

## **TURKISH TAX SYSTEM IN GENERAL**

The Turkish tax regime is an important part of the economy and can be divided into three main categories:

Income Taxes, such as Individual Income Tax and Corporate Income Tax

Taxes on Expenditure, such as Value Added Tax or Banking and Insurance Transaction Tax or Stamp Tax

Taxes on Wealth, such as Property Tax or Inheritance and Gift Tax

### **INCOME TAX**

An individual is subject to the income tax on his income and earnings. The rules of taxation for individual income and earnings are provided in the Income Tax Law 1960 (ITL).

#### **Liability**

Individuals who are resident in Turkey are subject to tax on their worldwide income and they are regarded as “*full tax liable*” in Turkey.

Nonresidents are taxed only on earnings and revenues derived in Turkey and they are regarded as “*limited tax liable*” in Turkey.

Residents include individuals with legal permanent residence in Turkey and those who reside in Turkey for more than *six months* during one calendar year (Provisional absence shall not interrupt the continuity of residing in Turkey).

In addition to residency criterion, within a limited scope, nationality criterion also applies regardless of their residency status, Turkish citizens who live abroad and work for government or a governmental institution or a company whose headquarter is in Turkey, are considered as unlimited liable taxpayers. Accordingly, they are subject to the income tax on their worldwide income.

Disregard the six-month rule in item above has a special exception that applies to expatriates such as businessman, scientists, experts, employees of governments or journalists who come to Turkey to perform temporary and pre-defined work as well as those who have arrived for the purpose of education, medical treatment, rest and travel. Such persons will still be considered as non-resident even if they stay in Turkey longer than six months in a calendar year.

Generally, if an individual is a non-resident of Turkey under these rules, he will also be a non-resident for purposes of the application of Turkey's tax treaty network. This may affect the taxation of non-Turkish income in the source country.

### **Taxable Income**

Turkey has a unitary tax system under which income derived from different sources is aggregated and tax due is computed on the total aggregate income. Tax is imposed on a calendar year basis in Turkey. Income derived in Turkey by residents and non-residents are categorized into seven categories.

These seven categories are:

1. Business income
2. Agricultural income
3. Salary and wage income
4. Self-employment earnings
5. Revenues from immovable properties
6. Income from capital investments
7. Other earnings and gains (i.e. capital gains)

Residents who have full tax liability status in Turkey are taxed on their income derived both in Turkey and outside Turkey.

The sources of income in Turkey for "*limited liable taxpayers*"(non-residents) are determined as follows:

*Business profit:* Income derived from every kind of business through a permanent establishment or permanent representatives in Turkey, is considered as income derived in Turkey.

*Agricultural income:* Income arising from agricultural activities carried out in Turkey is considered as derived in Turkey.

*Wages and Salaries:* Fulfillment of the following conditions indicates that the wage income is acquired in Turkey for individuals with limited liability:

- If the employment service is performed in Turkey or,

- If the services are “evaluated” in Turkey.

An employment service will be considered as having been evaluated in Turkey, if the salary amount is paid in Turkey or it is booked as cost or expense by the Turkish entity.

*Income from Independent Personal Services:* Independent personal services must be performed or accounted for in Turkey.

If the self-employment activities are performed in Turkey or the self-employment activities are evaluated in Turkey, this indicates that self-employment earnings are acquired in Turkey for individuals with limited liability.

Services which are rendered by resident and/or nonresident individuals are subject to withholding tax of 20% and the recipient of the services files a WHT return to the tax office on behalf of the professionals. If the service provider is nonresident, provisions of DTTs are taken into consideration. Provisions of DTTs might prevent taxation of such income in Turkey.

*Income from Immovable Property:* Revenues acquired from rental of immovable properties and rights by their owners, by their holders, by those holding easement and usufruct rights or by their tenants are taxable in Turkey (if the immovable property is located in Turkey or if such properties and rights are used or evaluated in Turkey).

Property and rights which are subject of rental income are defined in Article 70 of Income Tax Law. They are mentioned as;

- Land, building, mineral water and underground water sources, mines, stone pits, production places of sand and gravel, brick and tile fields, saltworks and their component parts; • Large fishing net fields and fishponds;
- Component parts of immovable properties leased separately and all their installations, inventory stock and flooring;
- Rights registered as immovable property;
- Searching, operating and franchise rights and their licenses, patent right, trademark, commerce title, any kind of technical drawing, design, model, plan and cinema and television films, audiotapes and videotapes, a secret formula acquired in industry, commerce and science or rights as right of usage or privilege of usage on a production method;

- Copyrights,
- Ships and shares of ship and all the motorized shipment and unloading vehicles;
- Motorized transfer and draw-frame vehicles, any kind of motorized vehicle, machine and installation and their appurtenance.
- Rights considered as immovable must be used or accounted for in Turkey.

