growth after 1980's. This had been attributed to three factors, namely a shift from agriculture towards industry and service activities, the modernization of the existing industry and technology transfer, and the effect of international trade and competition.

Turkey's GDP current prices and growth rates of GDP are as follows³:

Years	GDP Current Prices (Million TL)	Growth Rate (%)
2005	648,932	16.1
2006	758,391	16.9
2007	843,178	11.2
2008	950,534	12.7
2009	952,635	0.2
2010	1,103,750	15.9

Private investments were the driving force in accelerating economic activities in recent years. The liberalization of capital movements and the willingness of foreign creditors to lend to Turkish investors contributed to the high growth rate of private investment.

Turkey attaches a high priority to the encouragement of foreign investment and provides a variety of incentives.

²⁻³ www.tuik.gov.tr

Currency

The Turkish currency is called Turkish Lira (TL 1), which was introduced, instead of New Turkish Lira as from 1 January 2009. In addition, six digits were dropped from Turkish Lira denominations as from 1 January 2005. On the other hand, together with the TL, Kurush (Kr), which is a hundredth of TL 1, has become in use again as from 1 January 2005.

The Turkish Central Bank has issued notes of TL 1, TL 5, TL 10, TL 20, TL 50, TL 100 and TL 200. There are also coins in circulation in denomination TL 1, Kr 50, Kr 25, Kr 10, Kr 5 and Kr 1.

The following table shows the Central Bank exchange rate of Turkish Lira, to other major currencies as of 31 December 2011.

Country	Currency	TL value ⁴
US	1 USD	1.8889
Euro	1 €	2.4438
Great Britain	1 Pound Sterling	2.9170
Switzerland	1 Swiss Franc	2.0062
Japan	100 Japanese Yen	2.4340

Inflation

Turkish economy has experienced high inflation rates for more than a decade, but there has been significant improvement in reducing the inflation rates under the stabilization program run since 2001. The following table shows the inflation rates of past 5 years⁵:

Years	Producer Price Index (Annual%)	Consumer Price Index (Annual%)
2006	11.58	9.65
2007	5.94	8.39
2008	8.11	10.06
2009	5.93	6.53
2010	8.87	6.40
2011	13.33	10.45

⁴ www.tcmb.gov.tr

⁵ www.tuik.gov.tr

2.3 Employment Conditions

Residence and Work Permits

Most foreigners enter Turkey without a Visa and they can stay in the country up to 3 months. In cases where a visa is required, it may be obtained at the airports. A foreign individual sent by a foreign company to carry out business on its behalf in Turkey has to obtain a work permit from the Ministry of Social Security and Labour Affairs and a work visa from the Turkish consulate.

Then with this work permit he should apply for the residence permit to the Foreigners Office of Police Department.

Opening Hours

Office hours of bigger companies are from Monday to Friday from 8:30 am to 5:30 pm. Shopping hours are basically from Monday to Saturday from 9:00 am to 7:30 pm. However, on Sunday some have shopping hours. Government institutions do not have office hours on weekends. The banks are open till 5:00 pm from Monday to Friday. Automatic teller machines are widespread all over Turkey.

Cost of Living and Housing

Living in Turkey is not expensive for the foreigners from EU and USA. Housing, except in certain locations, and the cost of living is cheaper than their home countries.

Turkish Economy - Fiscal and Monetary Policy

Turkey is being faced with the public sector financing problem in last decades. As the State Economic Enterprises (SEE) has vital importance in the economy, governments had to spend much in this sector. Beside that, payments for huge infrastructure investments and the smaller ratio of the government revenues to GNP has caused to larger public sector borrowing. The foreign and domestic borrowing of government had an increasing tendency in relation with that high inflation had been aroused. There is also a big portion of revenues, which is untaxed because they are not a part of registered, and from unrecorded activities. In order to deal with those problems, the efforts have been given to diminish the public finance deficit resulting from SEE. The privatization for some of them is now on the stage. Government has also issued new taxation measures especially for untaxed revenues, and measures aimed at preventing money laundering.

3. Opportunities for International Investors

3.1 Incentives for International Investors

Turkey has been restructuring its economy since 1980 along the lines of a more liberal economic policy. In this context more emphasis is being placed on private sector especially in productive sectors of economy and the role of State is limited to infrastructure development and provision of public services. The new economic policy aims to diminish the unemployment, to realize the technology transfers, to privatize State Economic Enterprises, to overcome the deficit in the balance of payments and especially to increase the integration of the economy with the world economy and to attract more foreign capital to the Country. Turkey also uses the option of fiscal incentives to channelize domestic and foreign investments for industrial development and rural-urban integration. These incentives or tax expenditures are usually available to the investors for the promotion of private investment activities in selected sectors/regions depending on the scale of investment and in the following forms:

3.2. Investment Incentive Regime

The objective of the incentives is to encourage exports, high technology, increase competitiveness of the investments and employment, continuity of investment tendency and provide sustainable development.

Type of investments

- **Regional and sector-based investments:** Turkey is separated into four zones based on the development level of the regions in these zones. The first two zones represent the most and more developed regions where as the 3rd and the 4th zones are less and the least developed zones in Turkey.
- **Large scale investments:** Investments in excess of 50 million TL but such amount can increases/varies depending on the industry of the investment.
- **Other investments:** Investments which do not qualify either as a regional investment or a large scale investment.

Investment incentives:

Investment incentives are available to the investors through an "Investment Incentive Certificate" ("IIC"), which is obtained from the General Directorate of Incentive Application and Foreign Capital under the Ministry of Economy ("Authority").

In order for an investment to be granted an IIC, the minimum investment amounts in these four zones should be 1.000.000 TL and 500.000 TL for the first two and the last two zones respectively. And also any investment fulfilling the minimum investment amounts above are subject to the evaluation of the Authority.

Any qualifying investment can benefit from the below investments based on the properties of the investment.

General Incentives:

- Customs duty exemption
 - Value Added Tax (“VAT”) exemption

Special incentives:

- Reduced rate Corporate Income Tax
 - Social Security Employer premium contribution
 - Interest support on the financing
 - Allocation of Land



General Incentives:

- **Customs duty exemption:** 100 % customs duty exemption is available on the imported machinery and equipment (unless the originating country is an EU country).
- **Value Added Tax (“VAT”) exemption:** 100% Value Added Tax (“VAT”) exemption for both locally purchased or imported machinery and equipment for the eligible projects (Under the VAT Code, importation of machinery and equipment under an investment certificate is not subject to VAT, as well as local purchases of machinery and equipment).

Special Incentives:

Special incentives are provided to the regional investments and to large scale investments (i.e. investments in excess of 50.000.000 TL but such amount increases/varies depending on the industry of the investment) in addition to the General investments.

- **Reduced rate Corporate Income Taxes:** Statutory corporate tax rate is 20%. Corporate tax rates are applied as follows for the eligible investments in these four zones and for the large scale investments between 2% to 10% for the investments started after 31 December 2011 limited to an investment contribution amount calculated based on the contribution rates set forth in the legislation.
- **Social Security Employer premium contribution:** Social Security employer premium contribution for up to 5 years based on the zone(location) of the investment, limited to the premiums applicable to a minimum wage ceiling. The incentive amount is also limited to a percentage of the actual investment amount which should be checked for each investment project eligible for this incentive.
- **Interest support on the financing:** This incentive is applicable for the investments in 3rd and 4th regions. The total interest support for these investments amount up to 500.000 TL.
- **Allocation of Land:** Land can be provided to the investors as a right of easement or usage right for 49 years by the Ministry of Finance.

3.3 Incentives in Distressed Regions

Businesses initiated in certain distressed regions are granted certain tax incentives provided that such business is demonstrated to generate at least 10 new or current employments.

Incentives are as follows:

- Up to 100% of income withholding tax limited to the tax applicable to minimum wage ceiling per an employee until 31 December 2012 (Only the new investments those are completed as of 31.12.2007, 31.12.2008 and 31.12.2009 can benefit)
- Up to 100% of social security employer contributions limited to the contribution applicable to minimum wage ceiling per an employee until 31 December 2012.
- Up to 50% of electricity energy costs based on the sector of the investment and the start date of the business until December 2012 (Only the new investments those are completed as of 31.12.2007, 31.12.2008 and 31.12.2009 can benefit)

The period during which the first 3 incentives to be enjoyed may not be less than 5 years for the new investments to be completed until 31 December 2007, 4 years for the new investments to be completed until 31 December 2008 and not be less than 3 years for the new investments to be completed until 31 December 2009.

3.4 Research and Development Incentives

Law No 5746 Pertaining the Support of Research and Development Activities has been enacted as of 01 April 2008. Basic incentives and supports set forth under the Law No 5746 for the R&D investment projects are as follows;

• R&D Allowance

- 100% of R&D and innovation expenditures are deductible from taxable profits provided that the companies making these expenditures are located in a R&D Centre and employ at least 50 R&D personnel.
- 100% of research and development expenditures incurred for eligible projects those which are oriented to new technology and knowledge research are deductible from taxable profits provided that the number of researchers exceeds 500. An extra allowance at half portion of the increase in R&D and innovation expenditures compared to the previous year's expenditures is provided to the taxpayers.

The amount, which cannot be deducted in the relevant period due to the lack of taxable profit, is carried forward to the following fiscal periods.

• **Income Tax Incentives**

The salaries of R&D and support personnel are exempt from income tax until 2013 at the following portions under certain conditions:

- 90% exemption for the employees having a PHD,
- 80% exemption for other employees.

• **Social Security Premium Incentives**

50% of the employer's contribution of social security premiums is supported for five years for each R&D and support personnel. The incentive will be financed by the Ministry of Finance.

• **Technological Enterprise Capital Subsidy**

A capital subsidy of up to 100.000 TL would solely be given once without requesting any guarantee to business ideas of university and college graduates focusing on technology and innovation.

• **Stamp Duty Exemption**

All documents made out regarding R&D and innovation facilities within the scope of the Law No 5746 are exempt from Stamp Tax.

3.5 Incentives for Technology Development Zones

- Income derived from software and research & development(R&D) activities in technology developing zones by the taxpayers doing business in these zones are exempt from income and corporate tax until 31 December 2023.
- Wages of researcher, software programmer and research & development personnel related to these jobs in these zones are exempt from income tax and stamp tax until 31 December 2023.
- 50% of the employer's contribution of social security premiums is supported for five years for each R&D and support personnel.
- Delivery of goods and services which are produced exclusively in these zones and in the form of system management, data management, business applications, sectoral, internet, mobile and military command control application software are also exempt from VAT until 31 December 2023.

3.6 Incentives for Free Trade Zones

With the new amendment made by Law No. 5810, the following incentives come into effect by 01.01.2009 which are applicable until the end of the fiscal year in which Turkey fully accesses to the EU:

- The income derived from the sale of goods manufactured by the license holders in the Free Trade Zones is exempted from corporate income tax.
- Moreover, income derived by the license holders having a valid license obtained before 06.02.2004 can also benefit from corporate tax exemption until the expiration date of their licenses.
- Corporate income tax exemption does not cover the dividend distributions. Dividends of a company in Free Trade Zones are subject to dividend withholding tax at the standard rate of 15% at source when they are paid to an individual shareholder (resident or non-resident) or to non-resident corporations.
- The salary payments made by taxpayers operating in Free Zones to employees are exempted from Income Tax, provided that the taxpayers export at least 85% FOB values of annually produced goods. It should be noted that Council of Ministers is authorized to decrease this rate down to 50%.
- The documents and transactions regarding the operations in Free Zones are exempted from stamp tax and charges.

In addition to the above incentives, the delivery of goods and performance of services in free trade zones are excluded from VAT under VAT Code without any time limitation.

3.7 Attitudes towards Foreign Investment

Business Regulations

In principle, all fields of business, which are open to the Turkish private sector, are also open to foreign participation investments. Any business, factory, trade, tourism, or industrial establishment, either Turkish or foreign, must notify the respective local administration and tax authorities prior to commencing its activities. Recently, anti-trust regulations have also started to play a role to provide a fair competition. The regulations on intellectual property rights have also been revised to increase protection of such rights. Foreign Direct Investments Law provides the comfort that foreign investors cannot be discriminated.

Foreign Exchange Legislation

Turkey has a liberal foreign exchange regime, which allows local-foreign exchange accounts. Remittance of profits is guaranteed. To enable the transfer of the profit, approved tax statement, tax accrual and payment slips should be submitted. Provided that appropriate tax liabilities are fulfilled (like withholding tax), fees and royalties within the scope of management agreements, technical services agreements and license contracts can be remitted abroad. In addition to that, foreign investment partnerships and funds may invest in Turkish securities and freely remit dividends, interest, profit and capital. Moreover, Turkish resident companies are allowed to procure loans to group companies resident abroad. Please note that with the introduction of New Turkish Commercial Code, shareholders should not become indebted to the company as of 1 July 2012. It is expected that additional explanations will be made about the implementation of this restriction.

3.8 Local Banking System and Sources of Finance for Commerce and Industry

Central Bank of Turkey

The Central Bank issues money, serves as source of refinancing, clearing and collection to other financial institutions and as bank of the government. The Central Bank is independent of the government. It employs various measures to influence monetary conditions, including discount rate policy, minimum reserve requirements and open-market interventions.

Banking Institutions

Commercial and Saving banks, which account for the largest portion of the business volume, are active in most types of banking operations. They grant short-term loans and credit lines, medium and long-term loans, underwrite, issue, and trade in securities for customers and on their own account. They are also allowed to own shares and participation in other industries. Development and Investment Banks serve to finance the big investments and infrastructure constructions. Specialized banks provide services in special forms in their area of interest such as mining, dwelling constructions, etc. The Banking Law has also established a special institution called as Institution on the Regulating and Supervision of Banking (BDDK) which has vast authorities to regulate and supervise the banking industry and to implement the measures to the savings and efficient operation of the banking system.

4. Foreign Trade & Customs

4.1 Foreign Trade Legislation

Some of the applicable laws that regulate foreign trade activities are:

- Customs Law numbered 4458,
- Import Regime Decree,
- Export Regime Decree,
- Law on the Prevention of Unfair Competition in Imports No: 3577,
- Decree on the regime of technical regulations and standardization,
- Free Trade Zone Law numbered 3218,
- Combating with Smuggling Law numbered 5607,
- Value Added Tax Law numbered 3065,
- Special Consumption Tax Law numbered 4760,

4.2 Customs Regimes and Synopsis of Customs Transactions

In Turkish Customs Legislation, there exist 8 customs regimes which are:

- Release For Free Circulation Regime,
- Transit Regime,
- Customs Warehousing Regime,
- Inward Processing Regime,
- Processing Under Customs Control Regime,
- Temporary Admission Regime,
- Outward Processing Regime,
- Exportation Regime.

Established companies with a valid tax number can perform importation/exportation. After a customs declaration is submitted by customs broker, computer system evaluates the data and designates a line for the transaction. Basically, there are four lines:

- Red line (means physical control),
- Yellow line (means document control),
- Blue line (means deferred control i.e. simplified procedure)
- Green line (means no control).

Depending on the goods, their origin and regime some documents should be submitted for import customs clearance: commercial invoice, pro forma invoice (when final commercial invoice does not exist at the time of entry), A.TR if applicable, depending on the consignment freight and/or insurance invoice, Certificate of Origin if applicable, Value Declaration Form, Packing List, Inspection/Control/Surveillance Certificate etc. (if importation is subject to certification).

Some of the documents that should be submitted for export customs clearance are: commercial invoice, A.TR if applicable, packing list etc. Customs Code Article 60 and Customs Regulation Article 114 provide more details about documents that should be attached to customs declarations. Specifications related to customs duty, excise duty and documentations such as required certificates are designated according to HS number of product (12-digit code is used in Turkey).

4.3 Turkey and the EU

After the EU Turkey Association Agreement of 1963, Turkey signed a Customs Union agreement with the EU in 1995 which seeks to promote trade and economic relations. Turkey is a candidate country to EU since 1999 and an accession country since 2005.

The EU and Turkey have a profound trade relationship. The EU ranks number one in both Turkey's imports and exports while Turkey ranks 7th in the EU's top import and 5th in export markets. Textiles, transport, machinery, equipment and agricultural products dominate EU imports from Turkey. Main EU exports to Turkey are machinery, transport material and chemical products (European Commission Trade, 2011).

The customs union is based on free circulation of goods and preferential treatment is applicable for industrial goods and processed agricultural goods (Customs Union between EU and Turkey doesn't cover agricultural goods, services and ECSC goods). According to Council Decision about Rules of Implementation Customs Union between Turkey and EC numbered 2006/10895, in order to enjoy preferential treatment goods should be delivered directly to Turkey with an A.TR Certificate (this is a movement certificate rather than a certificate of origin). But, if it is necessary to deliver over 3rd country, goods should be under customs observation of the country and it should be proved to Turkish Customs Authorities that the goods are not further processed in 3rd countries. The information and description of goods on the invoice and customs declaration should correspond with the information on the A.TR certificate (an A.TR certificate should be submitted to customs administration within 4 months and if it is issued retrospectively or it is duplicated, this should be indicated on the remarks section of the certificate).

