

# SARIİBRAHİMOĞLU LAW OFFICE

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## USEFUL INFORMATION FOR MANAGERS OF FOREIGN CAPITAL COMPANIES IN THE TURKISH TAX SYSTEM

To begin with, without knowing and reading all the rules related to Turkish Tax Law, it is possible to make a misunderstanding about the event confronted. For this reason, it is necessary to read all the provisions carefully.

It should be remembered that aims of tax legislations is to receive money.

The problems that companies frequently confront and some questions and answers that concern companies in particular are explained below;

### 1. HOW SHOULD TAX LAW BE INTERPRETED?

The interpretation clause in tax law is in Article 3 of the Turkish Tax Procedure Law; The taxable event and the real nature of the transactions related to this event can be proved with all kinds of evidence except oath.

The justification of the article on a subject under investigation should also be considered.

If there is nothing concrete in the justification, the discussions held in the parliamentary minutes at that time may also clarify the issue. Going back even further, it is necessary to know the discussions of the Justice Commission.

### 2. DO FOREIGN LEGAL PERSONS BE TREATED DIFFERENTLY FROM TURKISH NATIONAL LEGAL PERSONS IN TERMS OF TAXATION?

There are two different principles in Turkey:

- The Principle of the Personality
- The Principle of the Territoriality of the Laws

What is meant by the territoriality of the laws, is the application of the laws to the transactions within the borders of the country.

What is meant by the principle of the personality is that the person is subject to the law of his country wherever he is.

**The principle of personality is applied in terms of income tax.** Regardless of where in the world an income taxpayer earns income, he/she pays income tax in Turkey on the income he/she earns.

In addition, the concepts of “full-fledged taxpayer” and “limited taxpayer” should be explained;

Persons who have residence in Turkey or residing in Turkey for more than 6 months in 1 calendar year are considered **full-fledged taxpayers.**

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They are obliged to pay tax in Turkey on all income they have earned inside and outside of Turkey.

In this case, the issue that is confused is the principle of “calendar year”. The calculation of the 6-month period is made regarding that “calendar year”.

*For example, if a person is in Turkey in the last 3 months of the year 2022 and the first 5 months of the year 2023, the person is not considered a full-fledged taxpayer.*

**Limited taxpayers**, on the other hand, are people who are not settled in Turkey and pay tax only on the income they have earned in Turkey which is listed in Article 7 of the Income Tax Law.

Whether a real person is a full-fledged taxpayer or a limited taxpayer is determined on the basis of articles 3, 4, 5, 6 and 7 of the Income Tax Law.

In corporations, legal persons whose law and business center are in Turkey are full-fledged taxpayers, while institutions whose law and/or business center are not in Turkey are limited taxpayers.

Taxation of a foreign institution in Turkey is subject to Corporate Income Tax.

### **3. HOW IS VAT TAXED WHEN THE MANUFACTURING AND THE EXPORTING COMPANIES ARE THE SAME?**

In case the manufacturer exports the goods he/she produces, it is necessary to think in two ways.

The exporter requests back the VAT included in the exported goods from the exporter within the scope of export exemption.

There is only one method for this; the export of the goods is authenticated by the customs declaration form.

Since the exporter does not pay VAT with the products which was bought from the manufacturer, that is, it was already purchased without paying VAT, cannot be returned as it was not paid. The refund will be made to the manufacturer.

### **4. HOW IS INCOME TAX CALCULATED?**

In terms of tax; the Income Tax Law taxes the income of real persons, the Corporate Tax Law taxes the income of legal persons, the Value Added Tax taxes the delivery of goods and services, the inheritance tax taxes the values passed on by inheritance or donation, etc.

The first important matter is the determination of income. **What is income?**

Seven income elements are counted in the Income Tax Law, which is also valid for legal entities. These seven income elements are also valid for corporate tax.

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Income items are defined according to the terms of the Income Tax Law, with the exception of commercial income.

The definition of commercial income is avoided. The reason for this is that the legislation regulating commercial activities is very scattered, and it is possible that something may be overlooked; therefore, it is sufficient to say "income derived from commercial and industrial activities".

Article 1 of the VAT Law clarifies this definition to a certain extent.