Rental income derived by resident and nonresident individuals from immovable assets and royalties for patents and rights are subject to WHT at a rate of 20%. This WHT may be eliminated or reduced under applicable DTTs if the income is derived by non-resident individuals.

*Other Income and Earnings:* The activities or transactions generating for other income, specified in the Income Tax Act, must be performed or accounted for in Turkey. The following types of income are included in investment income;

- Dividends from all types of share certificates
- Earnings arising from participation shares
- Profits distributed to the chairman and members of the board of directors of companies
- Interest income derived from public and private bonds and treasury bills
- All interest income (Time deposits, repo and others)

### **Tax Rates**

In principle, individual income and gains are subject to income tax at progressive tax rates which vary between 15% and 35% and calculated on a cumulative basis. The personal income tax rate varies from 15% to 35%. Income tax rates applicable to yearly gross earnings from 2012 are as follows:

<b>Exceeding TL</b>	<b>Not Exceeding TL</b>	<b>Tax On Lower Amount TL</b>	<b>Tax Rates on Excess (%)</b>
<b>0</b>	10.000	-	15
<b>10.000</b>	25.000	1.500	20
<b>25.000</b>	58.000	4.500	27
	(88.000 for wage income)		
<b>58.000</b>	-	13.410	35
(88.000 for wage		(21.510 for wage	

## **Deduction**

Individuals who render independent professional services or those who are carrying out commercial activities may deduct ordinary business related expenses, including salaries, rental payments, fees and the cost of utilities from taxable income. Depreciation on fixed assets is also allowed. Penalties shall not be deductible.

*Business Profits:* In order to determine net amount of business profits on the actual basis, the following expenses may be deducted from revenues:

- general expenses made for earning and maintaining business profit;
- food and boarding expenses provided for employees at the place of business or in its annexes;
- expenses for medical treatment and medicine;
- insurance and pension premiums;
- clothing expenses paid for employees;
- losses, damages, and indemnities paid based upon written agreements, juridical decrees, or by order of law;
- expenses for travel and lodging relevant to the business;
- expenses for vehicles which are part of the enterprise and used in the business;
- taxes in kind such as building, and consumption, stamp and municipal taxes and fees and charges, related to the business;
- depreciations set aside according to the provisions of the Tax Procedure Law;
- payments to the unions;

The employee parts of social security contributions and unemployment insurance premiums shall be deductible from gross employment income in determination of the income tax base.

The premiums paid by the employee for himself, his/her spouse or children related to the personal insurance policies covering life, death, accident, illness, disablement,

unemployment, maternity, birth and education, as well as the contributions paid to the Individual Retirement System can be considered as deduction in determination of income tax base. However, the following conditions should be fulfilled in order to apply the deduction:

- The insurance policy and the retirement contract should be concluded with an insurance company which is situated in Turkey and whose headquarters is in Turkey,
- The amount of the monthly premium, membership fee or contributions that are paid to Individual Retirement System, should not exceed 10% of the salary earned on that month (The premiums paid for the personal insurance policies other than Individual Retirement System should not exceed 5% of the wage earned on the month when the premium was paid).
- The annual totals of the monthly premiums, membership fees and contributions paid, should also not exceed the annual total amount of the legal minimum wage.
- Lighting, heating, water, elevator, administration, insurance, interest, tax and duty, depreciation and maintenance expenses paid by the individual who gains rental income can be deducted from taxable rental income. On the other hand, taxpayers may also choose lump-sum method which allows the deduction of 25% of the gross rental income instead of above mentioned expenses.

*Agricultural Income:* Small farmers are exempt from tax if a farmer's gross revenue or operational size of his farming enterprise is less than the amount specified by the Income Tax Law, then he is accepted as a small farmer for the application of income tax and exempt from the income tax.

On the actual basis, the following expenses are deducted from the gross revenue to reach taxable income for the year.

- expenditures made for obtaining seed, fertilizers, seedling plants, animal feeds and similar materials;
- expenditures made for purchasing animals, agricultural products and other materials which are acquired for the purpose of resale;
- salaries and wages paid to the employees;
- operation and maintenance expenses of agricultural machinery; equipment, and vehicles;
- depreciation expenses;

- rents and fees paid for machinery and equipment,
- interest incurred for loans received and used for enterprise,
- general expenses made for earning and indemnities paid based upon written agreements, juridical decrees, or by order of law;
- losses incurred in the selling of fixed assets (except immovable used in agricultural activities) which are part of the enterprise;
- full depreciation expenses and half of other expenses of the vehicles which are part of the enterprise and also used for personal and family needs.