4.4 Turkish Import Regime

The Import Regime reflects both Turkey's international rights and obligations and the country's economic needs. The Import Regime Decree is prepared every year, published in the official journal by December 31st and put into force by January 1st. Import Regime Decree indicates the rates of the customs duties separately for countries and country groups and the products are classified under six lists which are:

- Agricultural products (List: I)
- Industrial products (List: II)
- Processed agricultural products (List: III)
- Fish and fishery products (List: IV)
- Suspension list (List: V)
- List of goods used in civil aircraft eligible to relief from customs duties (List: VI)

4.5 Customs Valuation

The customs value of goods is determined to apply ad valorem rates of customs and excise duties i.e. VAT, SCT. Turkey accepted provisions of the WTO Agreement on Customs Valuation. Customs Valuation is regulated between articles 23 – 31 of Customs Law. The law primarily bases the customs value on the transaction value of imported goods which is the price actually paid or payable for the goods plus necessary adjustments of the import related costs and charges.

4.6 Anti-Dumping and Anti-Subsidy Practices

Ministry of Economy carries out dumping and subsidy investigations relating to unfair pricing practices of companies or countries exporting to Turkey. According to results of the investigation an anti-dumping duty or countervailing duty may be set up over goods of such companies or such countries.

4.7 Resource Utilization Support Fund (RUSF)

RUSF is applied on importation on credit basis and loans. There exit some exceptions such as importation with an incentive certificate. According to article 3/d of Council of Minister's Decree of RUSF numbered 88/12944 dated 12 May 1988, imports conducted through acceptance credits, letter of credit and payment against goods shall be subject RUSF calculated over the amount of importation. The current RUSF rate is 6% for importation on credit basis.

5. Company Law Requirements

5.1 Available Corporate Structures

A foreign company may perform business in Turkey in one of the following ways: Operate as a contractor, establish a branch or a subsidiary.

Establishment Procedures

Effective as from August 2003, the registration and foundation procedures relating to Turkish subsidiaries have been simplified and the requirement of obtaining permission of the Turkish Foreign Investment Department is no longer required.

Turkish subsidiary companies can be founded by way of registration with the local Trade Registry. Upon filing of the documents with the local Trade Registry as requested, it may take 2-3 days to finalize the establishment procedures.

However, establishment and change in the articles of association of some of the joint stock corporations, considering their scope of activity, may still require the approval of the Ministry of Industry and Commerce.

On the other hand, branch establishment in Turkey is subject to the permission of the Ministry of Industry and Commerce. Upon the permission of the Ministry, the branch can be registered with the local Trade Registry.

5.2 Joint Stock Corporations and Limited Liability Companies

The Joint Stock Corporation (Anonim Sirket, A.S.) and the limited liability company (Limited Sirket, Ltd.) are the most common forms of subsidiary companies under Turkish Commercial Law.

In the following businesses, the company structure is compulsory as a corporation (A.S.) by the related laws and decrees:

- Banking & Insurance,
- Reinsurance,
- Securities, Real Estate, and Venture Capital Investment Companies,
- Intermediary Institutions (Brokerage Houses),
- Financial Leasing, Factoring, Consumer Financing.

5.3 Limited Liability Company

Number of shareholders

A Limited Liability Company (Ltd) can be formed by at least 2 but no more than 50 persons. These shareholders may be individuals or corporate bodies, residents or non-residents.

Shareholders' liability

Liability of shareholders is in principle limited to the capital contributed to the Limited Liability Company. Nevertheless, shareholders of a limited liability company are responsible for tax and social security liabilities of the company, if it is in default and if tax office cannot collect outstanding taxes from the assets of the company. In other words, each shareholder is responsible for the unpaid taxes for its shareholding ratio in the company capital.

Articles of association

The Ltd. type of company should have an Articles of Association which includes; trade name, shareholders, seat and business purpose or object of the company, the amount of the capital and the amount subscribed by each shareholder. The duration of the company and method of publications concerning the company shall also be mentioned in the articles of association.

Management

Shareholders' Assembly is the supreme body of the Ltd. company which consists of the shareholders of the company. The company is represented and managed by the manager or managers appointed by the shareholders' assembly. The managers can be either resident in Turkey or in abroad as well as they can be either foreigners or local persons. In the absence of any provisions contrary to the articles of a Ltd., the shareholders are authorized and obliged to administer the business of the company in the capacity of manager and to represent the company. The management and representation of the company may also be entrusted to non-shareholders, in accordance with the articles of association or the resolution of the general meeting.

Share Capital

The minimum capital requirement for a limited liability company is 5.000 TL. It is also possible to allocate the number of shares freely among the shareholders. Par value of each share may not be less than 25 TL.

The following assets may be treated as capital for foreign investors:

- Cash,
- Machinery, equipment, parts, tools and goods as capital in kind,
- Intangible assets (patents, trademarks, etc.),
- Profits obtained from foreign investment and principals of foreign loans and interest thereon and other financial rights,
- Natural resources exploration and manufacturing rights,
- Shares in another company.

The capital of a Ltd. is not issued in the form of certificates. The minimum participation is 25 TL or any higher amount divisible to 25 TL. Any transfer of ownership must be entered in the register of shares, approved by minimum three fourth of the members and these members must be representing at least three fourth of the share capital. This transfer statement must be notarized and also conditional to any other restriction, if existing in the Articles of Association.

Annual Meetings

Shareholders meetings of a Ltd. are normally called by the managers or by the holders of at least 10 % of the share capital, once a year in the course of the three months following the closing of the financial year. For a Ltd. having more than 20 shareholders, the provisions regarding the general meetings of A.S. shall also apply to the general shareholders meetings. In Ltd. having 20 or less shareholders voting shall be cast in written form. The statutory rights of the general meeting include decisions on, amendment of the articles of association, approving the financial statements and determination of the destination of net profits.

Audit

In Ltd. companies, if the number of the shareholders exceeds 20, the appointment of a statutory auditor becomes a requirement.

Dissolution

A Ltd. company may be dissolved in the following cases.

- The expiration of the term for which they have been constituted by the articles of association,
- The decision of the shareholders' assembly,
- The court decision based on the application of the shareholders,
- Other considerations stated in the related laws such as impossibility of the realization of the establishment, the loss of two thirds of the share capital, the reduction of the number of shareholders below two, the realization of any cause of dissolution provided for by the articles of association, bankruptcy of the company.

Liquidation

Except the cases of merger with another company or in the event of a conversion into another form of a company or transfer to a public law corporation, the company shall be dissolved through a formal liquidation process.

In the absence of any liquidators having been designated by the articles of association or by a resolution of the shareholders' assembly, the company manager shall carry out the liquidation formalities. The company managers shall have the names of the liquidators registered with the Trade Register and announced three times at intervals, not exceeding one week. The creditors of the company shall be called upon to apply within one year and present their documents.

The official liquidation formalities which executed with the local authorities takes around 12 -18 months and all the fiscal requirements should be met during this period.

5.4 Joint Stock Corporation

Shareholders' liability

Liabilities of shareholders are limited to the capital committed to Joint Stock Corporation (Anonim Sirket, A.S.), for both tax and legal purposes.

Number of shareholders

A.S. can be formed by at least 5 persons. These shareholders may be individuals or corporate bodies, residents or non-residents.

Articles of Association

An A.S. company should have an Articles of Association which includes trade name, shareholders, seat and business purpose or object of the firm, the amount of the capital and the amount subscribed by each shareholder. Further, the amount of share capital, the nominal value of each share, the mode and terms of payments, the mode of convening the general meetings, time of meetings and conditions concerning voting are also stated in the articles of association of A.S. The duration, if it is limited, and method of publications concerning the company are also mentioned in the articles of association.

Management

There are two administrative bodies in the A.S. as the Board of Directors and the General Assembly. The board of directors is composed of at least 3 persons, who are shareholders or representatives of the legal shareholders, designated by the articles of association or elected by the general meeting. The Board can also

delegate its authorities in fully or partially to a board member or to a general manager appointed from outside of the company.

General Assembly, consisting of its shareholders, convenes as ordinary or extraordinary. The details are explained in the below section for the annual meetings.

Share Capital

The minimum capital requirement for an A.S. is 50.000 TL. It is possible to allocate the shareholding percentages freely among the shareholders.

The following assets may be treated as capital for foreign investors:

- Cash,
- Machinery, equipment, parts, tools and goods as capital in kind,
- Intangible assets (patents, trade marks, etc.),
- Profits obtained from foreign investment and principals of foreign loans and interest thereon and other financial rights,,
- Natural resources exploration and manufacturing rights,
- Shares in other companies.

The capital stock of an A.S. is divided into par value shares; the shares shall have a minimum nominal value of Kr 1. This value may be increased only by portions of Kr 1 each. Both common stock and preferred stock may be issued, either as bearer shares or registered shares. Each share shall carry at least one vote. The articles of association shall determine the number of votes given by the shares to their owners provided it is not contrary to this principle. If a share has several owners, they may exercise their right to vote only through a representative.

Annual Meetings

As mentioned above, General Assembly, consisting of shareholders, convenes as ordinary or extraordinary. The Board of Directors normally calls a general meeting of shareholders within 3 months following the end of accounting year. An extraordinary shareholders meeting can be called by the Board of Directors, Auditors or by the holders of at least 10 % (which can be diminished by the articles of association) of the share capital, if there are due reasons in doing so. The general meeting is to be held at least once a year within three months following the end of the financial year. The meeting is held generally at place where the A.S. has its statutory seat, unless the articles of Association provide otherwise.

If there is no restriction in the articles of association, voting right is computed on the participation rate. The owner is entitled to one vote for each participation with a nominal value of Kr 1. Decisions are made by a simple majority of votes, which represents more than one half of the share capital.

The statutory rights of the general meeting include decisions on the appointment of Board Members, Directors and auditors, approval of the accounts and financial statements, distribution of profits and determination of the remunerations to the auditors, amendments of articles of Association and liquidation of the company. Except certain important issues such as change of the scope of the activity, the decisions are made by a simple majority of existing votes.

Audit

The general shareholders' meeting appoints one or more auditors, not exceeding five, pursuant to procedures established by-laws. The majority of auditors in a company must be Turkish citizens. The auditors shall be chosen among shareholders or outsiders. They may not be at the same time elected as board member and they may not be the employees of the company. No professional qualification is required. The duties of auditors consist of controlling the business and transactions of the company and seeing that the directors comply integrally with the provisions of laws and of the articles of association. The companies listed on Istanbul Stock Exchange, banks, insurance companies and other financial institutions are to be audited by the independent auditors qualified under the Law governing the accounting profession in Turkey.

Dissolution

A.S. company may be dissolved in one of the following cases.

- The expiration of the term for which they have been constituted by the articles of association,
- The realization of the object of the company or the impossibility of its realization,
- The loss of two thirds of the share capital or the requisition of creditors by this reason,
- The reduction of the number of shareholders below five,
- The realization of any cause of dissolution provided for by the articles of association,
- Bankruptcy of the company.

If the dissolution results from a cause other than bankruptcy, the board of directors shall have it registered with the Trade Register and announced three times at intervals not exceeding one week. The creditors of the company shall be called upon to apply within one year and present their documents.

Liquidation

Except in the cases of merger with another company and conversion into a limited liability company or transfer to a public law corporation, the dissolved company shall enter into liquidation.

In the absence of any liquidators having been designated by the articles of association or by a resolution of the general meeting, the board of directors shall carry on the winding up operations. The board of directors shall have the names of the liquidators entered in the Trade Register and advertised three times at intervals not exceeding one week. The creditors of the company shall be called upon to apply within one year and present their documents.

The official liquidation formalities to be executed with the local authorities takes around 12-18 months and all the fiscal requirements should be met during the liquidation period.

5.5 Other Forms of Doing Business in Turkey

Liaison / Representative Offices

Such an office may be established with the permission of the Foreign Investment Department (FID) under the Turkish Prime Ministry. Foreign banks may also open representative offices subject to the permission of the Banking Regulatory and Audit Committee (BDDK).

The expenses of the liaison offices must be met by bringing foreign exchange from abroad. Under the present legislation, salaries received from a liaison office are not subject to income tax irrespective of the nationality of the employee. Liaison offices may be only involved with non-commercial activities in Turkey; they may not be engaged in any type of commercial activity. They are required to report their activities to the FID at the end of each year.

Branch

Foreign companies may operate through a branch in Turkey. The branch is represented by the branch representative based on the power of attorney to be issued by the parent company. The provisions applicable to branches for the registration of investments, import of capital and remittance of profits are the same as for a company.

Branch can be established with the permission of the Ministry of Commerce and Industry. The branch does not have separate articles of association but the parent's articles of association will be applicable as the scope of activity of the Turkish branch. The branch does not have a separate shareholders' assembly, which will take the related resolutions for the operations of the company, but these should be executed by the board of the parent of the Turkish branch. There is no minimum capital requirement for branch establishments. Branches are also subject to liquidation such as a subsidiary company which takes 12 – 18 months.

To Operate as a Contractor

A foreign company may carry on business in Turkey based on a contract obtained as result of international tenders. A foreign contractor's activities are limited to the contract signed with the Turkish customer, which is usually a State Organization.

The contract may involve delivery of equipment and machinery, its installation and / or technical services. Foreign contractors should be aware of the possible tax implications of the contract since each activity stipulated in the contract may have different tax consequences. Income obtained from the above activities is freely transferable from Turkey subject to the provisions of the contract.

Except for international tenders, it is necessary to obtain the permission of the Treasury to establish a joint venture for the execution of a contract. A foreign company operating as a contractor does not have to set up a branch or a company but is required to register with the tax office and the Social Security Organization depending on the nature of the contract.

Accounting and Reporting

Accounting in Turkey has traditionally been strongly influenced by the need to produce information, which is acceptable to the fiscal authorities and is in accordance with commercial and tax laws. With growing economic activities and international capital movements the emphasis is moving towards production of information for a wide range of users.

In accordance with this trend, the Ministry of Finance has issued a Communiqué on 26th December 1992, setting the new accounting standards and a Uniform Chart of Accounts in presentation of financial statements. This Communiqué aimed the information presented by financial statements to be reliable and true values, and comparable with other companies.

The Uniform Chart of Accounts is compulsory for all companies except the ones which have to use different accounting techniques by their sector such as banks, insurance, leasing and factoring companies and brokers. The annual accounts for all companies must include an income statement, a balance sheet and notes to those. Accounts must be drafted and shall be approved by the general shareholders meeting, within 3 months from the end of the financial period.

The format of accounts follows the model accounts contained in the Communiqué of Ministry of Finance. The new standard forms of financial statements have been adopted as from 1 January 1994. There are additional disclosure requirements for companies listed on the Istanbul Stock Exchange, which are set by the Board of Capital Market.

The milestone for accounting will be 01.01.2013 where with the introduction of New Commercial Code the companies have to keep their books in accordance with the Turkish Accounting Standards (TAS) as of 01.01.2013. TAS has been adopted from IFRS and the companies will have to change their accounting systems in order to keep their commercial books in accordance with TAS.

Each company should keep one set of books. Branch of a company may keep separate books, which will be consolidated by the parent company. Group companies are not required and allowed to prepare consolidated financial statements for tax purposes. Bookkeeping (accounts and explanations) must be in the local language in accordance with the Turkish legislation. However, it is optional to use a second language together with the Turkish language in the legal books. It is also a requirement to maintain accounts in local currency, Turkish Lira ("TL"). However, foreign currency equivalents may be stated on the documents (e.g. invoices) or records in addition to the local currency. Accounting in foreign currency only is permitted under special conditions (e.g. paid up capital of the company must be at least USD 100 million and at least 40% of its shares must be held by foreigners (i.e. on-residents) but, it will still be subject to permission of the Council of Ministers).

The taxpayers who want and meet certain conditions can benefit from the implementation of keeping the books and the documents in the electronic environment. On the other hand, there is a specific preparation period before the implementation. The taxpayers who complete the preparation period successfully are given a permission certificate for the implementation of keeping the books and documents in electronic environment.

5.6 Forms of Doing Business Other Than Through Branches or Subsidiaries

A foreign company may desire to enter the Turkish market without establishing a branch or a subsidiary respectively. For that purpose the foreign company may make use of:

- an independent sales agent,
- an independent distributor.

Even if the foreign company wants to set up its own branch or subsidiary in Turkey it is always worthwhile considering whether the marketing and sales functions should be done by employed personnel or by independent sales agents/distributors. In the latter case the company does not need to maintain an "own-sales" force, which could become very expensive. In various industry segments, especially in the field of information technology, chemicals and medical equipment, it has become common practice that finding customers is exercised by independent distributors.

Independent sales agent

Although respective provisions of the Turkish Commercial Code govern the rights and obligations of a sales agent, it is advisable to specify the essential elements of the sales agency agreement in a written contract.

Pursuant to Section 133 and 134 of the Commercial Code, each of the parties may, with reasonable causes and three months' notice terminate the agency contract. The party terminating the contract shall compensate the losses of the other party resulting from non-completion of business commenced.