"The continuity, scope, and nature of commercial, industrial, agricultural, and self-employment activities shall be determined in accordance with the provisions of the Income Tax Law; in cases where there is no clarity in the Income Tax Law, in accordance with the provisions of the Turkish Commercial Code and other relevant legislation."

An income that is not included in the income items listed in Article 7 of the Income Tax Law, which is a mixture of labor and capital, is a commercial activity if the income is capital-intensive, or it is a self-employment activity if the income is labor-intensive.

## **5. HOW ARE THE WAGES OF THE PERSONNEL WORKING IN THE LIAISON OFFICES TAXED?**

According to the provision in Article 23/14 of the Income Tax Law:

***“ARTICLE 23) The wages listed below are exempt from the Income Tax;***

*14 a) Wages paid in foreign currency to the service personnel employed by limited taxpayer employers whose legal and business headquarters are not located in Turkey, over the earnings of the employer outside Turkey;*

*b) Wages paid in foreign currency to the service personnel employed by limited taxpayer employers whose legal and business headquarters are not located in Turkey exclusively within the scope of the operating permit of the centre in the regional management centres established based on the permission obtained from the Ministry of Economy, over the earnings gained outside Turkey;”*

In accordance with the Income Tax General Communiqué Serial No. 147, two basic conditions are required for liaison offices;

- The employer of the person working in the liaison office should not have a commercial activity in Turkey
- Payment of wages to liaison office staff from their earnings in the foreign country and not from their earnings in Turkey.

## **6. HOW ARE EXPENSES DEDUCTIBLE FROM TAX?**

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Article 40 of the Income Tax Law is quite clear regarding this issue, except that the first paragraph is an omnibus paragraph:

*“General expenses incurred for the acquisition and maintenance of commercial income”*

The term "general expense" is not explicit. **The real nature of the transaction is the basis for taxation.** If it is not related to commercial activity, it cannot be written off as an expense.

- a. Is the declared address important? Example: The business address appears to be 14/5 in the building, but work is also carried out in flats 1 and 4. Can the expenses incurred in these apartments also be shown as expenses?**

The question of what a workplace is must first be answered; this issue is regulated in Article 156 of the Tax Procedure Law. In summary, the workplace is the place where commercial, professional, and agricultural activities are carried out. In accordance with Article 168 of the Tax Procedure Law, the workplace must be notified within 1 month.

There is no provision in the Income Tax Law that requires a self-employed person to have a single workplace.

## **7. IS THERE A TAX DIFFERENCE BETWEEN EMPLOYMENT OF FOREIGNERS AND CITIZENS?**

The wage earner employed by the foreigner pays taxes in the same way that Turkish employees pay taxes in Turkey. The employer is responsible for the tax.

There is only one difference. If one is insured in his/her country of residence, he/she does not pay insurance premiums in Turkey. The difference in tax terms is that if the foreigner is a real person who is a limited taxpayer, the minimum living allowance is not applied.

## **8. WHAT ARE TAX REDUCTIONS FOR FOREIGNERS?**

They are not different from the citizens.

## **9. WHAT ARE THE TAX LIABILITIES SUBJECT TO THE FOREIGN LEGAL ENTITY IN GENERAL?**

If a foreign legal entity is engaged in an activity that is within the scope of corporate tax in Turkey, it will be subject to corporate tax on a limited liability basis.

## **10. HOW DOES THE TAX PROCESS WORK IN MOVABLE AND IMMOVABLE PURCHASING?**

- a. In terms of Movables:**

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When it comes to movable property, the first thing that comes to mind is the vehicle, and the most important issue in terms of vehicles is to register them to the traffic.

If a first-hand vehicle is purchased, SCT and MTV are paid. If a second-hand vehicle is purchased, there is no SCT.

VAT is paid in the purchase of machinery and equipment.

## **b. In terms of Immovables:**

If there is a sale of real estate regarding the inventory of an economic enterprise, an invoice is issued for this sale and VAT is calculated. VAT is encountered in terms of tax.

If a real estate that is not included in the economic enterprise belongs to a real person and this real estate is subject to sale, the Income Tax Law, duplicate article 80/6 is applied.