*Salaries/Wages:* In determining taxable amount of salaries and wages the following expenditures are allowed to be deducted from gross amount:

- Legal deduction made according to various laws or regulations,
- Payments made for pensions,
- Payments made for various insurances,
- Payments made for labor union membership,

*Income from Immovable Property:* In computing net income from immovable property, costs related to maintenance, management, renovation and running, and depreciation may be deducted from the gross income on the actual basis, it is also allowed to make a lump-sum deduction instead of actual costs, except for the income from the lease of the rights mentioned above. In such cases, lump-sum deduction is 25 per-cent of the rental income.

*Income from Movable Property:* In determining net income from movable property, costs related to and allowed to be deducted from gross income include insurance costs, collection costs, and taxes and other levies, excluding income tax, paid for securities.

The mentioned elements are included in business profit when they are connected to the business activity of the recipient. In such case, this income is treated as business profit and become subject to the rules described earlier related to the rules described earlier related to the business profit.

*Other:* Net amount of capital gains is determined by deducting acquisition costs and the costs incurred to the alienation of the capital assets from the proceeds received in return of the alienation.

## **The Minimum Living Allowance**

“The Minimum Living Allowance” can be deducted from the tax on employment income. The minimum living allowance base applicable for each month of employment is;

50% of the monthly gross amount of legal minimum wage that is effective at the beginning of the calendar year (TL 796,50 for 2011) for the employee himself,

10% of the monthly gross amount of legal minimum wage mentioned above for a spouse who is unemployed and does not earn income

7,5% of the monthly gross amount of legal minimum wage mentioned above for the first two children and 5% for other children

The tax credit is calculated by multiplying the total minimum allowance amount by 15%. However, the credit cannot exceed the total tax calculated on the employment income and no refund is granted in the event of an excess amount.

Minimum Living Allowance is not applicable for non-resident individuals who derive employment income in Turkey.



## **CORPORATE TAX**

The rules concerning the taxation of corporations are contained in the Corporation Tax Law, No: 5520 (CTL).

### **Liability**

Companies whose legal or business headquarters (as stated in their articles of association) are located in Turkey or whose operations are centered and managed in Turkey are subject to corporation tax on their worldwide income. In Turkish tax legislation, they are described as “*full liability taxpayers*”; they are also known as resident companies.

Taxable income of “*limited liability taxpayers*” (nonresident companies or taxpayers other than full liability taxpayers) is comprised of the following:

- Professional fees obtained in Turkey
- Profits from commercial, agricultural and industrial enterprises in Turkey (if they have an establishment or a permanent representative in Turkey)
- Income arising from rental of real estate, rights and movable property in Turkey
- Income obtained in Turkey from various types of securities
- Other income and revenue obtained in Turkey

The term legal head office, as used in the context of the Corporate Tax Law, means the office specified in the written agreements of the mentioned entities. Therefore, it is not difficult to ascertain where the legal head office of a company is located. However, the place of effective management, which is defined as the place in which the business activities are concentrated and supervised, is not easy to determine in some cases. As may be expected, the Law defines the term limited tax liability quite parallel to term unlimited tax liability, as the liability requiring to tax only the income derived in Turkey, provided that both legal head office and the place of effective management are abroad.

### **Taxable Income**

The corporate tax is levied on the income and earning derived by corporations and corporate bodies. The income elements by Corporate Tax Law are the same as those covered in the Income Tax Law.

- Corporations and corporate bodies specified by the Law as taxpayers in respect to the corporate tax are as follows:

- Capital companies and similar foreign companies;
- Cooperatives;
- Public enterprises;
- Enterprises owned by foundations societies and associations;
- Joint ventures.

### **Tax Rates**

For 2012, the corporate tax rate is 20%. However, incentive programs provide for reduced corporate tax rates for income from certain investments in certain sectors.

### **Corporation Tax Exemptions**

#### ***Participation Exemption***

Dividend income derived from Turkish (resident) participations. Corporate Tax Law provides a participation exemption for dividends derived by companies from Turkish (resident) participations. Dividends qualifying for the participation exemption are fully exempt from corporate tax.

To qualify for the participation exemption, a Turkish resident company need only hold a participation in another Turkish resident company.

Dividend income derived from foreign (nonresident) participations. The Turkish tax law also provides a participation exemption for dividends derived by companies from foreign participations. Dividends qualifying for the participation exemption are fully exempt from corporate tax.