Distribution Agreement

Under a distribution agreement, the distributor purchases the goods from the principal (foreign company or the Turkish subsidiary of a foreign company) and sells the goods in the markets allocated to him. The distributor absorbs the risk of the obsolescence of goods purchased and the non-collection of accounts receivable due from the customers. The parties are therefore free to structure the agreement as they see fit. The distributorship agreements can cover a wide range of subject matters like:

- determination of prices charged by the principal to the distributor,
- annual turnover targets,
- after sales services,
- sharing of advertising costs, etc.

5.7 The New Turkish Commercial Code

On the verge of becoming a member of European Union, Turkey has entered an era of adaptation to a whole new set of rules and regulations. In this respect, perhaps the most important transformation is made under the area of legislation. In order to achieve a complete harmonization with EU Legislation, a major change took place starting from the fundamental Turkish Laws. As a result, the core element of the new laws and regulations that are prepared and passed by the Turkish Parliament is under the influence of the basic principles of EU Legislation.

In light of these, one of the most important fundamental law that is passed by the Turkish Parliament is The New Turkish Commercial Code No.6102. The New Commercial Code replaces the old commercial code that has been in force since 1956 which has been substantially amended several times by the Parliament in order to obtain conformity with the rapidly changing World of Economy and Trade.

As a result, keeping the acquisitions of the previous code, the New Turkish Commercial Code is formed in line with the principles of transparency, corporate

governance, public enlightenment and auditing under International Financial Reporting Standards (IFRS).

Enforcement Date of the New Code

New Turkish Commercial Code has been legislated as of January 2011 and published on the Turkish Official Gazette as of February 2011.

New Turkish Commercial Code will be in force on July 1st 2012, however some articles regarding auditing will be in force on January 1st 2013. Articles which are concerning company website will be in force as of July 1st 2013.

Significant changes introduced by the New Turkish Commercial Code Company with one shareholder

Capital stock companies such as joint stock companies and limited liability companies can be established with one shareholder, furthermore, the aforesaid companies which are already established will be able to decrease the current number of shareholders to only one shareholder.

Moment of Establishment

The moment of signing articles of association by company founders in front of the notary public will be deemed as the establishment moment of companies. The moment of acquirement of legal personality will be the moment of registration with the Trade Registry.

Statement of Founders

At the time of establishment of a capital stock company such as a A.Ş. or Ltd., founders shall be obliged to prepare and sign a statement that is pursuant to the principal of integrity and in accordance with content stated within the Code.

Transaction auditor

One or several auditors, who shall be a member of the auditing profession as stated in the related Turkish Laws and Regulations that is either an independent certified public accountant or a sworn financial advisor, shall undertake the auditing services of the capital stock company during the company establishment procedures. Thus, an establishment report shall be prepared by the auditor which contains the information that is listed in but not limited to the related article of New Turkish Commercial Code.

Turkish Companies Trade Registry and Company Trade Names

Trade Registries shall be centralized and a Trade Registry Database that will be used as an electronic information bank shall be founded by the Ministry of Industry and Commerce and Turkish Union of Chambers and Commodity Exchange.

Furthermore, according to the New Commercial Code No.6102, Government and the related Chamber shall be held jointly and severally liable against the errors on the Trade Registry and for the compensation arising from the said error.

There is also an amendment concerning the tax office application for starting of work during the establishment procedures. Upon the enforcement of the new Code, sending the copies of the application documents to the related tax office for Corporate Tax payers will become obligatory for the Trade Registry officials. Thus, the obligation of notification regarding starting of work with the tax office shall be deemed as completed.

Regarding trade names, they will be protected as equally as the names under the Copyright Law such as Industrial property rights.

Company books

According to the new amendments, company books will be held in accordance with the Turkish Accounting Standards as of January 1st 2013.

Journal, ledger book, inventory book are the company books that are obligatory to keep for merchants and additionally stock ledger, decision book and General assembly and negotiation book are also obligatory for corporate bodies.

Company books and other necessary records must be prepared in Turkish and can be kept in the online system. In this case access to this information shall be provided properly and easily.

Web Site

According to the new commercial code, stock corporations are obliged to set up a web site.

The necessary information is specified and listed under the new commercial code as below;

- The official announcements that is required by law,
- The documents shall be presented to the shareholders and associates,
- Every kind of invitations and summons, including the ones that are related with the general assembly,
- Balance sheets, their footnotes and annexes,
- The annual report of the board of directors and the evaluation report regarding the degree of the compliance with the fundamental principles of corporate governance,
- Reports of auditor, private auditor and operational auditor.

Failing to set up a website is punishable by imprisonment up to six months and gives rise to pecuniary punishment which corresponds to a fine from 100 days to 300 days.

Prohibition to become indebted to the company

According to the new Commercial Code, it is expressly stated that shareholders of the companies are not allowed to become indebted to the company. There are two exceptions for this rule; debt of subscription and transactions related to the activity of business of the company which are conducted in line with the arm's length principle.

General Assembly

General Assembly can be convened by way of using the benefit of the online technologies in accordance with the New Turkish Commercial Code. Procedures regarding the online general assembly will be determined with a regulation.

Multi-corporate Enterprises

One of the most important regulations introduced by the New Commercial Code is concerned with the Multi-corporate Enterprises. In this regard, parent company and its affiliates are defined and the relation between these companies are expressly set as below;

If a company directly or indirectly;

- Owns the majority of the voting rights of another company
- Holds the right to select the number of members that will be able to form the majority to take a decision in a management body of another company according to its articles of association,
- Holds the majority of the voting rights solely or together with other shareholders of another company in addition to their own voting rights, in accordance with a contract.

In order to apply the rules for the Multi-corporate Enterprises, the head office of the parent company or one of its affiliates shall be in Turkey.

Every year the sister company has an obligation of preparing a dependence report, which sets forth the relation between its parent company. Moreover, the parent company is not allowed to use its powers of domination to cause damages to its sister company.

Squeeze –out

Another important innovation regarding the dismissal of a shareholder is introduced by New Turkish Commercial Code. The squeeze-out will be possible in case two conditions are fulfilled. Since the squeeze out can be occurred between parent company and sister company; firstly, parent company shall hold the 90 percentage of the sister company and secondly the shareholder who will be subject to squeeze-out shall cause inconvenience up to a point where it would prevent the sister company from performing its activity. In this case the parent company will have the right to purchase the shares of the said shareholder from real market value and squeeze-out the shareholder.

Independent Auditor

After the New Commercial Code becomes operative, the companies will no longer be under the obligation of having an internal auditor as a statutory organ. Instead, the area of auditing is regulated with a whole new set of rules which aim to serve the purpose of compatibility with the international standards. According to this new set of rules, companies will be subject to independent auditing that shall be provided by auditing firms. In this regard, the shareholders of an independent auditing firm shall be either an independent certified public accountant (CPA) or a sworn financial advisor (SFA). Small and medium sized enterprises shall also receive independent auditing service from one or more CPA or SFA. Regardless of their size, companies' financial reports and their accounting procedures will be in line with Turkish Financial Reporting Standards which is prepared in accordance with International Financial Reporting Standards.

Joint Stock Company Establishment

According to the new commercial code, it is possible to establish a joint stock company with one shareholder. The minimum amount of capital required for establishing a joint stock company is 50.000 TL, with a minimum nominal value of 1 Kurush, which did not change with the New Code. However, for the joint stock companies that are open to public thus adopt a registered capital policy, the minimum amount of capital is 100.000 TL. Nevertheless, the Council of Ministers is empowered to raise the minimum capital amount requirement in order to establish a joint stock company. Virtual media such as domain names, emblems and all kinds of transferable virtual media will also be accepted to be registered as capital along with Intellectual Property Rights such as trademarks and patents. Another important point regarding the establishment procedures is that, founders are obliged to provide a declaration of establishment regardless of the type of capital which can either be submitted in cash or in kind.

Management

In accordance with the new amendments in the New Commercial Code, Board of Directors (BoD) can be consisted of one or more individuals or corporate bodies unlike the current Code that requires at least three individuals in order to form BoD. Moreover, the obligation of being a shareholder of the company is no longer required in order to be a member of Board of Directors. However, there is a major requirement for the member of BoD imposed by the New Commercial Code. In this regard, at least one member of BoD who shall be entitled to represent the company shall be a Turkish citizen and reside in Turkey. This requirement will also be applied for the BoD with one member. In case, a corporate body becomes a member of BoD, an individual shall be appointed to act on behalf of the corporate body in the BoD and this individual shall also be registered with the local Trade Registry. Consequently, no individual is allowed to attend the BoD meeting other than the registered individual.

Furthermore, there is an education requirement for member of BoD in New Commercial Code. According to this requirement, one out of four members of BoD shall be a university graduate. However, this rule will not be applied for the BoD with one member.

Limited Liability Company Establishment

According to the new commercial code it is possible to establish a limited liability company with one shareholder. According to the amendments in the new commercial code regarding the establishment procedures of the limited liability company, the obligation to set a time limit for the duration of the company in the articles of association is invalidated. A new obligation that shall be taken into account in the preparation of articles of association is to specify the managers of the company.

In this respect, at least one of the managers shall be resident in Turkey and shall also be authorized to represent the limited liability company solely. The minimum amount of capital is raised to 10.000 TL. from the current amount of 5.000 TL. However, Council of Ministers is empowered to increase the minimum capital requirement to establish a limited liability company up to ten times. Moreover, the monetary payment for the capital shall be made in single lump sum basis and the founders are no longer allowed to make the payment in installments. The nominal value of the capital stock shares are 25 TL. Lastly, the limited liability company is allowed to purchase ten percent of its shares.

Management

The management body of a limited liability company consists of manager/managers. According to the New Commercial Code, in case there are more than one manager, a new management body will be formed which called "Manager's Assembly". Manager's assembly is entitled to take decisions concerning all the matters except the ones that lie within the General Assembly's responsibility under the related Codes and Articles of associations. Moreover, at least one of the managers shall be resident in Turkey in case there is more than one manager.

Liquidation of capital stock companies

The New Code also brought some changes on the liquidation procedure for companies. There are two main changes on the status and appointment of the liquidator. According to new changes, if there are cases which leads the court to decide the company's dissolution, then the court will also have the right to appoint the liquidator. The second change is at least one of the liquidators shall be Turkish citizen and resident in Turkey.

There are also some new institutions set up within the new Code regarding liquidation procedures such as additional liquidation and withdrawing from liquidation.

Additional liquidation

Even though the process of liquidation has been completed, if there is necessity to take further measures concerning liquidation, this new institution shall be considered as temporary measure. In order to apply the additional liquidation, there can be numerous cases. However to clarify the issue, here are some examples for additional liquidation; a) if the legal requirements are not appropriately fulfilled during the allocation of assets, b) in case of opening law suits against shareholders who received false acquisition from the liquidation portion in order to refund this portion, c) in case of opening law suits against the competent authorities for their responsibilities.

Back out of liquidation

In case of termination of the company with expiration of the company duration or as a result of a decision taken by General Assembly, on the condition that company assets have not been allocated to the shareholders; the General Assembly takes a decision regarding the continuation of company with the aim of interest and back out of liquidation. The said decision shall be taken with votes that correspond at least sixty percent of the capital.

Re-domiciliation in the New Turkish Commercial Code

The Application Law of New Turkish Commercial Code enables re-domiciliation of a company that is established in Turkey to another country without liquidation or re-establishment in other country. However, there are some requirements to do that it is not possible for a Turkish company to be fully de-registered from Turkish Trade Registry unless some conditions are met i.e. the full satisfaction of the creditors. Re-domiciliation of the company will be governed under the Trade Registry Regulations.

In order to apply the re-domiciliation, Trade Registry Regulations are made within six months following the date the new Turkish Commercial Code that is published in the Official Gazette (the date is February 14, 2011). Re-domiciliation will be effective on July 1, 2012 if the new regulations are made within six months.

However, after such a framework for the New Turkish Commercial Code perspective, related legislative amendments with regard to tax should also be made in order to implement "re-domiciliation". These should cover direct and indirect taxation areas.

6. Corporate Taxation

New Corporate Tax Law No:5520 has been enacted on 21 June 2006. In this context, the previous Corporate Tax Law No: 5422 dated 03 June 1949 and its annexes and amendments have been abolished.

New Corporate Tax Law has made some important amendments in the current applications and also brought some new concepts into the tax legislation. With the new Corporate Tax Law, Turkish corporate tax legislation has especially more clear, objective and harmonized provisions concerning to "thin capitalization" and "transfer pricing" in line with the international literature.

On the other hand, Corporate Tax Law No: 5520 has brought some new concepts into Turkish tax legislation such as "Controlled Foreign Corporation", "Tax Havens".

6.1 Taxes on Corporate Income

Companies Subject to Tax

The following entities are subject to taxes on income levied under the Corporate Tax Law, No. 5520 of June 21st 2006,

- (i) Companies with Share Capital:** Joint stock companies, limited liability companies and limited companies with shares which are founded under the Turkish Commercial Code and similar foreign companies. Funds which are subject to regulation and supervision of Capital Markets Board and similar foreign Funds are also included here.
- (ii) Co-operative Companies:** Co-operatives founded under Co-operatives Law No: 1163 or co-operatives founded under its special laws and similar foreign co-operatives.
- (iii) State Economic Enterprises:** Commercial, industrial and agricultural organizations outside of (i) and (ii) above, which have continuous business activity and owned by or affiliated to central and local administrations, municipalities, and other public organizations,
- (iv) Commercial, industrial and agricultural organizations outside of (i) and (ii) above** owned by or affiliated to foreign states, foreign state administrations and organizations are also treated as state economic enterprises.

- (v) Economic entities owned by foundations and associations: commercial, industrial and agricultural organizations outside of (i) and (ii) above, which have continuous business activity and owned by or affiliated to foundations or associations and similar foreign enterprises are economic entities run by foundations or associations. Unions are treated as association and congregations are treated as foundation.
- (vi) Joint Ventures: These are established between entities subject to corporation tax and individuals to render work with the objective of sharing profits under the joint responsibility. Corporate tax liability of joint ventures is subject to election by its partners and therefore the joint ventures are considered as partnerships (i.e. partners are liable to tax) unless the partners made such an election so that the joint venture is treated as if it is a company for corporate tax purposes.

State economic enterprises and economic entities run by foundations and associations, whether or not they have a) legal personality, b) independent accounting systems, or c) share capital or d) own business places and regardless of whether they are formed for the purposes of profit, are subject to taxes on income.

Territoriality

Those taxpayers whose legal or business centers are in Turkey, are subject to taxes on their worldwide income. If both of the legal and business centers are not in Turkey, then the company is qualified as non-resident and is subject to tax only on income generated within Turkey. The legal centre is shown in the Articles of Association and the business centre is the place where business activities are concentrated.

Taxable Income

Taxable income is defined as the difference between the net worth at the end of the year and the net worth at the end of the preceding year, with certain adjustments, mainly to eliminate capital items and to recognize special statutory allowances and disallowances. Turkish companies must compute their taxable income by starting with the balance sheet income included in their annual statements (so called commercial balance sheet) and then make the adjustments required by the tax laws. Non-deductible expenses are added, whilst the tax exempt income and losses carried forward are deducted.

In the preparation of financial statements, Turkish commercial law permits wider latitude in the valuation of assets, and in the determination of accruals, reserves and liabilities than those which are allowed by the tax laws.

Inflation accounting has become available in determination of taxable profits, as from January 1, 2004, if (i) accumulated inflation rate during the last 3 years

(including the current year) is more than 100 %, and, (ii) the inflation rate of the current year is higher than 10 %. Inflation accounting for tax purposes is designed more or less in a similar manner of IAS 29 under which, in principle, non-monetary items (such as inventory, fixed assets, paid-in capital, etc.) are adjusted for inflation. Monetary gain or loss arising from monetary gain or loss arising from the inflation accounting is evaluated as taxable income. On the other hand, since the conditions stated above were not satisfied for the year 2005 and subsequent years, inflation accounting was just applied for the year 2004. Upon the introduction of the inflation accounting, possibility of revaluation of fixed assets and making use of LIFO as inventory valuation method have been abolished also as from January 1, 2004.

6.2 Allowable Deductions

The net business income is determined by deducting expenses relating to the operating of the business from the gross income realized by the business.

The tax law first provides that all general expenses incurred with the purpose of generating and maintaining commercial income are tax deductible. Then the law lists all other tax-deductible expenses. Non-deductible expenses are also separately determined.

- Charges to Turkish companies for management expenses by a parent or sister corporation are tax deductible as long as they comply with Turkish transfer pricing regulations. (Please refer to section 7 for details information).
- Taxes imposed on goods such as taxes on real estate, stamp tax, registration duties and municipal fees, are deductible.
- Payments of royalties for the use of patents, copyrights, know how and trademarks are deductible.
- A specific bad debt reserve is allowed where:
 - (a) The dispute on the receivable is under review by the Courts, or
 - (b) Miscellaneous receivables which have not been paid after a formal notarized or written request to pay,
 - (c) The Banking Law and related regulations have special reserve requirements for non-performing loans.
- Expenses incurred for business entertainment are deductible on condition that bills, which state the purpose and the names of the guests, support them.