To qualify for the participation exemption for dividends derived from foreign participations, all of the following conditions must be satisfied:

- The Turkish company must have owned at least 10% of the shares of the foreign company for an uninterrupted period of at least one year as of the date of receiving the dividend.
- The foreign company must be a limited or joint stock company.
- The foreign company must be subject to corporate tax at an effective rate of at least 15% (for corporations whose principal activities is the procurement of finance and insurance, the rate must be at least the rate of corporation tax in Turkey, which is 20% for 2012).
- The dividends must be transferred to Turkey by the due date of filing of the annual corporate tax return (25 April).

The participation exemption also applies to income derived from permanent establishments (PEs) and permanent representative resident abroad if the following conditions are met:

- The PE or permanent representative is subject to corporate tax at an effective rate of at least 15% in the country where the PE or permanent representative is located. For PEs whose principal activities are the procurement of finance, including financial leasing, or investment in marketable securities and insurance, the rate must be at least the rate of corporation tax in Turkey, which is 20% for 2012.
- Income derived from foreign PEs must be transferred to Turkey by the due date of filing of the annual corporate tax return (25 April).
- Special participation exemption rules apply to companies established in foreign countries whose principal purpose is construction, repair, assembly and technical services. If, under the laws of a foreign country, the establishment of a corporation is necessary to undertake these activities, dividends repatriated by the foreign subsidiary to the Turkish parent company qualify for the participation exemption, regardless of whether the conditions described above for the participation exemption are satisfied.

A participation exemption also applies to capital gains.

### ***International Holding Companies Regime***

A special regime applies to international holding companies.

International holding companies may benefit from the participation exemption with respect to dividends derived from foreign participations if they satisfy the conditions

applicable to other entities. They also may benefit from the participation exemption with respect to capital gains, but different conditions apply. Turkish international holding companies benefit from the participation exemption with respect to capital gains if foreign participations account for at least 75% of the noncash assets of the international holding company and if the international holding company has held a shareholding of 10% or more in the foreign limited or joint stock company for at least two years.

Additionally, dividends distributed by Turkish international holding companies to nonresident companies out of profits derived from their foreign participations, are subject to one-half of the general 15% WHT rate on dividends. Therefore, the dividend WHT rate can be applied as 7.5%.

### ***Others***

Corporation tax exemptions are available under the participation exemption and the international holding regime. In addition, the following corporate tax exemptions apply to Turkish and foreign investment funds and companies:

- Profits derived by mutual funds (excluding foreign-exchange funds) and trusts from transactions involving their operating portfolio
- Profits derived by risk capital investment funds or companies from transactions involving their operating portfolio
- Profits derived by real estate investment funds or companies from transactions involving their operating portfolio
- Profits derived by designated private pension investment funds

### **Capital Gains**

Capital gains derived by all companies, including branches of foreign companies, are included in ordinary income and are subject to corporation tax. Capital gains are generally computed by subtracting the cost of the asset, including the related expenses paid by the seller, from the selling price.

Capital gains derived from sales of depreciable fixed assets are not taxable to the extent the gains are reinvested in new fixed assets. However, the amount of gains used to acquire new assets is subtracted from the depreciable cost of the new asset. Capital gains that will be used for reinvestment are transferred to a special reserve account. If the special reserve is not

used to finance the purchase of similar new assets in the following three years, the balance in the reserve is included in taxable income.

Capital gains derived from sales of resident companies' shares by nonresident companies without a permanent establishment in Turkey are subject to corporation tax. In computing these gains, changes in exchange rates are not taken into account.

Seventy-five percent of capital gains derived by corporate taxpayers from the disposal of shares owned for at least two years qualify for corporate tax exemption if the gains for which exemption is claimed are recorded as a special fund under the shareholder's equity account in the balance sheet until the end of the fifth year following the year of sale.

### **Dividends**

Dividends received by resident companies from other resident companies are not subject to corporate tax. Dividends received from foreign companies are included in taxable income. However, certain dividends received from foreign companies may qualify for exemption from corporation tax under the participation exemption or the international holding regime.

15% WHT is imposed on dividends paid by resident corporations to the following recipients: resident individuals; resident recipients who are not subject to corporation tax and income tax, or are exempt from such taxes; nonresident individuals; nonresident corporations (excluding those receiving dividends through a PE or permanent representative in Turkey); and nonresident recipients who are exempt from corporation tax and income tax.

A branch remittance tax is imposed at a rate of 15% on profits remitted by nonresident corporations that have a PE or permanent representative in Turkey to their headquarters.

### **Foreign Tax Relief**

Corporation tax and similar taxes paid abroad on income that is derived abroad and that is included in the Turkish accounts may be offset against the corporation tax that is assessed on such income in Turkey.

In cases in which the controlled foreign company (CFC) rules are applied, the taxes similar to income and corporation taxes that the foreign affiliate has paid can be set off against the corporation tax that is calculated on the basis of the earnings of the foreign company.

Resident companies that have a direct or indirect participation in shares or voting rights of 25% or more in foreign subsidiaries can claim a tax credit for the corporate or income tax paid by foreign subsidiaries in their jurisdictions on profits out of which dividend distributions were paid to the resident companies. The credit is limited to the tax in Turkey that is attributable to the dividend distributions. As a result, the credit applies only to dividends that do not qualify for the participation exemption.

Amounts that are set off against the taxes that are assessed in Turkey on the income derived from the foreign countries may not exceed the tax amount that would be calculated by applying the local corporation tax rate (20%) to such earnings.

Foreign taxes that cannot be offset against the corporate tax in Turkey because of insufficient corporate income may be carried forward for a period of three years. The tax credit can also be offset against advance tax payments.

### **Deduction**

In essence, the provisions of the income Tax Law concerning the determination of business profit also applies to the procedure required in determining corporate income. Basically, net corporate income is defined as the difference between the net worth of assets owned at the beginning and at the end of the fiscal year. In addition to the expenses mentioned in article 40 of Income Tax Code allowed to be deducted from revenues, the followings may also be deducted regarding to the determination of business profit, by corporations:

- expenses related to the issuance of stocks and shares;
- initial organization and establishment expenses;
- expenses incurred for general board meeting as well as expenses made for mergers dissolutions, and liquidations;
- in case of insurance companies, technical reserves required for the insurance contracts still valid at date of inventory;
- profits shares accrued to active partners of partnerships in commendams limited by shares;
- profit shares accrued to partners by participation banks for participation accounts;

- research and development deductions calculated as %40 of new technology and know-how research expenses realized within business.

All business-related expenses are deductible, with the following exceptions:

Interest on shareholder's equity or on advances from shareholders.

Reserves set aside from profits (except technical reserves of insurance companies and doubtful debts from debtors against whom legal proceedings have been instituted).

Corporation tax and all monetary and tax penalties and interest imposed on such tax.

Discounts or other losses arising from selling the corporation's own securities for less than par value.

For nonresident companies, commissions, interest and other charges paid to headquarters or other offices outside Turkey on purchases or sales made on their behalf, as well as allocated charges to contribute to losses or expenses of headquarters or branches outside Turkey. However, charges are deductible if they are made in accordance with allocations keys that are in compliance with the arm's length principle and if they are related to the generation and maintenance of business income in Turkey.

Interest, foreign-exchange differences or comparable expenses that are calculated or paid on disguised capital

Disguised profit distribution through improper transfer pricing.

## **VALUE ADDED TAX (VAT)**

All deliveries of goods and services that take place in Turkey in the context of commercial, industrial, agricultural and professional activities are subject to VAT. Goods and services imported and deliveries and services arising from other activities are also subject to VAT.

In general, the person liable for the payment of VAT is the one who delivers and imports the goods or performs the services. The input VAT that a taxpayer pays for goods and services purchased can be offset against (deducted from) output VAT calculated on deliveries of goods and services. In case the amount of output VAT on sales is greater than the input VAT, the positive difference becomes payable. In case the amount of output VAT is less than the input VAT, the difference can be carried forward and can be offset against oncoming output VATs.

### **Liability**

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

No VAT registration threshold applies. VAT registration is granted automatically by the tax office when a business registers for corporate and income tax purposes. It is necessary to have a fixed place of business to register for tax registration. A fixed place of business includes a residence, place of business, registered head office or business center in Turkey. Only entities that are registered for tax may import goods into Turkey.

*Group registration:* VAT grouping is not permitted under Turkish VAT law. Legal entities that are closely connected must register for VAT separately. Related parties are regarded as separate for tax purposes.



*Nonestablished businesses:* A “nonestablished business” is a business that has no fixed establishment in Turkey. A nonestablished business may not register for VAT only. If a Turkish taxable person receives services from an entity that does not have a fixed establishment in Turkey, VAT is accounted for using the reverse-charge mechanism (that is, the Turkish recipient of the service must self-assess VAT).

Reverse charge: The reverse charge is a form of self-assessment for VAT through which the recipient of services accounts for the tax. The reverse charge applies if certain services 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. The Ministry of Finance is authorized to determine the parties responsible for the payment of VAT. The recipient does not need to be a taxable person under Turkish VAT law. The recipient may be an individual or an institution.