- Travel expenses (including meals and lodging) are deductible if they are incurred for business purposes and are reasonable as compared with the importance of business. By Budget Law each year per diem allowances are set out for government employees at each wage level. Payments by an employer to an employee in excess of the amount paid to government officials earning the same salary levels are subject to taxation as remuneration. However, if an employer pays actual meal and lodging expenses, based on receipts issued by the third parties, such payments are not taxable.
- Donations to government offices, municipalities, villages, associations that pursue the public interest and foundations under the Civil Code with a tax exempt status granted by the Government, and organizations engaged with scientific research and development are deductible up to 5 % of taxable income of the relevant year.
- All construction expenses made for the school, health premises, dormitories, nursery schools, rest homes, rehabilitation centers donated to the establishments stated above, and all kind of donations and gifts made to these corporations for the construction of the mentioned premises or for the continuance of the activities of the existing premises.
- Total amount of the donation made in cash or in kind via Prime Ministry upon receipt for the natural disasters decided to be helped by Board of Ministers.
- Total amount of sponsorship expenses for amateur sport activities decided by the relevant laws and 50% of sponsorship expenses for the professional sport activities.
- Employee salaries and payment to the chairman, directors and auditors are deductible. Payments may be in the form of allowances, fees, premiums and bonuses. Payments in kind are also tax deductible but are deemed as salary and taxed as such.
- Interest costs; either as a direct charge or as depreciation allowance when capitalized.
- Undocumented expenses up to 0.5 % of the gross income realized in foreign currency related to export, construction and maintenance services performed outside of Turkey, and international transportations.
- Fees paid to the Employer's Union are deductible with the condition that monthly fees paid should not exceed the daily total payment of salaries.

- A loss incurred in any financial year can be carried-forward for 5 years against future profits for purposes of corporation tax. It cannot be carried back.
- In addition to the usual deduction of R&D expenses, 100 % of R&D costs incurred for eligible projects can be entitled as a deduction from the taxable profits subject to certain conditions. The amount, which is not deducted in the relevant period due to the lack of sufficient taxable profits, can be carried forward to the following accounting periods provided that they are under the scope of Law number 5746 regarding with R&D activities.

6.3 Non-allowable Deductions

• **Disguised Profit Distributions (Transfer Pricing)**

If a taxpayer enters into transactions regarding sale or purchase of goods and services with related parties, where the prices are not set in accordance with arm's length principle, then related profits are considered to be distributed in a disguised manner through transfer pricing. Such disguised profit distributions through transfer pricing are not accepted as tax deductible for corporate income tax purposes. (Please refer to section 7 for detailed information).

• **Legal Reserves**

Any kind of reserves (including all kinds of reserves computed under the Turkish Commercial Code, Banking Law and special laws concerning corporations or their Articles of Associations) is not deductible.

• **Cost Allocation**

Interest, commissions etc. paid to a parent company or branches outside Turkey for purchases and sales carried out on behalf of a non-resident company in Turkey and amounts allocated to meet the expenses and losses of the parent company and its branches outside Turkey, are not tax deductible with the exceptions of;

- amounts related to the generation and continuation of income in Turkey and allocated in line with the cost allocation keys determined in accordance with the arms length principle, and
- travel expenses incurred by authorized persons sent from foreign countries in connection with the auditing and supervision of a branch in Turkey.

• **Thin Capital Costs**

Interest, foreign exchange losses and other similar expenses related to the borrowings from related parties which are regarded as thin capital are treated as non-deductible expenses for corporate income tax purposes.

The Corporate Tax Law imposes a specific debt/equity ratio of 3:1 for consideration of thin capital. If the borrowing obtained directly or indirectly from shareholders or persons related to shareholders exceed three times the shareholders' equity of the company at any time during the relevant year, the exceeding portion of the borrowing will be treated as thin capital.

If the shareholder (or related party) providing the loan is qualified as a bank or a financial institution which operates in line with its own field of activity, then the 50% of the borrowings obtained from these will be taken into consideration in the calculation of debt/equity ratio - hence the allowable debt/equity ratio will be increased to 6:1.

However, borrowings obtained from the intra-group credit companies which are only financing the relevant group companies cannot be taken into consideration as 50% in the calculation of debt/equity ratio.

Loans mentioned below (but not limited to) will not be qualified as thin capital;

- Loans obtained from the 3rd parties against non-cash guarantees provided by shareholders or the persons related to the shareholders,
- Loans obtained by companies' subsidiaries, shareholders or related persons from the banks and financial institutions or from the stock markets that are transferred wholly or partially to the company with the same term and conditions.

Excluding foreign exchange differences, the interests paid or calculated and other similar expenses over the thin capital (that exceeds the 3:1 debt equity ratio) is treated as dividend distributed to shareholders as of the last day of the accounting period in which thin capital conditions are satisfied.

6.4 Exclusions from Income

Dividends - domestic participation gains exemption

Dividends received by a Turkish company from a resident corporate taxpayer are not taxed in the hands of the recipient company. The exemption is also available to the non-resident companies to the extent that the dividends are attributable to a Turkish permanent establishment or branch. Dividends received by the companies from founder's shares that give a participation right to the profit of another resident company and from other redeemed shares are exempt from corporate taxation. Capital gains are not covered under this exemption.

Dividends – foreign participation gains exemption

Dividends received from participations outside Turkey are exempt from corporate taxation if certain conditions are valid. These are, generally, among others, (i) the participation rate has to be at least 10 %, (ii) the participation should have been held at least for 1 year, and (iii) foreign tax burden is at least 15 %, (iv) gain should be transferred to Turkey until the date filing of corporate tax return of the fiscal year in which the relevant gain obtained. Capital gains upon disposal of shares in foreign participations are not covered under this exemption. Under the same conditions, foreign branch profits may also eligible for this exemption.

Capital gains exemption for the sale of the shares of a foreign participation / subsidiary

The capital gains obtained by a resident joint stock company from the sale of the shares of the participations/subsidiaries whose legal and business centers are outside of Turkey (i.e. shares of the foreign subsidiaries) are exempted from the corporate tax if the following conditions are satisfied all together;

- At least 75% of the total assets of the Turkish company, other than cash equivalents, should be composed of participation in foreign subsidiaries shares at least for an uninterrupted period of 1 year as of the date of the gain obtained,
- Turkish joint stock company must hold at least 10% of shares of these foreign subsidiaries,
- The foreign subsidiary must be a company in the status/nature of a joint stock or a limited liability company,
- The shares of the foreign subsidiary must be held by the resident joint stock company at least for two whole years.

Exemption for the gains obtained through foreign business place and legal representative

Gains obtained by the companies through the business place or legal representatives abroad are exempted from the corporate tax with the fulfillment of the certain conditions. These are, generally, among others, (i) gains should be subject to at least 15% tax burden in accordance with the tax legislation of the relevant countries, (ii) gains should be transferred to Turkey until the date of the filing of the corporate tax return of the fiscal year in which the relevant gain obtained.

Export exemption

Profits of non-resident companies which have a place of business or a permanent representative in Turkey which forwards goods purchased in Turkey for the purpose of export, without selling such items in Turkey, are not considered as taxable profits attributable to the place of business or permanent representative.

Exempt Income

The following types of income are exempted from Corporation Tax:

- (a)** New share issue premiums (Agio), which represent the difference between the nominal and sale values of shares issued by joint-stock companies, are exempt from corporation tax.
- (b)** Offshore income from construction, repair, maintenance and technical services is exempt from corporation tax.
- (c)** Portfolio management income by securities investment funds and companies, the profits of real estate investment funds and companies, and venture capital investment funds and companies, and pension funds, and housing financing funds and wealth financing funds, and the portfolio management profits obtained by investment funds or companies which have portfolio based on the gold and precious metals dealing in exchange markets founded in Turkey are exempt from corporation tax. However, this income, except for pension funds' income, will be subject to a withholding tax at 15 % irrespective of whether distributed or not under new Corporate Tax Law. Council of Ministers is authorized to reduce this withholding tax rate to zero or to increase it to 20% and also authority to differentiate within the same limits according to the types of funds or companies and nature & allocation of the assets in their portfolios. In this context; the withholding tax rates are as follows based on Council of Ministers Decree 2009/14594;
 - 0% for portfolio management income by securities investment funds and companies.
 - 0% for profits of housing financing funds and wealth financing funds.
 - 0% for profits of real estate investment funds and companies.
 - 0% for profits of venture capital investment funds and companies.
- (d)** 75 % of capital gains arising from the disposal of immovable properties and participation shares, founder's shares, pre-emptive rights and redeemed shares in other companies are exempt from the corporate tax. Major requirements are (i) assets sold should have been held at least for two years; (ii) the exemption is applied in the year in which sale occurred and capital gain benefit from the exemption should be kept in a special reserve account at least for five years (iii) sales revenue should be collected until the end of second calendar year following sale year (iv) exempted amount can not be transferred to another account (other than paid-up capital) or withdrawn from company within five years and also the company is not liquidated within 5 years.

- (e) There are tax-holidays available also under some specific laws related to the business activities maintained in Turkish Free Zones (i.e. the income concerning manufacturing activities in Free Zones is exempted from corporate income tax up to the membership of Turkey to EU, this exemption does not cover the dividend distributed) and in Technology Development Areas as well as the tax holiday available for profits made through operating vessels that are registered as Turkish International Ship Registry Office. Profits arising from providing education and rehabilitation services are exempt from corporate taxation for period of 5 years starting from commencement of such businesses subject to fulfillment of certain conditions.

Investment Incentive Allowance

Investment Incentive Allowance was a mechanism which enabled the taxpayers to deduct some of their eligible investment expenditures against their fiscal profits. In the absence of any fiscal profits, the carried forward investment allowance was being allowed to be carried forward for utilization against the future fiscal profits without any time limitation.

Article 19 of the Income Tax Code concerning investment incentive allowance has been abolished as of January 1, 2006. However, it is envisaged that the application of investment incentive allowance, with some exceptions, would continue to be applied until the end of 2008 under some circumstances.

Alteration has been made in 2010 as the companies might continue utilizing deferred investment allowances as %25 of their fiscal income due to the law numbered 6009, article 5. Finally, in February 2012, constitutional court decided to terminate existing process and by the publish of decision in official journal on 18.02.2012, the companies are able to utilize the whole amount of their investment incentives.

6.5 Corporate Taxation

Computation of Corporate Income Tax

The corporate income tax rate is 20 %.

Withholding tax on dividends

When dividends are paid out, the company is required to make a withholding from the dividends. The rate of withholding tax is 15 %. Dividends paid to a Turkish resident entity (i.e. Turkish holding company) or a Turkish branch of a foreign company is not subject to the withholding tax. A share capital increase by the company using the retained earnings would not be considered as a dividend distribution, so no dividend withholding tax applies.

Withholding tax on branch profits

There would be a withholding tax on the branch profits of non-resident companies upon remittance of such profits to the headquarters. The rate of withholding tax is 15% effective which is applied on the amount after the deduction of corporate income tax from taxable branch profits.

Advanced corporate income tax (ACIT)

All resident and non-resident companies, who earn commercial or professional income and who are obliged to file annual corporate income tax return, are also required to file ACIT return at 20 % on the basis of the actual quarterly profits. ACIT is not a requirement for the multi-year construction works being subject to taxation on the basis of completed project basis.

ACIT paid during the year is offset against the final taxes calculated on the annual corporate income tax return. Any excess payment may be offset against other tax liabilities, and in the absence of such liabilities it is refundable upon the claim within one year.

Tax Returns and Payments

The normal fiscal year-end is December 31st. Where the calendar year is not appropriate because of the nature of business, permission can be obtained from the Ministry of Finance for an alternative fiscal period.

Annual corporate income tax returns must be filed, within the period from 1st to 25th days of the fourth month following the end of the fiscal year and corporate income tax is payable (after the offset of ACIT and other available tax credits) until the end of the month in which the tax return filed.

Advance corporate income tax return must be filed by the 14th of the second month following the quarter end and is payable on the 17th of the same month. Withholding tax on dividends has to be filed by the 23rd of the month following the dividend payments to shareholders and paid on 26th of the same month.

Controlled Foreign Corporation (CFC)

The profits of foreign companies controlled by tax resident companies or persons by means of the direct or indirect and separate or joint ownership of at least 50% of the capital, dividends or voting rights are subject to corporate income tax in Turkey irrespective of whether profits distributed or not, subject to the fulfillment of the below conditions all together;

- 25% or more of the gross revenue of CFC must be composed of passive income such as interest, dividend, rent, license fee, security sales gain etc,
- The CFC should be subject to a tax burden lower than 10 % ever its commercial income in its country,

- The CFC's total gross revenue in the relevant year should exceed the foreign currency equivalent of 100,000 TL.

The highest rate owned at any time within the relevant fiscal year should be taken into consideration as "Control Rate".

If CFC distributes dividend over its profit, dividends that has already been taxed in Turkey will not be subject to any additional corporate income tax in Turkey. However, profit distributed that has not been previously taxed in Turkey will be subject to corporate tax.

Taxes paid by CFC over its related profit in foreign countries will be offset against the corporate income tax calculated over this profit in Turkey.

Foreign Tax Credit

Taxes paid abroad on profits transferred back to Turkey may be credited against corporate income tax, but only to the extent that they do not exceed local corporate income tax calculated thereon.

Statute of Limitations

A tax return is not subject to question or additional assessment after the end of the fifth year following the year the tax liability was incurred. This period cannot be prolonged. However, the time taken for an administrative or court proceeding is not counted in the five years.

Withholding Taxes

In general, the Turkish Taxation System has the following types of withholding taxes applicable to corporations.

• Multi-Year Construction Works

Progress payments for the construction and repair works lasting more than one year are subject to 3% withholding . Such construction works is taxed on completed project basis, and the amount of withholding taxes paid on progress payments are deducted from the tax due at the end of the construction.

• Payments to Non-resident Entities

The following payments to non-resident companies are subject to withholding tax.;

- Progress payments for the construction and repair works lasting more than one calendar year at 3 %
- Professional fees at 20 %,
- Rentals and royalties at 20 %,

- Dividends and interest at 15 %,
- Sales proceeds of copyrights, patents, trademarks etc. at 20 %.

The rates applicable for payments to non-residents can be seen in Appendix IV in detail.

• **Payments to Tax Havens**

All sorts of payments made to the entities (including business places of resident companies in the relevant countries) that are established or operating in the countries which are announced by the Council of Ministers by taking into consideration whether there is an unfair tax competition or not and the exchange of information, would be subject to withholding tax at a rate of 30 % until a new rate is determined by the Council of Ministers irrespective of the fact that;

- The said payments are in the scope of tax or not or,
- The entity that receives the payments is a taxpayer or not.

On the other hand, the Council of Ministers has authority to amend the above mentioned rate within certain limits and might use its authority for each sort of payments or for each line of activities and sectors separately.

Withholding tax will not be applied to principal, interest and dividend payments for the borrowings obtained from foreign financial institutions and also insurance and reinsurance payments.

Withholding taxes over payments made to Controlled Foreign Corporations (CFC) in line with the above regulation can be offset from corporate income tax calculated over CFC's profit included in the tax return in Turkey.

• **Payments to Resident Companies**

The following payments to resident companies are subject to withholding taxes:

- Interest on all types of bonds and bills
- Capital gains derived from the sale of bonds and bills issued on or after 1.1.2006 and from the sale of stocks quoted in Istanbul Stock Exchange (ISE) that are purchased on or after 1.1.2006 and held less than 1 year.
- Interest on bank deposits and Repo income.

Alternate Tax Basis

A non-resident company which does not have commercial income generated from a business in Turkey and pays withholding tax at source may file a corporate income tax return showing gross revenue and expenses and calculating the taxes payable on net income. If the tax computed is less than the tax deducted by withholding, then a claim may be made to have the excess tax refunded. Otherwise, withholding taxes are final.

6.6 Effects of Law No: 6111 (Tax Amnesty Law) from a Corporate Tax Perspective

Turkey introduced a wide-ranging tax amnesty on 25th February 2011 through the enactment of Law No: 6111 (which is known as Tax Amnesty Law). The application period for Tax Amnesty Law expired in year 2011 but its impact has to be considered for Turkish entities.

Amongst other aspects, the Tax Amnesty Law provided shelter to entities against tax inspections for corporate taxes for years from 2006 to 2009 if the tax payer made a voluntary increase in its tax base and pay the additional taxes. In the case that the taxpayers who benefited from Tax Amnesty Law from a corporate tax perspective loses 50% of the unused carried forward tax losses originated within that year and cannot be utilized against the future profits of the company (including fiscal year 2010).

6.7 International Corporate Taxation

Residency and Taxation of Non-Resident Entities

A company is considered to be resident in Turkey if it has either its legal seat or place of effective management in Turkey or both. Legal seat refers to the place of official center of company, defined in, such as, the articles of association. The place of effective management refers to the place where the top management of the company is located. As a general rule, residence of a company is determined by the domestic rules of the contracting states. However, in some cases provisions of tax treaties might be applied.

If neither of two conditions is met for the residency in Turkey, then a company is considered to be non-resident for tax purposes. Non-resident entities are subject to taxation in Turkey on their Turkey sourced income.

Taxable income of non-residents is determined-but not limited to these-based on the following type of income:

- Profits from commercial (business) activities earned through a business place or a permanent representative in Turkey,
- Income derived from professional services performed in Turkey (or the fees that are obtained in Turkey),
- Income derived from income from lease of immovable properties, intangibles and machinery in Turkey (also transfer of intangibles in Turkey),
- Interest income obtained from Turkey,
- Dividend income obtained in Turkey,
- Capital gains of transactions performed in Turkey or obtained in Turkey.