The reverse charge applies to the following services performed or used in Turkey:

- Transfers of copyrights, patents, licenses, trademarks, know-how and similar rights
- Import commissions
- Services of independent professionals, such as engineering, consulting, data processing and provision of information
- Interest payments made to foreign entities other than banks and financial institutions
- Rental services
- 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

*Penalties for reverse-charge supplies:* Penalties apply to several VAT offenses, including failure to account for VAT under the reverse-charge mechanism. The penalty equals 100% of the tax that has not been accounted for. The interest applies from the due date of the tax payment to the date on which the penalty notice is issued.

## **Taxable Transactions**

Taxable transactions defined in VAT Law include the supply of goods and services, importation of goods and services and other activities.

The following transactions carried out in Turkey are subject to VAT:

(a) Supply of goods and services within the scope of commercial, industrial, agricultural or independent professional activities,

(b) Importation of all kinds of goods and services,

(c) Other activities;

- Postal, telephone, telegram, telex and other similar services; radio and television services,

- Organization of all kinds of betting, gaming and lotteries including authorised public lotteries,

- Organization of shows, concerts and sporting events with the participation of independent professional artists and professional sportsmen,

- Sales at customs bonded warehouses and in auctions,

- Transportation of petroleum and gas and their products through pipelines,

- Leasing of the goods and rights stated in Article 70 of the Individual Income Tax Law,

- Deliveries and services of a commercial, industrial, agricultural or professional nature performed by enterprises that belong to national and local government agencies and establishments, universities, associations, foundations and all kinds of professional organizations,

- Deliveries and services deemed to be taxable upon voluntary registration with the tax authorities, to avoid uncompetitive pricing.

Any real person or legal entity, resident or non-resident, private or public, engaged in the above transactions is subject to tax. Exemptions granted under other tax laws are not valid for VAT purposes if they concern an activity that falls within the scope of the VAT Law.

### **Tax Rates**

The term “taxable supplies” refers to supplies of goods and services subject to VAT. The term “exempt supplies” refers to supplies of goods and services not subject to VAT. “Partially exempt” supplies (as specified in Articles 16 and 17 of the VAT Law) do not give

rise to a right of input tax deduction (see Section F). Some supplies are classified as “fully exempt,” which means that no VAT is chargeable, but the supplier may recover related input tax. These supplies include exports of goods and related services.

In Turkey, the following are the VAT rates:

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.

The following tables list examples of partially exempt supplies of goods and services, fully exempt supplies of goods and services, and supplies of goods and services that are taxed at the reduced VAT rates.

Examples of partially *exempt supplies* of goods and services:

- 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 and certain other items
- Storage services performed at bonded warehouses or temporary storage places
- Delivery of goods or performance of services in free-trade zones

Examples of fully *exempt with credit* supplies of goods and services:

- Exports of goods and services
- Services rendered at marinas and airports for marine and air conveyances
- International transport
- Supplies to persons engaged in petroleum exploration

- Supplies of goods to investment certificate holders
- Sales to the Directorate of the Defense Industry

Examples of goods and services taxable at 1%:

- Newspapers and magazines
- Basic foodstuffs
- Used passenger cars

Examples of goods and services taxable at 8%:

- Foodstuffs
- Books
- Pharmaceuticals
- Medical products
- Some construction equipment
- Admission charges for cinemas, theaters, and operas

*Excise tax:* An excise tax is imposed on the import, manufacture and first acquisition of a range of goods. The following are the groups of products subject to excise tax:

- Petroleum, gas and derivatives
- Automobiles and other vehicles
- Tobacco and specific beverages
- Luxury products

### **Type of Exemptions**

#### *Full Exemptions*

With right of deduction and with right of refund

- Exportation exemption
- Exemption for sea, air, and railway vehicles
- Services provided to sea and air transportation vehicles

-Petroleum explorations

-Exploring, processing, enrichment and refining activities for precious metals

#### *Partial Exemptions*

Input VAT can't be deducted and refunded, therefore the input VAT charged on invoices is either expensed or "cost of goods"

-Exemption for transitions, transferring, transformation, division transactions of enterprises

-Exemption for participation shares and sales of immovables of corporations

-Exemption for delivery of participation shares and immovables to banks as recompensation claims

#### **Non-Deductible VAT (Cost Or Non-Deductible Item Or Capitalised)**

In the following cases, VAT may not be credited from the VAT computed on taxable transactions:

-VAT on purchases of cars (which should be recorded as an expense or cost).

-Missing and stolen stocks (excluding those lost due to fire in places of compelling reason declared by Ministry of Finance).

-VAT on non-deductible expenses.

-Input VAT on exempt deliveries listed in Article 17 of the VAT Law.