Foreign entities may operate in Turkey to run a business in form of branch or through their subsidiaries as separate entity. These forms are elaborated in more detail below. Besides, operations of non-resident entities might be considered to constitute a permanent establishment for tax purposes. These create the concept of business place in local rules. Of course the provisions of tax treaties should also be taken into account. Business profits of non-resident entities are assessed in the same way as that of resident companies for their Turkish sourced income (please see the other sections in "Corporate Taxation").

Permanent Establishment

Under Turkish Corporate Income Tax Legislation; the income derived by nonresident entities through their Permanent Establishment ("PE") or Permanent Representative ("PR") in Turkey are subject to tax in Turkey. Turkish Corporate Tax Law refers to provisions of Tax Procedural Law regarding the definition of PE and provisions of Income Tax Law regarding the definition of PR.

In this respect, a workplace (PE) is defined as the places of business which is dedicated/allocated to the carrying out commercial, industrial, agricultural or professional activities. A business place of a non-resident entity operating in Turkey solely for the purpose of buying or producing goods in Turkey to be later exported is not considered to be a PE.

On the other hand, a PR is defined as the person who is bound to a principal by a service or representation act, and is authorized to carry out transactions on behalf and on account of the principal for a definite or indefinite period of time.

There are no further specific definitions or guidelines in respect of the definition of a PE under domestic law. Based on the generally accepted interpretation of the above mentioned tax law provisions, the following are seen as common features of a PE of a foreign entity in Turkey:

- There should be an income generating activity performed by the foreign entity (or its representatives) in Turkey,
- The foreign entity should have a fixed place of presence in Turkey where the activities are concentrated,
- There should be a close link between this fixed place of presence and income generating activities.

Based on the above, it is usually accepted that Turkish tax laws follow the PE definition OECD model tax treaties where activities carried out in Turkey who do not have a strong connection with the income generation (e.g. preparatory and auxiliary services) should not lead to recognition of PE; on the other hand, the persons who carry out commercial transactions on behalf of a foreign entity may still lead to taxation in Turkey if deemed as PR as explained above.

In contrast to the provisions under domestic rules, warehouses and independent agents are generally not included in the definition of "permanent establishment" under Turkey's treaties.

Branches

Branches are treated as non-resident entities for tax purposes and subject to corporate taxation in Turkey for their profits generated in Turkey.

Under local foreign investment legislation, a branch of a foreign company is a type of foreign direct investment and the establishment of a branch is subject to the same requirements and procedures as a foreign company that intends to run a business in Turkey. A branch office may only operate in the areas of activities of the head office. It is managed by a representative (could be a foreigner but is required to be a Turkish resident) who is appointed to this effect by a power of authorizations. The representative must be authorized to represent the foreign entity in Turkey before all public and private authorities.

A Branch has to fulfill all statutory bookkeeping and filing requirements in Turkey same as a usual resident entity.

Subsidiaries

Another form which can be used to run a business in Turkey is to set up a subsidiary as a separate legal entity, which can be established as Limited Liability Company (Ltd.) or Joint Stock Company (A.Ş).

These two forms of companies are considered as Turkish resident for tax purposes and subject to corporate taxation on their worldwide income as opposed to PE and Branches.

Withholding Taxation

The taxation of income received by non-resident entities in Turkey is regulated under the Article 30 of Corporate Income Tax Law. According to the Article, parties who make the payment to non-residents are responsible for withholding and the payment of taxes. The general withholding tax rate is 15% under the article, however the Council of Ministers are authorized to determine the rates between the range of 0% and 30%.

Dividends

Dividends distributed to non-resident entities are subject to 15% withholding tax. The withholding tax applies when the dividends are actually distributed in cash or on account. The use of profits to increase the capital of the company is not considered as profit distribution and hence not subject to dividend withholding taxation. This is the final tax for non-residents and there is no further filing requirement.

Income of Branches in Turkey is not subject to withholding taxation unless remitted to headquarters. The 15% withholding taxation applies for remittance of income to head office. The income of PEs is also subject to 15% withholding. The rate of 15% withholding tax can be reduced to 5%-10% through the use of tax treaties.

Royalties

Royalties paid to non-residents are subject to withholding tax at 20%. In a case that the non-resident company has a PE in Turkey, no withholding tax applies and however those royalties should be declared in the annual corporate income tax return and subject to taxation accordingly. This is the final tax for non-residents and there is no further filing requirement.

Gains received from the sale of copyrights, patents, trademarks and other intangible rights are subject to a final withholding tax of 20%.

The reduced rates of withholding tax over the royalty payments are available for all Turkish Tax Treaties and the rates vary between 5% and 15% (the general cap of 10% applies for nearly all tax treaties).

Interest

Interest paid to non-resident entities is subject to withholding taxation at the gross amount of interest paid to non-resident entity. In a case that the non-resident entity has a PE in Turkey, the interest income is included in the annual return and subjected to taxation accordingly. This is the final tax for non-residents and there is no further filing requirement.

Withholding tax rates applied to interest payments to non-resident companies are as follows, unless a treaty provides for a lower rate.

A rate of 0% applies to:

- Interest on Turkish government bonds and debentures (including those issued abroad),
- Interest on bonds and debentures issued by companies on or after 1 January 2006,
- Loan interest paid to foreign banks or states, or to international institutions,
- Loan interest paid to other companies that are authorized habitually to provide loans in the country in which they are established and provide loans not only to related companies but also to all individuals and legal entities,
- Interest on debentures issued by Turkish resident companies with the maturity over than 5 years,
- Income on lease certificates issued by Turkish resident asset lease companies with the maturity over than 5 years.

A rate of 1% applies to:

- Interest paid by banks on subordinated loans similar to equity and interest paid by banks and other companies on loans received by way of securitization abroad.

A rate of 3% applies to:

- Interest on debentures issued by Turkish resident companies with the maturity between 3 and 5 years.
- Income on lease certificates issued by Turkish resident asset lease companies with the maturity between 3 and 5 years

A rate of 5% applies to:

- Interest in relation to the sale of goods on credit.

A rate of 7% applies to:

- Interest on debentures issued by Turkish resident companies with the maturity between 1 and 3 years,
- Income on lease certificates issued by Turkish resident asset lease companies with the maturity between 1 and 3 years.

A rate of 10% applies to:

- Other loan interest,
- Interest on debentures by Turkish resident companies with the maturity less than 1 year,
- Income on lease certificates issued by Turkish resident asset lease companies with the maturity less than 1 year.

A rate of 15% applies to:

- Interest on deposit accounts,
- Interest over profit participating loans,
- Portion of profits received from profit/loss partnership certificates,
- Income from repo transactions for treasury bonds and debentures.

Capital Gains

In accordance with the provisions of Income Tax Law, capital gains received by non-residents upon disposal of shares and other assets are taxable in Turkey as long as the related gains are deemed to be Turkish sourced. In reference to Turkish income tax code provisions, such capital gain is deemed to be Turkish sourced if the sale transaction is performed in Turkey or the transaction is evaluated in Turkey (i.e. the payment is born by a Turkish taxpayer).

If capital gain, received by non-resident entities, is considered as Turkish sourced then it would be subject to corporate income tax at usual rate of 20%. Furthermore, the remaining amount after corporate taxes would also be subject to 15% dividend withholding taxation (taxation of remittance of capital gains). Hence, the effective tax rate reaches up to 32%.

The taxation right of the capital gains over the disposal of shares is generally remains with the country of which the selling entity is a resident provided that the minimum holding period should be more than 1 year under many of Turkish Tax Treaties.

Professional Services

Professional service fees paid to non-resident companies are subject to 20% withholding if the service is rendered in Turkey or the payment is made in Turkey. Turkey generally follows 183 days test in tax treaties. Accordingly, in most of Turkish

Tax Treaties, the professional services are taxable in Turkey if the employees of the non-resident entity stay in Turkey more than 183 days in a 12 months period.

Withholding tax rate is reduced to 5% for oil exploration activities performed in Turkey.

Income from Lease of Tangible Assets

According to local rules, payments to non-residents for the lease of movable or immovable properties are taxable in Turkey if the assets are in Turkey or the relevant rights are used in Turkey. Such leasing payments to non-residents are subject to withholding tax at 20%. The payments for the financial leasing, however, are subject to 1% reduced rate of withholding taxes.

Multi-Year Construction Works

Payments for construction works and repair projects which spread more than one calendar year are subject to 3% withholding taxes.

Turkey's Treaty Network

Turkey's double tax treaty network consist of 81 countries, 75 of this are already in effect, 5 new treaties (Australia, Brazil, Switzerland, Philippines, and Malta) have been signed but not yet in effect, 1 treaty (Finland) has been signed for renewal.

In addition, the previous Germany Treaty has been abolished effective from 1 January 2011 and it is proposed to be replaced by the new Treaty signed on 19 September 2011.

Other than the above, Turkey has started negotiations on signing the Treaty with Mexico and Vietnam in year 2011.

Please refer to Appendix (IV) where the table for the treaty countries and relevant provisions are summarized.

Tax Treaties Signed but not yet in Force

Turkey has signed tax treaties with the below list of Countries and these treaties will be in effect following the approval of the Parliaments of both Countries.

Country	Date of Signature	Dividend(%)	Branch Profits (%)	Interest (%)	Royalties(%)
Australia*	28.04.2010	5/15	5/15	10	10
Finland*	06.10.2009	5/15	5/15	5/10/15	10
Philippines**	18.03.2009	10/15	10	10	10/15
Switzerland**	18.06.2010	5/15	5/15	5/10	10
Brazil**	16.12.2010	10/15	10	15	10/15
Germany***	19.09.2011	5/15	-	10	10
Malta***	14.07.2011	10/15	10/15	10	10

(*) Treaty has been ratified by the contracting state, and would be in effect from 1 January following the year of completion of ratification process by Turkey.

(**) Treaty has been ratified by Turkey, and would be in effect from 1 January following the year of completion of ratification process by the contracting state.

7. Transfer Pricing Regulations

In Turkey, the transfer pricing provisions have been stated under the Article 13 of Corporate Tax Law with the heading of "disguised profit distribution via transfer pricing". The General Communiqué on disguised profit distribution via Transfer Pricing, dated November 18, 2007 sets details about implementation.

If a taxpayer enters into transactions regarding sale or purchase of goods and services with related parties, where the prices are not set in accordance with arm's length principle, then related profits are considered to be distributed in a disguised manner through transfer pricing. Such disguised profit distributions through transfer pricing are not accepted as tax deductible for corporate income tax purposes.

7.1 Arm's Length Principle

Arm's length principle is defined as setting prices or amounts for the purchase or the sale of the goods or services between the related persons as the prices or amounts would be charged for the same transactions carried out with unrelated parties/ third parties.

Methods for setting the arm's length prices and amounts; it is stated that the best suitable one of the following methods for the transaction can be used for setting the prices and amounts for the transactions with related persons. In other words, in the determination of the arm's length prices and amounts, the methods that can be used by the taxpayers are stated in the article and it is also stated that taxpayers will set the prices or amounts for the transactions with the related persons by choosing one of the methods which is the best appropriate for the nature of the transaction.

The methods are;

- **Comparable uncontrolled price method:** This method means that arm's length selling price applied by a taxpayer is determined by comparing with the market price stated for the comparable purchase or sale of the goods or the services between the unrelated parties.
- **Cost plus:** Arm's length price is calculated / determined by increasing the costs of the relevant goods or services with a reasonable rate of gross profit margin.
- **Resale price method:** arm's length price is calculated/determined by deducting a reasonable rate of gross sale profit margin from the price which will be applied for the resale of the relevant goods or services to the unrelated parties,
- If there is not any possibility to achieve an arm's length price by using the above methods, taxpayer can use another methods determined by itself in

accordance with the nature of the transaction. On the other hand, the method for setting the prices and amounts applied for the sale or the purchase of the goods or services with the related persons can be determined via an agreement in advance with Ministry of Finance with the application of the taxpayer.

The method determined in such a way will be certain in the conditions and periods stated in the agreement, as not exceeding three years.

The related profit regarded as distributed wholly or partially in a disguised way via transfer pricing is treated as dividend distributed as of the last day of the accounting year in which the conditions stated in this article satisfied in line with the Income and Corporate Tax Law implementations or treated as the transfer of the amount to the headquarter for the non-residents. Then previous taxations will be adjusted forth parties according to this. In order to make this adjustment, taxes assessed for the companies distributing the profit in a disguised way should be finalized and paid.

For intra-country group transactions, disguised profit distribution via transfer pricing would be applicable if treasury loss is occurred at the domestic intercompany transactions of the corporate tax payers. The treasury loss is defined as under declaration or late declaration of all type of taxes as a result of the prices or the amounts which are not in line with the arm's length principle.

7.2 Documentation Requirements

According to government decree and the General Communiqué number 1 taxpayers have two different documentation requirements; prepare transfer pricing form and yearly transfer pricing report.

• Transfer Pricing Form

According to the new rules, taxpayers are obliged to complete a form called "transfer pricing, controlled foreign company and thin capitalization form" attached to the company's annual corporate tax return. In this form, taxpayers are required to present all intra-group transactions that took place during the year and indicate the selected transfer pricing methods to test the arm's-length nature of the intra-group transactions. This form also has controlled foreign company and thin capitalization sections and taxpayers have to fill these sections too.

• Yearly Transfer Pricing Report

Corporate taxpayers also have to prepare yearly transfer pricing report for their related party transactions. However, there is a different requirement between large corporation tax office members and other corporations. Large Corporations Tax Office members must issue an annual report listing their international and

domestic related party transactions which are the sales or purchases of goods or services to/from related parties during the calendar year and also must be ready to present information and documents with the report. Companies registered with the Large Taxpayers Tax Office are typically the largest companies determined by reference to their turnover, payable taxes, and asset size and located in Istanbul. All banks and insurance companies are also among the members of the large corporations tax office members regardless of their location and size.

Corporate taxpayers other than the ones registered to Large Taxpayers Tax Office are liable to prepare this annual report listing only their international transactions with related parties.

Corporate taxpayers who do not have international related party transactions, and individual taxpayers are not required to prepare a yearly transfer pricing report, but they have to prepare transfer pricing documents stated on the General Communiqué.

The Communiqué rules set forth details of the information that needs to be included in the transfer pricing documentation. According to the Communiqué, the required minimum documentation elements include:

- Description of activities of the company, organizational structure, definition of the related parties (i.e., tax id number, addresses, phone number, etc.) and ownership information of these parties,
- All functions are performed and risks taken,
- Pricing lists of the products of the year,
- Details of cost of goods,
- The amount and invoice information about all transactions with related and unrelated parties within the year,
- All agreements signed with the related parties,
- Financial statements of related parties,
- Intra-group pricing policies,
- Intra-group accounting standards and policy differences if they exist,
- Ownership of intangible assets,
- Transfer pricing method selected by the company (comparability analysis, selected comparables whether external or internal),
- Calculations and assumption for reaching the arm's-length price,
- Calculations for reaching the arm's-length range, if applicable.

The Government Decree and the General Communiqué state that documentation should be prepared by the tax return submission date, which is 25th of April for normal calendar year, and it should be submitted to the Tax Authority upon request.

The decree and general communiqué state that if the transfer pricing documentation is prepared in a foreign language, Turkish translations also have to be submitted to the tax authorities.

7.3 Advance Pricing Agreements (APA)

Turkey's first unilateral advance pricing agreement (APA) concluded in July 2011

When an agreement between a taxpayer and a tax authority is signed, it is called an APA. This determines the principles of applying transfer prices for a number of years for the transactions amongst related enterprises in the future. If the agreement is drawn between one tax authority and a taxpayer, then it is called unilateral APA; and as transfer prices affect related enterprises that are located in other countries, there can be bilateral or multilateral APAs. Because of that, unless local laws and regulations do not provide guidance for tax authority and taxpayers, the mutual agreement procedure of applicable double tax treaties can be used to conclude bilateral or multilateral APAs.

According to the press release from Turkish Revenue Administration (TRA) on July 15, 2011, the first 'unilateral APA' has been concluded and signed between the TRA and a taxpayer following approximately one year of negotiations.

Since the new transfer pricing regulations that were introduced in Turkey (which has been effective from January 1, 2007), Turkish taxpayers are entitled to enter into APA with the TRA of Ministry of Finance for the determination of methods in relation to setting fees and prices as applied by corporate taxpayers over their transactions with foreign related parties (i.e., non-resident related parties) upon their request.

The main purpose of the application of APAs is to prevent the potential tax-related disputes and controversies in relation to transfer pricing as applied by taxpayers over their transactions with related parties. Concluding an agreement with TRA, taxpayers will be protected against the tax risks which enable taxpayers to foresee.

With the first APA in Turkey, we expect that there would be more unilateral APA applications from now on and this will pave the way for bilateral and multilateral APAs in the future.

8. Indirect Taxation

8.1 Value Added Tax

Taxable transactions

VAT applies to the following transactions:

- The supply of goods or services in the course of performing commercial, industrial, agricultural, or independent professional activities made in Turkey by a taxable person,
- Goods and services imported into Turkey,
- Deliveries and services arising from other activities specifically stated in law.