#### **VAT Refund**

Value Added Tax (input VAT) shown on invoices and similar documents related to the transactions which are exempt from the tax, such as:

-Exportation of goods and services,

-Exemption for vehicles, petroleum exploration and investments made under an investment incentive certificate,

-Transit transportation,

-Diplomatic exemption, are deducted from the Value Added Tax (output VAT) to be calculated on the transactions of the taxpayer which are subject to VAT. In the absence of transactions subject to VAT, or if the output VAT is less than the input VAT, then the input

VAT which cannot be deducted is refunded to those who perform such transactions, on the basis of principles to be determined by the Ministry of Finance.

### **SPECIAL CONSUMPTION TAX (SCT)**

Special Consumption Tax (SCT) has been introduced to Turkish tax system, effective from August 1st, 2002. SCT is settled to establish a single consumption tax structure in Turkey (apart from the value added tax), and abolished 16 different consumption taxes and fund levies, which were in effect.

SCT is levied on the delivery or on the initial acquisition or on the importation of certain goods specified in 4 different kinds of lists. The contents of the lists, taxable event and the applicable SCT rates/amounts are shown in the table below:

*List 1: Natural gas, petroleum products, LPG, petrol derivatives, base oil, solvents and derivatives of solvents and similar kinds of goods etc.*

Delivery of the goods by their importers and manufacturers (including refineries) or auction sale of the goods before SCT levied on

A fixed amount per measurement unit depending on the kind of goods

*List 2: Vehicles;*

Subject to registration: First acquisition

A proportional tax variable between 0.5% and 84%

Not subject to registration: Importation or delivery of the goods by the manufacturers or auction sale of the goods before SCT levied on

Cars 3% to 84%; Buses 1%; Midi/minibuses 4% or 9%; Motorcycles 3%, 8% or 37%; Planes 0.5%; Sailboats 6.7 % or 8%

*List 3: Non-alcoholic beverages, alcoholic drinks, cigarettes, tobacco products etc.*

Importation or delivery of the goods by the manufacturers or auction sale of the goods before SCT levied on

A proportional tax or minimum fixed amount per measurement unit depending on the kind of goods.

- Between 25% to 63% for beverages

- 30% or 63% for tobacco products

*List 4: Luxury goods (personal care products, cosmetics, precious stones, durable goods, electrical house equipments, electronic goods etc.)*

Importation or delivery of the goods by the manufacturers or auction sale of the goods before SCT levied on 6.7% or 20%

Some deliveries, importations and initial acquisitions qualify SCT exemption in certain conditions specified in the SCT legislation (i.e. export deliveries; import, first acquisition and deliveries of goods specified under List I, II and III to international organizations and their personnel that have been granted tax exemption based on international agreements and to diplomatic representatives and consulates of foreign countries in Turkey as well as to their members who possess diplomatic rights on condition of reciprocity; delivery of goods specified under List I and IV to certain public institutions; first acquisition of vehicles by disables; first acquisition of planes by Turkish Aeronautical Association etc.)

## **BANKING AND INSURANCE TRANSACTION TAX (BITT)**

BITT is imposed on the gross income of banking and insurance companies with respect to all types of transactions, except the transactions conducted according to the Financial Leasing Code. In order for the BITT to occur, a transaction has to be conducted; a collection related to the transaction has to be made in cash or on account and the amount collected has to be on advantage of the related party. The taxpayers of BITT are banking and insurance companies and bankers. Also the tax is usually reflected to customers for their transactions. General BITT rate is 5%. The tax rates for specific transactions are stated below: BITT is declared and paid monthly. A return has to be filed and the tax has to be paid by the 15th day of the month that follows the month of the transactions.

## **STAMP TAX**

Stamp tax is applied to a wide range of legal documents such as contracts, agreements, letters of undertaking, deeds of settlement, letters of cancellation, letters of guarantee, financial statements, returns and remunerations (payroll).

The taxpayers of the stamp tax are those who sign the documents. The companies who sign the contract are joint liable for the payment of the stamp tax. The taxes for the documents issued abroad or in the foreign embassies and consulates in Turkey are paid by those who present these documents to the official bodies in Turkey, who transfer or endorse them or who benefit from their provisions.

Contracts signed outside Turkey may not be subject to stamp tax. However, such a contract will still be within the scope of stamp tax practice if one of the following conditions is fulfilled.

- Presenting to Turkish authorities (official departments),
- Providing with a formality or endorsement,



- Using (benefiting) from the provisions of the contract in any way in Turkey.