Tax payer

A taxable person is any person or legal entity that has VAT liability in Turkey. Any entity that has a fixed place of business or regularly carries out commercial or professional activities in Turkey must register in Turkey.

There is no threshold for VAT registration. VAT registration is granted automatically by the tax office when a business registers for corporate income tax purposes.

Group registration: VAT grouping is not permitted under Turkish VAT law. Legal entities that are closely connected must register for VAT individually.

Non established businesses: A non established business may not register for only VAT. If a Turkish taxable person receives services from an entity that does not have a fixed place in Turkey, VAT is accounted for using the reverse-charge mechanism.

Reverse charge: The reverse charge applies if certain supplies subject to Turkish VAT are made by a person that is not resident in Turkey or that does not have a permanent establishment or headquarters in Turkey. It is a form of self-assessment for VAT through which the recipient of a supply of services accounts for the tax.

The reverse charge applies to the following services performed by non residents without a fixed place of business in Turkey:

- Services of independent professionals, such as engineering, consulting, data processing, and provision of information,
- Transfers of copyrights, patents, licenses, trademarks, know-how, and similar rights,
- Import commissions,

- Interest payments made to foreign entities other than banks and financial institutions,
- Rentals,
- Transfer or assignment of the right to use capacity for the transmission, emission, or reception of signals, writings, images, sounds, or information of any nature by wire, radio, optical or other electromagnetic systems,
- Other services not specified in this list but utilized in Turkey.

VAT rates

In Turkey, the following VAT rates are applied:

- Standard rate: 18%
- Reduced rates: 1% and 8%

The standard VAT rate applies to all supplies of goods or services, unless a specific measure provides for a reduced rate or exemption.

Examples of goods and services taxable at 1%

- Newspapers and magazines
- Some foods and beverages
- Used passenger cars
- Financial leasing services (under certain conditions)

Examples of goods and services taxable at 8%

- Some foods and beverages
- Books
- Pharmaceuticals and medical products
- Some construction equipment
- Ready-wear products, garments and textile products
- Admission charges for cinemas, theaters, and operas

VAT Exemptions

Exemptions are classified in two different groups. The term “fully exempt” supplies refers to supplies of goods and services not subject to VAT and recovery or refund of the input VAT is possible (exempt with credit).

“Partially exempt” supplies refer to supply of goods and services not subject to VAT but no right of input tax deduction.

Examples of fully exempt with credit supplies of goods and services are;

- Exports of goods and services

- Services rendered at marines and airports for marine and air conveyances
- Supplies to persons engaged in petroleum exploration
- Supplies of goods to investment certificate holders
- Sales to the Directorate of the Defense Industry
- Sales to diplomats or diplomatic entities based on reciprocity principle
- International transport

Examples of partially exempt supplies of goods and services are;

- Leasing immovable property by an individual
- Financial transactions
- Supplies to certain cultural bodies
- Supplies by and to certain governmental bodies
- Water for agriculture
- The supply of unprocessed gold, foreign exchange money, stocks and bonds, duty stamps, scrap metal, plastic etc.
- Storage services performed at bonded warehouses or temporary storage places
- Delivery of goods or performance of services in free-trade zones

Time of supply

Time of supply for goods takes place when they are delivered and for services it takes place when they are performed. However, if the supplier issues an invoice before the time of supply, VAT applies to the extent that the supply is covered by the invoice. A prepayment or deposit does not result in a taxable transaction.

The time of supply for imported goods is either the date of importation, or the date on which the goods leave a duty suspension regime.

Taxable Base

The taxable base of a transaction is generally the total value of the consideration received, not including the VAT itself. The VAT Law deals with the taxable base under four headings, namely the taxable base on deliveries and services, on importation, on international transportation, and special types of taxable base.

In case a consideration does not exist, is unknown or is in a form other than money, the taxable base is the market value. Market value is the average price payable in the market for similar goods and services and is determined with reference to the Tax Procedural Law.

Recovery of input VAT

A taxable person may recover input VAT, which is charged on goods and services received for business purposes and related with taxable or fully exempt transactions.

Input tax includes VAT charged on goods and services supplied in Turkey, VAT paid on imports of goods, and VAT self-assessed on reverse-charge services.

A valid invoice or customs document must accompany to recover input tax.

The right of deduction may be exercised in the tax period in which the purchase documents are entered into the recipient's books of account, but only during the calendar year in which the taxable event takes place.

Non-deductible input tax: Input tax is not recoverable if it is charged on purchases of goods and services that are not used for business purposes and are considered to be non-deductible expenses for corporate tax purposes. In addition, input tax may not be recovered for partially exempt transactions (input VAT associated with passenger cars is recoverable only if they are rented or operated for a usage fee).

Partial exemption: An input tax deduction is granted for taxable supplies and for supplies that are exempt with credit. An input tax deduction is not granted for partially exempt supplies. If a taxable person makes both taxable and partially exempt supplies, it may recover only input tax allocated to supplies that are taxable or fully exempt.

Refunds: If the amount of input VAT recoverable in a period exceeds the amount of output VAT payable in the same period the excess amount is carried forward to following months. Refunds of the excess are available only for the following:

- VAT related to supplies of goods subject to a reduced rate
- VAT related to supplies of goods and services that are exempt with credit

The amount of the VAT refund may be credited against other tax liabilities.

Invoicing

Delivery of goods or performance of services should be invoiced within 7 days. Moreover, recipients of the supplies must retain copies of the invoices.

Foreign-currency invoices: An invoice issued for a domestic sale must be issued in Turkish lira (TL). The invoice may also show the invoiced amount in a foreign currency if the TL equivalents are stated. However, an invoice issued for an export sale may be issued in a foreign currency.

VAT returns and payment

Returns are filed on monthly basis and must be submitted by the 24th day of the following month.

Payment in full must be made in TL by the 26th day of the same month.

8.2 Special Consumption Tax

Special Consumption Tax is an excise tax and it is imposed on the import, manufacture and first acquisition of a range of goods.

Special Consumption Tax was implemented in August 2002 by abolishing 16 different indirect taxes and funds in order to make the indirect taxation system harmonized. Unlike VAT, which is applied on each delivery, Special Consumption Tax is charged only once. There are mainly 4 different product groups that are subject to Special Consumption Tax at different tax rates.

Scope of Tax

Goods in the Lists attached to the Special Consumption Tax Law are the subject of the tax.

There are mainly 4 different product groups that are subject to special consumption tax at different rates;

- List I is related to petroleum products, natural gas, lubricating oil, solvents and derivatives of solvents.
- List II is related to automobiles and other vehicles, motorcycles, planes, helicopters, yachts.
- List III is related to tobacco and tobacco products, alcoholic beverages and cola.
- List IV is related to luxury products (durable white goods, cellular phones, diamonds etc.).

The taxpayers of the Special Consumption Tax

Taxpayers are different according to the lists. They are;

For List I; manufacturers and importers of the petroleum products,

For List II; merchants of motor vehicles, importers for using or sellers through auction

For List III; manufacturers, importers or sellers through auction of tobacco, alcoholic beverages and cola.

For List IV; manufacturers, importers or sellers through auction of luxury products.

9. Income Tax on Individuals

Income tax is unitary in nature. The source of income is defined in 7 categories: Business profits, agricultural profits, employment income, professional income, rental income, interest & dividends, and other income.

The category of “other income” covers income, which do not fall under the first 6 categories, mainly being capital gains and income from certain incidental transactions.

There are two main types of tax statutes: resident taxpayers, and non-resident taxpayers. Residents are taxed on their worldwide income, whereas, non-residents are taxed only on their Turkish source income.

Turkish citizens, who work abroad, even if employed by companies with headquarters situated in Turkey or by the Turkish Government, are not subject to Turkish taxation in respect of income obtained and taxed outside Turkey.

A foreigner who spends less than a continuous period of six months in Turkey during a calendar year and whose centre of vital interest is not concentrated in Turkey or who, although stays in Turkey for more than six months but has come to Turkey for a specific and temporary assignment (e.g. businessman, expert, press or radio correspondent), is regarded as non-resident and is taxed accordingly.

9.1 Taxable Income

Gross Income

Taxable gross income includes amounts received from the following sources:

- Income from commercial activities,
- Income from agriculture,
- Income from professional services,
- Income from employment services (wages and salaries),
- Income from capital investments (interest and dividends),
- Income from immovable assets and rights (rental income), and
- Other income and earnings (capital gains, etc.).

With some exceptions, income (or losses) from the above categories is combined.

Exclusions and Exemptions

Certain amounts received by individuals need not to be reported for tax purposes. The followings are specifically exempt.

- Annual rental income up to 3.000 TL,

- Employment income wholly consisting of salaries derived from one resident employer, provided that all payments are taxed by withholding mechanism on payroll,
- Interest income which has been subjected to withholding tax at source,
- Half of dividend income received by a resident taxpayer from a resident corporation,
- Income derived by authors, sculptors, painters and composers, etc. and their heirs from copyrights and patent rights,
- Pensions and other social security compensations received up to certain levels,
- Reimbursement (made by the employer) of travelling expenses incurred by employees for business purposes,
- Salaries paid in foreign currency by the representative/liaison offices of foreign companies,
- Retirement and termination indemnity payments (maximum 2.805,04 TL for the first half of 2012)
- Capital gains from the disposal of Turkish corporation shares held for more than two years,
- Capital gains from the disposal of real estates retained by individuals for more than five years.

Deductions and Allowances

Turkish income tax law provides various deductions and allowances for each category of income. Some important deductions and allowances are explained below:

- Business expense deductions set out for companies are also applicable to individuals, to the extent that they relate to an individual's business income, and
- Compulsory pension contributions and social security premiums,
- ❖ The following benefits are not taxable from the employee standpoint:
 - Insurance premiums paid for the taxpayer and his family for death, sickness, disability, birth and education are deductible from the taxable salary. However, the insurance company should be established in Turkey and monthly insurance premiums should not exceed those established by law,
 - If meals are provided at the business premises, total payment made by the employer is tax exempted. Otherwise, only certain amount is exempted.
 - Transportation provided by the employer,
 - Accommodation provided by the employer, to the employees working in mining, factory and those whom the employee should provide accommodation in accordance with the special legislation. (which should be owned by the employer and not be more than 100 square meters),
 - Children allowance up to the amount received by a government employee, for maximum two children,

- Indemnity and assistance payments for reasons of death, disability, illness and unemployment,
- Assistance paid to employees because of marriage and birth, limited to two months' salary.
- ❖ Donations to government offices, municipalities, villages, associations in the public interest and foundations under the Civil Code of up to 5 % of taxable income, and
- ❖ Insurance premiums to the insurance companies established in Turkey for life, sickness, disability, motherhood, etc. up to 5 % (or 10 % in certain cases) of declared income and with a maximum of the minimum wage/salary for each member of the family. This deduction is not applicable for non - residents.
- ❖ Annual expenses incurred on education and health up to 10% of the income declared on the annual tax return are deductible,
- ❖ Effective from January 1, 2007, minimum subsistence allowance entered into force. Accordingly, it is adopted that an amount is calculated by multiplying the rate applied to the first income tax bracket of the income tax tariff with 50% for the taxpayer, 10% for his spouse not working or not having any income, 7,5% for the first two children and 5% for each of the children remaining, of the annual gross amount of the minimum wage (amount valid at the beginning of the calendar year when the wage is earned, for the employees who are above 16 and working in the industrial sector); then this amount can be deducted from the income tax to be calculated over the wage.
- ❖ Rental income earners may either itemize expenses related to immovable or may deduct a lump sum of 25 % of gross rentals expenses,
- ❖ In calculation of taxable capital gains, the cost of assets whose disposal led to capital gains may be indexed to the inflation only if the inflation during the holding period is in excess of 10%. Non-residents are allowed to eliminate foreign exchange gains when calculating the taxable gains from disposal of Turkish securities.

9.2 Income Tax Rates

Income tax rates applicable for year 2012 are as follows.

INCOME SCALES (TL) (NON-EMPLOYMENT INCOME)	RATE (%)
Up to 10.000	15
10.001-25.000	20
25.001-58.000	27
58.001 and upwards	35

INCOME SCALES (TL) (EMPLOYMENT INCOME)	RATE (%)
Up to 10.000	15
10.001-25.000	20
25.001-88.000	27
88.001 and upwards	35

Tax Credits

After tax has been calculated, credits against tax payable are allowed for;

- Tax withheld at source on certain income, and
- Foreign income tax that is limited to the amount of Turkish tax applicable to foreign income provided that the primary taxing right belongs to Turkey and certain conditions are satisfied.

Tax Credit on Dividends

Resident taxpayers have to include 1/2 of gross dividends received from a resident company in their taxable income. Withholding tax paid at source, however, is wholly creditable against tax calculated on the return.

Tax Returns, Filing, Payments

Tax returns must be filed by 25th March in the following year. Income tax is payable in two equal installments in March and July.

Non-residents are taxable on all earnings of income collected or realized in Turkey unless exempted. The filing requirements and taxation systems on non-residents in general, are as follows:

- Income from commercial and agricultural activities must be included in the tax return,
- Salaries, income from services and proceeds of sale of rights, interest, rent and dividends are subject to withholding tax. No further filing is required, and
- The proceeds of sale of real estate and income from movables that have not been subjected to withholding tax must be declared on individual declarations.

10. Labour

10.1 Labour Legislation

Turkish Labour Law practices derive mainly from two broad sources, namely the “official” and “private” sources of Labour Law. The Turkish Constitution of 1982 stands as the most prominent source and one, which takes precedence over other areas of legislation. The Labour Legislation in Turkey consists, at present, of the following acts: the Labour Act, the Maritime Labour Act, the Act Concerning Labour/Management Relations in the Press, the Trade Unions Act, the Collective agreements, Strikes and Lock-Outs Act, the Social Insurance & Unemployment Insurance Act, the Labour Courts Act, the National Holiday and General Vacations Act, the Weekend Holiday Act, the Employment Services Act, The Labour Office's Act, the Apprentice, Artisan and Master Workmen Act, The Civil Servants' Trade Unions Act, Employment of Foreign Employees' Act.

Weekly Working Hours and Vacations

In general the working week consists of a maximum of 45 hours. Total working hours may be divided freely among the working days; however, working hours cannot exceed 11 hours in any day.

Under Weekend Holiday Act (No: 394), it is obligatory to hold a holiday one day in a week. Employees are entitled to use minimum subsequent 24 hours weekend holiday in a 7 days working period. Nevertheless, on condition of obtaining permission, it is possible to keep the workplace open 7 days a week.

For example, large department stores can hold their workplaces open without holding a weekend holiday.

Under the National Holiday and General Vacations Act, the official holidays are the following:

- * January 1st, New Year's Day.
- * April 23rd National Sovereignty and Children's Day, 1 day.
- * May 1st, Labor and Solidarity Day
- * May 19th, Youth and Sports Day, 1 day.
- * August 30th Victory Day, 1 day.
- * October 29th the Republic Day, starts at 13.00 pm. on October 28 and continues on October 29.
- * Ramadan Holidays, 3.5 days, the dates vary, starts at 13:00 pm on the day before the religious day
- * Offering Holidays 4.5 days, the dates vary, starts at 13:00 pm on the day before the religious day

Overtime Work

The overtime work is defined as the working hours, which exceeds 45 hours in a week. The days on which overtime work is done cannot exceed 270 hours a year. Hourly wages for overtime is 50 % more than that for ordinary working hours. When overtime work is undertaken in the weekend holiday or on official holidays, the employee is entitled to an additional full day working wage. The consent of the worker is necessary for overtime work.

Vacation Pay

Workers who have been employed more than one year starting from the day he is entered to the place of work and including the period of probation are entitled to an annual paid vacation. The duration of the legal annual paid vacations are as follows:

- * 14 working days per year for service period from 1 year to 5 years,
- * 20 working days per year for service period over 5 years but less than 15 years,
- * 26 working days per year for service period over 15 years.

Employment Contracts

Work, which continues for maximum 30 workdays on account of its nature, is called temporary work, and work that lasts longer is called permanent work. In case of temporary work, a large number of provisions of the Labor Code are not applied.

Employment contracts that have duration of one year or longer should be concluded in written form. It is not necessary to execute these at the office of the notary public, and employment contracts are exempt from all taxes, duties and charges. Nevertheless, should the notary public certify the contract; a fee must be paid to it. In the case that the contract is not in written form (for jobs with a duration of less than one year), the employer is responsible for giving the worker a signed document specifying the general and special conditions of the job.

Work on Call Basis

“Work on call basis” is a newly defined part time employment agreement, where the employer requests from the employee to perform a specific work deemed necessary and the terms of such agreement should be drawn as a part time employment contract. In such a case, if not otherwise stated in the employment contract, the working hours are accepted as 20 hours in a week and at least 4 hours in a day. The call should be made at least 4 days before the starting date of the work.

Compensating Work

Employer has the right to request for compensating work within two months if the work is stopped due to the compulsory reasons or if the employees have holidays before and after the official and general holidays or work less than ordinary working hours or if a vacation right is given to the employee at his own request. Compensating work cannot be more than three hours in a day and cannot also exceed maximum working hours.

Termination of the Contract

When employment contracts for a definite period of time terminate on the date stipulated in the contract, no further financial responsibilities fall on the parties.

In case of permanent employment contracts for an indefinite period of time, matters pertaining to the annulment of the contract and the rights ensuing from this annulment can be summarized as follows:

Notice Pay

Prior to the annulment of permanent employment contracts for an indefinite period of time, notice should be given to the other party. Thus employment contract will be considered as annulled in:

- * 2 weeks from the date of notification for employment of 0-6 months,
- * 4 weeks from the date of notification for employment of 6 months-1.5 years,
- * 6 weeks from the date of notification for employment of 1.5 years-3 years, and
- * 8 weeks from the date of notification for employment of exceeding 3 years.

These intervals, so called the period of notice, may be extended, but not curtailed, through contracts.

The employer may cancel the employment contract by paying the employee his/her wage for this period in advance. Should the employee be dismissed for affiliation or making a complaint to a trade union, the wages mentioned are paid in 3-fold.

Severance Pay

The obligation to pay the worker a severance pay arises in the case the permanent employment contracts for an indefinite period of time are cancelled:

- * by the employer for reasons other than those stipulated in Article 25-II (Unethical behaviours of the employee) of the Labour Code,
- * by the worker in conformity with Article 24 of the Labour Code,
- * on account of obligatory military service,

- * a woman on her own volition terminates the service contract within one year from the date of her marriage, or
- * the termination of the contract with the death of the employee.

Severance pay is assessed according to the last wage received and number of the years worked for the employer. Such payments are calculated at a minimum 30 days' wage per year of employment at the rate of pay of which maximum amount is announced by the government applicable at the date of retirement or termination. In calculating the wage that will form the basis of the severance pay, any benefits other than wages that were given to the worker during the last year under various names and all privileges that accrue from the contract and can be measured in money will be taken into consideration.

Presently, the maximum severance pay for each year of employment is 2.805,04 TL (for the period 01.01.2012 – 30.06.2012).

Collective Layoffs

Collective dismissal of the workers from a workplace is defined under Article 29 of the Turkish Labour Law (No: 4857). Accordingly, if the number of the employees dismissed in a one month period is in the below mentioned ranges, then this should be deemed as "collective dismissal" and subject to special provisions:

- * between 20 and 100, at least 10 worker
- * between 101 and 300, at least 10 % of the workers
- * 301 and more, at least 30 workers.

In case of the above, the employer must inform the names and qualifications of these to the relevant Labour Office along with a reason for their dismissal at least one month following the date of dismissal so that workers can be placed in new jobs.

Furthermore, workers who have been dismissed by means of compliance with the periods of notice, or those that cancel the service contract on account of the emergence of force majeure conditions that necessitate the stopping of work at the workplace where the worker is employed for a period exceeding one week cannot be replaced by other workers within the 6 months following the date of dismissal or resigning.

The employer who wishes to reemploy workers for work of same nature during this period publishes the situation through suitable means, and notifies the former workers of the fact through the notary public. Workers who do not apply to the workplace within 15 days forfeit this right.

10.2 Labour Costs

Wage Regulation

There is no ceiling to the wages that can be given. On the other hand, wages cannot be below the minimum wage. The minimum conditions concerning wages have been specified in the Labour Code. However, the restrictions stipulated by the law may be altered in favour of the worker. The representatives of the government, workers and employers determine the minimum wages to be given in the agricultural and industrial sectors latest every two years. In recent years the minimum wage has been determined before the two-year period was over.

Monthly minimum wage applicable for the period of 01.01.2012 – 30.06.2012 and 01.07.2012 -31.12.2012 is determined respectively as 886,50 TL and 940,50 TL in gross terms. It is forbidden to employ workers at wages below this minimum. The employer is obliged to pay or to advance to all workers using their annual vacation the wages for the vacation period before the worker starts his/her vacation. Wages for the weekend holidays, national holidays and general holidays that coincide with the annual paid vacation period are paid separately.

Bonuses and Other Extra Payments

There are no legal obligations in this respect. They are determined totally by the own accord of the parties. Should a certain sum be given as a monthly wage or bonus, there will be no tax advantages.

10.3 Social Insurance- Health Insurance

Social Insurance

All workers and functionaries are considered as insured from the moment they start working. Prior to commencement of work, the company must be registered with the local labour office as an employer, and must register itself and each employee with the local social security office. The company has the responsibility for registering any employee subsequently hired within the month of his engagement.

Social insurance covers industrial accidents, occupational diseases, illness, maternity, disablement and death.

In the case the worker suffers an industrial accident in connection with his job at the work place or in another location or contracts an occupational disease, he/ she receives assistance for treatment, is paid wages for the periods he/she is unable to work, and when necessary he/she is provided with artificial devices and appliances.

This insurance branch is applied in general illness, accident and disablement cases other than industrial accidents and occupational diseases. For this purpose a physician, hospitalization, medication and treatment give the worker assistance for examination.

The spouse, children and parents of the worker also benefit from the sickness insurance.

The hospital treatments of the insured persons are carried out at the Social Security hospitals established for this purpose.

Maternity insurance provides for the extension of a certain and necessary assistance to the insured women and the non-insured wives of insured men in case of pregnancy and childbirth.

Social Insurance Premiums

Social security premiums are compulsory in respect of all persons earning salaries and wages.

Social insurance premiums are calculated on the basis of the monthly wages and are paid jointly by the worker and the employer at the following rates:

BRANCHES	EMPLOYEE (%)	EMPLOYER (%)	TOTAL (%)
Short Term Social Security Branches including occupational accidents and diseases (varies according to the job)	-	1 – 6,5	1 – 6,5
Disability, Old Age, Death	9	11	20
General Health Insurance	5	7,5	12,5
Total Minimum	14	19,5	33,5
Total Maximum	14	25	39
Unemployment insurance	1	2	3

The above rates are applied to the gross total of salaries, wages and bonuses up to a current maximum monthly of 5.762,40 TL and 6.113,40 TL respectively for the period of 01.01.2012-30.06.2012 and period of 01.07.2012-31.12.2012.

The premiums are paid each month to the Social Insurance Institution at the place where the worker is employed prior to the 30th day of the following month.

In calculating the income withholding tax on the wages by the employer, the employee contribution (e.g. 15 %) is deducted from the withholding tax base.

Health Insurance

As explained above, social insurance also includes health insurance. Furthermore, social insurance is compulsory. Individuals or enterprises, which wish to do so, cannot be released from the obligation of social insurance on the grounds that they have subscribed to a private health insurance scheme.

Social Security and General Health Law, numbered 5510, will be implemented after 01.01.2012. Accordingly, anyone resident in Turkey will be covered by the General Health Insurance according to the conditions of the 60th article of the Social Security and General Health Law.

Effective January 1, 2012 this law applies to foreigners who have been resident in Turkey more than 1 year.

The foreigners are required to apply to Social Security Institution within the one month after the completion of one year residence without interruption in Turkey. Otherwise, according to mentioned law article 102; these foreigners will be charged with interest applied by the Social Security Institution.

Foreigners entitled to social security in their home countries are not covered by the General Health Insurance in Turkey.

In Turkey many employers subscribe to private health insurance schemes for their employees in addition to the social insurance. They can, in this manner, ensure that their employees are examined and treated in better hospitals. However, a private health insurance is not obligatory. There are many insurance companies that offer health insurance schemes.

10.4 Rules applicable to expatriates

A foreign individual sent by a foreign company established abroad to carry out business on its behalf in Turkey who has notified the Department of Social Security that he is insured abroad will not be subject to Social Security deductions in Turkey.

International Agreements

Turkey has agreements with Germany, Austria, Belgium, Denmark, Sweden, Libya, Norway, UK, Switzerland, Netherlands, France, T.R.N. Cyprus, Azerbaijan, Romania, Albania, Bosnia Herzegovina, Czech Republic, Georgia, Canada, Quebec and Macedonia, Luxembourg, Bulgaria, Italy, Portugal and Spain. In case of individuals who are nationals of one of the above countries, which have social security tantalization agreements, the provisions of the above agreements have to be considered to determine their social security status in Turkey.

Except in the cases referred to above, a foreigner employed by a Turkish company is liable for full Social Security deductions as is the case for a Turkish national.

10.5 Collective Agreements - Trade Union Rights

Matters pertaining to collective agreements, strikes and lockouts have been regulated by Act Number 2822 dated 5.5.1983.

Collective Agreements

According to the law, collective agreements are agreements reached between the trade union and the employers' association or the non-affiliated employer for drawing up a service contract and regulating its content, termination and relevant matters.

Collective agreements can also contain provisions regulating the mutual rights and obligations of the parties, the implementation and supervision of the agreement and the methods to be applied for the settlement of the disputes.

Collective agreements have to be made in writing and can have duration of minimum one year and maximum 3 years. This period cannot be shortened or extended after the agreement has been signed.

The procedure for contracting a collective agreement has been stipulated by the law. This consists of, in the stated order, determining the unions that will make the agreement and obtaining the certificate of authorization for making an agreement, calling the other party to collective negotiations within 15 days from the date of receipt of certificate of authorization, specifying the venue, date and hour of the collective negotiations within 6 workdays following the forwarding of the call to the other party, carrying out the collective negotiations, and finally signing the agreement.

Strikes

In cases when the dispute in the collective negotiations cannot be settled, within the 6 days starting after 6 days have elapsed from the notification of the above mentioned document, a decision can be taken to strike. Strikes undertaken before the legal periods have elapsed are those for political purposes, general strikes and sympathy strikes that are illegal.

The cases of occupation of the workplace, slow-downs, decreasing efficiency and other types of job actions are subject to the same sanctions as illegal strikes. A strike or lockout that is in the nature of endangering public health or national security can be postponed for 60 days by the Council of Ministers.

Lockouts

The employers' association or the non-affiliated employer who is a party to the dispute can decide for a lockout within 6 workdays after the decision to strike adopted by the trade union has been notified to him/her.

Special arbitrator

The parties can with mutual consent refer to a special arbitrator at any stage of their dispute regarding collective rights and interests. A provision in the collective agreement to the effect that the matter can be referred to a special arbitrator through the application of one of the parties will be valid. In that case, the arbitrator upon the application of the party settles the dispute.

11. Mergers, Acquisitions and Reorganizations

11.1 Mergers

The absorption of one or more companies into an existing company where the absorbed company is deemed to be dissolved without liquidation is defined as a merger under Turkish Commercial Law. Turkish Commercial Law requires both the absorbing and absorbed companies to be in the same legal form. Where the companies are not in the same legal form, one of the companies has to be converted into the legal form of other before the merger can take place.

Taxable Mergers

A merger under the Turkish Commercial Law provisions is considered to be a taxable merger if the specific requirements for a tax free merger (pursuant to provisions of Articles 18, 19 and 20 of Corporate Tax Law) are not satisfied. In a taxable merger, the assets of the absorbed company are deemed to have been transferred at market value to the absorbing company which leads to taxable capital gains. The absorbing company is entitled to book the assets at their market values as their tax basis for depreciation purposes.

In a taxable merger, tax losses of the absorbed company cannot be transferred to the absorbing company. Nevertheless, the absorbed company can offset the existing tax losses against the capital gains arising from the transfer of assets through a taxable merger.

Tax Free Mergers

A merger under the Turkish Commercial Law provisions is recognized as a tax free merger (also known as a takeover) if the following tests are satisfied:

- Both the absorbing and absorbed companies are tax residents
- The absorbing company incorporates all assets and liabilities of the absorbed Company into its balance sheet on a carryover basis (i.e. no step up for the value of the assets)
- Other procedural and filing requirements are satisfied on a timely basis

Under a tax free merger

- The absorbed company is subject to the usual taxation rules for profits up to the date of the merger

- The absorbing company assumes all known or unknown tax liabilities of the absorbed company
- Tax losses of the absorbed company can be transferred to the absorbing company, if the absorbing company continues the business activities of the absorbed company minimum for 5 years following the date of the merger. However, tax losses that can be transferred to the absorbing company are limited to the shareholders equity of absorbed company as of the date of the merger
- The tax free merger does not affect the tax attributes of the absorbing company
- Shareholders of the absorbed company acquire shares in the absorbing company without changing the tax basis of their shares in the absorbed company.

11.2 Acquisitions of Companies

The following information provides a high level overview of the tax considerations that may be of interest for a foreign investor when planning an acquisition in Turkey:

Regulations for Acquisition

There are neither government controls nor restrictions on investments in assets, business entities or acquisition of other rights in Turkey. However, certain business activities require a regulatory approval before change of ownership (e.g., banking and insurance, telecommunications, tobacco and alcoholic beverages, production and distribution of energy, etc.). Acquisition of real estate in Turkey by foreign investors is also subject to specific regulations which need to be observed by the foreign investors.

Asset vs. Share Acquisition

A foreign company can acquire a Turkish company by acquiring either the assets or the shares of the target company. In case of an asset acquisition, this can be done either via a branch of the foreign entity, which is taxable in Turkey on non-resident status, or via a Turkish subsidiary of the foreign company. The respective tax implications are summarized below:

PURCHASE OF ASSETS

Acquisition of assets can be only done through a Turkish company or a Turkish branch of a foreign company.

Purchase Price

In principle, the transfer of assets under an asset-deal type transaction should be conducted at fair value, which should be the market value. Transfers between related parties must be documented to comply with transfer pricing requirements.

Goodwill

In case of an asset-deal, an excess of the purchase price over the fair value of the assets being transferred represent the goodwill, which can be capitalized by the buyer and depreciated for tax purposes over a period of five years. Turkish tax law does not require recognition of internally developed goodwill and rights in the tax basis balance sheet, so there is usually no tax basis cost for the goodwill in the seller's books and it, therefore, represents pure taxable income.

Depreciation

The depreciation period of assets are refreshed in an asset deal. The selling entity has the right to deduct all remaining net book value of assets as the tax basis cost against the transfer value; and the buyer has to book the assets at their transfer value and start depreciating a new term of useful life for each asset (as prescribed by the Communiqués of the Ministry of Finance).

Tax Attributes

The tax attributes (i.e. tax losses and incentives) are not transferred to a buyer in an asset deal. However, the selling entity has the right to use its existing tax losses and VAT credits against the taxable profits (such as capital gains) and VAT obligations arising from the asset transfer.

Value Added Tax ("VAT")

Transfer of assets through a regular asset purchase agreement is subject to VAT at regular rates depending on the type of assets being transferred (normally 18%). Real estate properties that are included in the asset purchase agreement could potentially be exempt from VAT if held for a period of more than 2 year.

The buyer has the right to get a deduction of the VAT incurred on asset deal against VAT generated from its sales. However, the full recovery of VAT can take time depending on the VAT generation of the acquiring entity, which leads to an additional cash flow problem on asset purchase transactions.

Transfer Taxes

In an asset deal, asset purchase agreement would usually be subject to 0.825% stamp tax on the basis of contract value whereas transfer of title to real estate subject to a title deed registration fee of 1.65 % both seller and buyer separately.

PURCHASE OF SHARES

Acquisition of shares by a foreign entity has no immediate Turkish income tax consequences.

Goodwill

If the acquisition is via a Turkish branch or subsidiary, goodwill implicit in the share price cannot be recognized for tax amortization purposes. There is no step-up availability for Target company assets.

Depreciation

A Turkish company buying the shares in another entity cannot depreciate the value of shares for tax purposes. The shares are booked at historical acquisition value and offset against future proceeds from sales as a tax basis cost.

Tax Attributes

A change in the shareholding will not have any effect on the tax attributes of the target company. Following the acquisition of shares, the target company can continue to carry forward its tax losses.

Value-Added Tax (VAT)

Share transfers by an individual are out of the scope of Turkish VAT. Where the transferor of shares is a corporate entity (e.g. a company or a branch) in Turkey, the transaction is principally in the scope of Turkish VAT. In this case, transfer of shares (in Joint Stock Companies) are exempted from VAT, however sale of participation shares (in Limited Liability Companies) by a Turkish entity can potentially attract Turkish VAT at 18% unless the participation shares are held for a period of more than 2 years.

Tax Indemnities and Warranties

In a share deal transaction, the historical tax liabilities of the target (known or unknown) remain in the company and are acquired by the new shareholder(s). It is, therefore, usual for the buyer to ask for tax indemnities and warranties in a share acquisition.

Transfer Taxes

Agreements relating to purchases and sales of shares are normally subject to stamp duty at 0.825 %. Agreements relating to transfers of shares of Turkish companies by other companies after a holding period of two years are exempt from stamp duties by virtue of the specific exemption provided by the Corporate Tax Law.

Concerns for the Seller

Sale of assets

The sale of assets of an entity is subject to usual corporate tax on the gains realized from the sale of the assets. Losses arising from the sale of assets are available

for immediate deduction or carry-forward. With respect to sale of certain fixed assets (e.g. real estate property), 75% of the gains realized from such sales may be exempted from corporate taxation provided that the real estate has been held for at least two years and the gains are retained in a special reserve account in the Balance Sheet for at least five years. Note that the transfer of the real estate property which has been held at least for two whole years by the companies is exempt from VAT.