The base of the stamp tax is the amount stated on the document. In case the amount is not clearly stated but if it is possible to calculate the value of the contract from the variables stated in the contract, calculated amount will be taken into consideration.

Stamp tax can either be lump sum or proportional. In other words, there is either a fixed amount of tax to be paid or the amount is computed as a percentage of the value of the transaction evidenced by the document.

The tax rates or amounts differ depending upon the nature of the document or the transaction. Amounts set in foreign currencies are converted to Turkish Lira over f/x selling rates determined by Turkish Central Bank.

The general stamp tax rate applicable to the agreements is 0.825 %. On the other hand, the tax rate is 0.165 % for rental agreements and letters of cancellation; 0.825 % for letters of guarantee and deeds of settlement and 0.66% for remunerations (payroll).

If another document is referred on the document whose nature is to be determined, the tax is levied according to the nature with regard to the provisions of the referred document. In this case, the amount to be taken as a basis as determined money, will of course include the money and amounts indicated on the attachments or on the documents referred.

Each original copy of the documents is subject to separate stamp tax.

Meanwhile, in the calculation of stamp tax over each document there is a cap\ceiling to be considered which is TL 1.251.383,40 for the year 2011.

Stamp tax can be paid in three ways; by putting printed stamp, in respond of receipt and by withholding from the gains.

Stamp tax returns shall be submitted till 23th day of the following month and paid till 26th day of the following month of the month in which the document is signed / issued.

## **TAX ON CUSTOMS**

Goods imported from abroad are the subject of the tax. Taxable events are free circulation of goods, registration of customs declaration, and temporary importation in case of partial exemption. Taxpayer is principally person who declares to the customs office.

Customs duties are assessed on written declaration by the taxpayer and paid within 10 days dating from communication.

### **INHERITANCE AND GIFT TAX**

For 2011, beneficiaries and gift recipients are subject to inheritance and gift tax at rates ranging from 1% to 30%. The tax is paid over three years in two equal installments, in May and November. For year 2011, TL 118,438 for inheritance gains and TL 2,730 for gift gains are exempt from tax.

Turkish citizens are subject to inheritance and gift tax on worldwide assets received. Resident foreigners are subject to inheritance and gift tax on worldwide assets received from Turkish citizens and on assets located in Turkey received from resident foreigners or nonresidents. Nonresident foreigners are subject to inheritance and gift tax on assets located in Turkey only.

### **MOTOR VEHICLE TAX**

The persons (both individuals and corporate) for whose names motor vehicles are registered are entitled to pay motor vehicle tax for each year in two equal installments on January and July. The amount of tax is determined separately for each group of vehicle by taking into consideration the age and engine capacity of the vehicle. The motor vehicle taxes paid for the passenger cars are not deductible for corporate and income tax purposes.

### **REAL ESTATE TAX**

The buildings and lands in Turkey are subject to real estate tax. The tax taxpayer is the owner of the building/land, the owner of any usufruct over the building/land, or if neither of these exist, any person that uses the building/land as its owner. There is a partial exemption of 25 % of the tax value (not to be less than TL 2,500) of buildings or apartments used as residences. This partial exemption applies for five years from the year following the year when construction was completed.

The tax base for the building/land tax is the tax value of the building/land. The tax value is the value recorded at the Land Registry. The rate of building tax is generally 0.2% although the rate falls to 0.1% for buildings used as residences. The rate of land tax is 0.1%

and parceled land tax is 0.3%. These rates are increased by 100 % within the frontiers of metropolitan municipality and contiguous regions as defined by law.

A declaration is submitted to the municipality where the building or land is located if there is a modification which might lead to a change in tax value. Taxes are paid annually in two equal installments, the first at any time during the period from March through May and the second in November.

### **RESOURCE UTILIZATION SUPPORT FUND (RUSF)**

This fund is levied on specific transactions such as loans obtained from abroad whose term is less than one year and importation of goods on credit basis. The applicable RUSF rate is 3% on loan amount granted or CIF (Cost- Insurance-Freight) value of the goods. RUSF is not applied on transactions which are made in scope of an investment incentive certificate

### **SPECIAL COMMUNICATION TAX**

Telecommunication services are generally subject to special communication tax. The taxpayers of this tax are operators who render telecommunication services. This tax is usually borne by customers. Special communication tax rates are as follows:

- Mobile telecommunication services 25%
- Services related with the transmission of radio and television broadcasts 15%
- Services related to internet via cable, wireless and mobile 5%
- Other telecommunication services 15%

Special communication tax is reported and paid monthly. Each month's return is submitted to the tax office and the tax is paid by the 15th of the following month.

This tax is not included in the VAT base, besides considered as non-deductible for income and corporate tax purposes.