Sale of shares

The sale of shares in another corporation is subject to corporate tax on the gains realized from the sale of shares. Losses are available to off-set income from other activities of the entity. The corporate tax exemption on 75% of such gains is available under the conditions mentioned above (i.e. 2 year holding period and requirement to retain the gains in a special reserve account for at least 5 years) in respect of sale of real estate property.

If the seller of the shares is an individual, capital gains derived by individuals on the sale of shares (of a Joint Stock corporation) held for more than two years are fully exempt from personal income tax; otherwise, if the shares are held less than two years, then the capital gains are subject to personal income tax at usual rates. (i.e. 15% to 35%). There are no similar exemptions for individuals in respect of capital gains arising from transfer of participation rights in a Limited Liability Company.

Please refer to our comments above with respect to VAT implications in case share transfer transactions.

Comparison of Assets and Share Purchases

In view of the above, please find below a summary of the tax considerations comparing an asset purchase transaction vs. a share purchase transaction:

Advantages		Disadvantages
A s s e t P u r c h a s e	<ul style="list-style-type: none">Purchase price can be depreciated or amortized for tax purposesStep-up in tax basis is obtainedPrevious liabilities of the seller not inheritedPossible to acquire part of a businessMore flexibility in fundingAbsorbing a profitable business into a loss-making company is possible	<ul style="list-style-type: none">Potential need to renegotiate the existing agreements, renew licenses etc.Potentially higher capital outlayMore transaction costs (stamp taxes, title registration fees etc)Likely to be unattractive to the seller (for tax purposes)Tax losses remain with the seller

	Advantages	Disadvantages
S h a r e	<ul style="list-style-type: none"> Purchase on net-asset basis, hence, lower capital outlay Likely to be more attractive to the seller (for tax purposes) 	<ul style="list-style-type: none"> Acquisition of potential tax liability due to difference between market value and tax basis of assets in the target company
P u r c h a s e	<ul style="list-style-type: none"> Acquire the tax attributes of the Target (i.e. tax losses) Continue to enjoy existing contracts, licenses, etc. 	<ul style="list-style-type: none"> Inability to recognize goodwill Acquisition of contingent (unknown) liabilities of the target

11.3 Corporate Reorganizations

Tax Free Spin-off

There are two types of tax free divisions allowed under the Turkish tax laws:

- A full division is reorganization where a company is divided into two or more existing or new companies while the transferring company is dissolved, pursuant to the provisions of Article 19-3-a of Corporate Tax Law. This type of division allows transfer of tax losses. By the introduction of the new Turkish Commercial Law effective from July 2012, it will be also possible to implement such a division from a Commercial Law perspective (which was not clearly regulated under the old Commercial Law).
- A partial division is reorganization where certain assets (i.e. participation shares or real estate property that has been held for a period of more than 2 years or complete production / service facilities) of a company are contributed into a new or existing company as capital in kind on a carryover basis, pursuant to the provisions of Article 19-3-b of Corporate Tax Law. A reorganization of a Turkish branch of a foreign company by way of a partial division has recently become possible provided that the transferee company is a tax resident.

Tax implications are similar as a tax free merger, except that transfer of losses is not possible under a partial division.

Tax Free Share Swaps

A share swap is a tax free transaction if the acquiring company receives the target shares in exchange for its shares to acquire control of management as well as a majority of shares in the target company. Although a tax free share swap is principally defined as a non-cash transaction, it is allowed to pay the shareholders of the company whose shares have been acquired up to 10% of the nominal value of the shares to be given to them.

Conversions

Conversions (i.e. change of legal form of a company) carried out under the requirements for tax-free mergers will not be considered as a taxable reorganization.

Liquidations

A Turkish Corporation may liquidate its assets and distribute the proceeds to its shareholders through a formal liquidation process to be carried out in accordance with Turkish Commercial Law requirements.

In the taxation of liquidations, financial period is replaced by liquidation period, which starts when a company is put into liquidation. The period between this date and the end of the same calendar year, as well as every calendar year following this date, is considered as a separate liquidation period. When liquidation is finalized, the final liquidation profit or loss is computed and the liquidation returns, which were previously filed, are corrected and, if necessary, taxes overpaid are refunded.

The company will be subject to usual taxation rules during the liquidation period and will be required to maintain all legal bookkeeping and filing obligations as a normal company.

The repayment of capital to shareholders at the end of liquidation does not trigger any taxes, but distribution of excess profits or reserves to the shareholders will attract dividend withholding tax at 15% (may be reduced by Double Tax Treaty provisions).

Note that it is statutory requirement for the tax office to carry out a tax audit upon the closing of liquidation.

12. APPENDICES

12.1 Appendix I: Chart of Principal Turkish Taxes

Corporate income tax	Increase in net worth	20 %
Advance corporate income tax	Net taxable income	20 %
Individual income tax		15 - 35 % (all source of income including salary income)
Value Added Tax – VAT	Sales value	
• General		18 %
• Certain products and services		8 %
• Certain products		1 %
Banking & Insurance Transaction Tax		
• General		5 %
• Interbank deposit transactions		1 %
• Repos		1 %
• Money market transactions between banks and brokers		1 %
• Sale of Government bonds and T-bills		1 %
• Sale of foreign currency		0 %
Stamp Duty (Where the stamp duties are payable, the amount of the stamp duty payable on each document is limited to 1.379.775,30 TL for the year 2012.)	Value specified in the documents	Usually at 0.825 % (0.165% for rental contracts, 0.66% for salaries)
Gift and Inheritance Tax	Value	1 – 30 %
Customs Duties	Value	Various
Transfer of real estate	Sales Value	1.65 %, each buyer and seller
Special Consumption Tax		
• Petroleum products	Per liter, kg, etc.	Specific 1 to 84 %
• Vehicles	Value and engine size	25% - 63% (*) and lump-sum
• Alcoholic beverages & tobacco products	Value, retail sale price for tobacco products	6.7 % – 20 %
• Certain luxury goods	Value	
Special Communication Tax	Service fee	
• Mobile telecommunication services		25 %
• Radio & Television broadcasting services through satellite or cable		15 %
• Wired, non-wired and mobile internet service providing facility		5 %
• Other telecommunication services		15 %
Lottery taxes (National Lottery, horse racing, Toto, lotto, etc.)	Various	Specific and ad valorem at 10 %
Motor Vehicle Tax	Model, engine, weight	Certain amounts revised each year
Major Municipal & Local Taxes:		
Real estate taxes	Tax Value	
* Buildings	Per tariff, gross profit	0.1 - 0.4%
* Land		0.1 - 0.6%
Entertainment tax	Fee	Specific, 0 - 20 %
Communication tax	Sales Value	1 %
Electricity & Gas consumption tax	Per flat and business premises	1 - 5 %
Environment protection tax		Certain amounts revised each year

(*) Only the percentage tax rate is applied provided that not being less than the tax calculated by using the minimum lump-sum tax amounts.

12.2 Appendix II: Chart of Withholding Tax

DESCRIPTION	TAX BASE	NON RESIDENT COMPANY (*) (%)	NON-RESIDENT INDIVIDUAL (****) (%)	RESIDENT COMPANY (**) (%)	RESIDENT INDIVIDUAL (****) (%)
Technical / Professional Services • General	Gross billings	20	20	n a	20
Construction projects lasting more than a calendar year	Progress billings	3	3	3	3
Salaries • Turkish payroll	Gross less social security contributions	-	15 - 35	n a	15 - 35
Rentals/Royalties	Gross	20	20	n.a	20
Financial Leases	Gross	1	n.a	n.a	n.a.
Dividends	Gross	15 (****)	15	n.a	15
Branch profits	Net profits less corporate taxes	15	n a	n a	20
Interest on loans	Gross	0 (*****) / 1/5/10	-	-	-
Sales proceeds: • of copyrights and patents • of other intangible rights	Gross billing	20 20	20 -	n a n a	17 -

* In the Article 30 of Corporate Tax Law, withholding tax rate applied to certain payments to non-resident companies is set as 15%. On the other hand, the Council of Ministers is authorized to reduce withholding tax rate to zero or to increase it to 30%.

** In the Article 15 of Corporate Tax Law, withholding tax rate applied to certain payments to resident companies is set as 15%. On the other hand, the Council of Ministers is authorized to reduce withholding tax rate to zero or to increase it to 20%.

*** Withholding tax rates applicable to resident and non-resident individuals are based on the Council of Ministers Decrees numbered 2011/1854, 2009/14593-4, 2006/11449, 2006/10731 and 2003/6577.

**** Except those who are receiving dividends via a fixed business place or a permanent representative.

***** Zero rate withholding tax is available depending on status of the foreign lender (i.e. banks and financial institutions). 1% interest on subordinated loan facilities to the Turkish banks being subject to the provisions of the supplementary capital in compliant to the Turkish Banking Law and interest on loans received by banks and other corporations by way of securitization based on a cash flow or an asset portfolio from abroad. 5% withholding tax is applied for interest on instalments or credit for the purchase of imported goods. 10% withholding tax is available on other loans and transactions that are not within the above mentioned loans.

12.3 Appendix III: Computation of taxes on the year-end profits

The corporate income tax will be calculated in its simplest form as follows:

Explanation	Calculations
Book profits adjusted for tax purposes	100
Corporation tax at 20 %	20
Available for distribution	80

The following tax computation may be more applicable in most of the cases.

Operating profits	500
Dividends from a resident company	250
Total book profits	750
Disallowable expenses	100

“No dividend policy” is assumed.

Computation of corporation tax would be as follows:

Book profits	750
Disallowable expenses	100
Tax adjusted profits	850
Exempt income	
Dividends	250
Taxable profits	600
Corporate tax base	600
Corporate tax at 20 %	120
Total taxes	120
Available for distribution	630

Dividend distribution and legal reserve requirements

When the company decides to distribute dividends, a withholding tax will be applied on the amount of dividends paid out (except for the dividends to resident entities or the Turkish branches of foreign corporations). The rate of withholding tax is 15 %. Consider the following example, with assumption that the paid in capital of the company is 100.000 TL and a full dividend policy is adopted.

Explanation	Calculations
Corporate profit	100.000
Corporate income tax at 20 %	20.000
Available for distribution	80.000
First legal reserves (5 % of net profits, up to 20 % of paid in capital)	4.000
Gross first dividends (5 % of paid in capital of 100,000)	5.000
Available for secondary dividends	71.000
Secondary legal reserves (1/11 of available for secondary dividends)	6.455
Gross secondary dividends	64.545
Gross dividends (first dividends and secondary dividends)	69.545
Withholding taxes on dividends at 15%	10.432
Net dividends	59.114

12.4 Appendix IV: Turkish Withholding Taxes by Treaty Countries

Country	dividends (%)	branch profits (%)	interest (%)	royalty (%)
Austria	5/15	5	10/15	10
Ireland	5/10/15	5	10/15	10
South Korea	15/20	-	10/15	10
Jordan	10/15	-	10	12
Tunisia	12/15	-	10	10
Romania	15	15	10	10
Netherlands	15/20	7.5	10/15	10
Pakistan	10/15	10/15	10	10
United Kingdom	15/20	15	15	10
Finland	15/20	15	15	10
T.R.N.Cyprus	15/20	15	15	10
France	15/20	7.5	15	10
Sweden	15/20	15	15	10
Belgium	15/20	15	15	10
Denmark	15/20	7.5	15	10
Italy	15	15	15	10
Japan	10/15	10/15	10/15	10
U. Arab Emirates	5/10/12	5/10/12	10	10
Hungary	10/15	10	10	10
Kazakhstan	10	10	10	10
Macedonia	5/10	5	10	10
Albania	5/15	5	10	10
Algeria	12	12	10	10
Mongolia	10	10	10	10
China	10	10	10	10
India	15	15	10/15	15
Malaysia	10/15	10	15	10
Egypt	5/15	5	10	10
Poland	10/15	15	10	10
Turkmenistan	10	10	10	10
Azerbaijan	12	12	10	10
Bulgaria	10/15	10	10	10
Uzbekistan	10	10	10	10
United States	15/20	15	15/10	10/5
Ukraine	10/15	10	10	10
Israel	10	10	10	10
Belarus	10	15	10	10

Country	dividends (%)	branch profits (%)	interest (%)	royalty (%)
Russia	10	10	10	10
Kuwait	10	10	10	10
Slovakia	5/10	10	10	10
Indonesia	10/15	10/15	10	10
Lithuania	10	10	10	10/5
Croatia	10	10	10	10
Moldova	10/15	10/15	10	10
Singapore	10/15	10	7.5/10	10
Kyrgyzstan	10	10	10	10
Tajikistan	10	10	10	10
Sudan	10	10	10	10
Czech Republic	10	10	10	10
Bangladesh	10	10	10	10
Latvia	10	10	10	5/10
Spain	5/15	5/15	10/15	10
Slovenia	10	10	10	10
Greece	15	15	12	10
Syria	10	10	10	15/10
Estonia	10	10	10	10/5
Thailand	10/15	10/15	10/15	15
Luxembourg	5/10/20	10	10/15	10
Iran	15/20	15	10	10
Saudi Arabia	5/10	5/10	10	10
Lebanon	10/15	10	10	10
Morocco	7/10	7	10	10
Rep. of South Africa	10/15	10	10	10
Portugal	5/15	5	10/15	10
Serbia Montenegro	5/15	5	10	10
Ethiopia	10	10	10	10
Bahrain	10/15	15	10	10
Qatar	10/15	10/15	10	10
Bosnia Herzegovina	5/15	5/15	10	10
Canada	15/20	15/20	15	10
New Zealand	5/15	5/15	10/15	10
Norway	5/15	5	5/10/15	10
Oman	10/15	10	10	10
Georgia	10	10	10	10
Yemen	10	10	10	10

Authors



Abdulkadir Kahraman
Tax Partner,
Head of Tax Services
T: +90 216 681 91 00 - 9004
E: akahraman@kpmg.com



Levent Berber
Head of Legal
Legal Financial Services
T: +90 216 681 91 00 - 9172
E: lberber@kpmg.com



Fikret Çetinkaya
Tax Partner
Tax Compliance Services
T: +90 216 681 91 00 - 9007
E: fcetinkaya@kpmg.com



Sami Şener
Tax Partner
Tax Compliance Services
T: +90 216 681 91 00 - 9021
E: ssener@kpmg.com



Ayhan Üstün
Tax Partner
Tax Consultancy Services
T: +90 216 681 91 00 - 9020
E: ayhanustun@kpmg.com



Ferrah Sefer Kurdoğlu
Tax Partner
Tax Compliance Services
T: +90 216 681 91 00 - 9019
E: fsefer@kpmg.com



Hakan Orhan
Tax Director
Tax Compliance Services
T: +90 216 681 91 00 - 9052
E: horhan@kpmg.com



Nihat Sönmez
Tax Director
Tax Compliance Services
T: +90 216 681 91 00 9048
E: nsonmez@kpmg.com



Feyyaz Yazar
Tax Director
Transfer Pricing Services
T: +90 216 681 91 00 - 9043
E: fyazar@kpmg.com



Yavuz Öner
Tax Director
Indirect Taxation Services
T: +90 216 681 91 00 - 9042
E: yoner@kpmg.com



Neslihan Reapers
Tax Director
Outsource Services
T: +90 216 681 91 00 - 9041
E: nraepers@kpmg.com



İbrahim Halil Öztürk
Tax Director
Customs Services
T: +90 216 681 91 00 - 9044
E: ibrahimozturk@kpmg.com



Eray Büyükkösekban
Tax Director
International Executive Services
T: +90 216 681 91 00 - 9049
E: ebuyuksekban@kpmg.com



Begüm Kitiş
Tax Director
Tax Consultancy Services
T: +90 216 681 91 00 - 9047
E: bkitis@kpmg.com



Didem Keşmir
Senior Tax Manager
Tax Compliance Services
T: +90 216 681 91 00 - 9119
E: dkemir@kpmg.com



Beyza Göktürk
Tax Manager
Legal Financial Services
T: +90 216 681 91 00 - 9143
E: bgokturk@kpmg.com

Contacts:

KPMG İstanbul
Kavacık Rüzgarlı Bahçe Mah.
Kavak Sok. No:29 Beykoz
34805 İSTANBUL
T: +90 216 681 90 00
F: +90 216 681 90 90

KPMG Ankara
Turan Güneş Bulvarı,
Galip Erdem Cad. No: 41
Yıldızevler - Çankaya
06650 ANKARA
T: + 90 312 491 72 31
F: + 90 312 491 71 31

KPMG İzmir
1456 Sok. No: 10/1 K:11
Punta İş Merkezi
Alsancak 35220 İZMİR
T: + 90 232 464 20 45
F: + 90 232 464 21 45

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional after a thorough examination of the particular situation. KPMG International is a Swiss cooperative. Member firms of the KPMG network of independent firms are affiliated with KPMG International. KPMG International provides no client services. No member firm has authority to obligate or bind KPMG International or any other member firm vis-a-vis third parties, nor does KPMG International have any such authority to obligate or bind any member firm.

© 2012 Yetkin Yeminli Mali Müşavirlik A.Ş., a Turkish corporation and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative, a Swiss entity. All rights reserved. Printed in Turkey.