Accordingly, **regardless of the method of acquisition, Value Increase Gain is applied in terms of gains arising from disposal within 5 years from the acquisition date.**

This provision also applies to limited taxpayers. However, the declaration of limited taxpayers is an individual declaration, not an income tax declaration.

Duplicate article 81 of the Income Tax Law should be examined for the calculation of the increase in value. In the acquisition of the real estate, the economic value including the taxes paid is deducted from the sales price and the difference is the value increase price.

According to the reiterated Article 81 of the Income Tax Law, the exemption amount for capital gains is 25,000 for the year 2022.

Another important issue is the valuation provision to protect the sale transaction from inflation. Pursuant to the last sentence of the duplicated article 81 of the Income Tax Law, the acquisition price is increased in proportion to the increase in the total goods price index, excluding the month of disposal. With this increase, the increased acquisition price is accepted as the purchase price and deducted from the sale price.

For example;

A, bought a real estate for 100 TL and paid 10 TL for taxes and other expenses.

The price index 1 month before the date of purchase and sale of the real estate by A is 20 TL.

So, it reached 120 TL. There was also a purchase cost of 10 TL.

In other words, the immovable property bought by A was cost 130 in total.

A sold this real estate for 250 TL.

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The figure found by deducting 130 TL from 250 TL is the increase in value.

From this, the exemption amount of 25,000 TL in 2022 is deducted.

Income tax is calculated based on the remaining amount.

It should be noted that the value increase gain is valid in the sale.

## **11. WHAT ARE THE VAT TAXATION RATES FOR IMPORTS AND EXPORTS?**

There is no difference. The same VAT rate applies on imports as on the domestic market. There is no VAT on exports, there is VAT on manufacturing.

## **12. WHAT IS THE TAX SITUATION IN TRANSIT PASS?**

There is no VAT on the transit pass. Because VAT is specific to transactions made in Turkey.

Income from transit trade is included in the Income or Corporate tax of the year it is brought to Turkey. If the transit trade is also carried out in the free zone, it is not subject to VAT. Exports to the free zone benefit from the export exemption, just like exports abroad, VAT is not charged.

If a product is sold from the manufacturer to the exporter, there is no VAT tax from the seller's side in that transaction. When the exporter exports that good, it is already covered by the export exemption. It is important whether the buyer is subject to VAT.

Within the scope of the inward processing permit, the products are already being imported customs-free. It has a manufacturing certificate, and it is being delivered to the exporter within the scope. Due to the nature of the system, tax-free transactions are made. When the product is exported, the manufacturer receives a refund of the taxes paid.

Free zones are within the scope of foreign countries in terms of transaction taxes and value added tax, but the earnings obtained from the free zone are exempt from tax within the framework specified in the law.

### **a. INWARD PROCESSING REGIME:**

It is an export incentive system that provides customs exemption for the raw materials or inputs that are necessary to produce export products by exporting companies but are imported and therefore subject to import customs duty.

Within the scope of the Inward Processing Authorization Certificate, a product is imported from abroad without customs duty and VAT, and contract manufacturing is carried out in Turkey with the goods received that way. When the manufactured goods made by the contract manufacturer are delivered to the exporter, the inward processing permit is closed. There is no VAT on this

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transaction when the goods are exported. However, the income from this transaction is subject to income or corporate tax.

## **13. IS THE WITHHOLDING TAX FOR WORKPLACE RENTS ALSO COLLECTED IN THE FREE ZONE?**

It is within the borders of the Turkish Republic and is evaluated in terms of transaction tax. There is a general notification of the institutions related to free zones, there is only one difference, **free zone exceptions do not cover withholding.**

## **14. HOW IS THE TAXATION OF FOREIGNERS TEMPORARILY ASSIGNED IN TURKEY AND IMPLEMENTATION OF SOCIAL SECURITY IS DONE?**

According to the Income Tax Law, persons who come to Turkey temporarily for a job are not deemed to have settled in Turkey.

It refers those who work for 180 days on a temporary basis. However, even if it exceeds 180 days, it is not fully counted.

### **a. How is it taxed?**

It is taxed just as a person in Turkey is taxed. And tax is taxed according to the tariff in article 103 of the income tax.

### **b. What is the status of this person in his/her home country?**

If this person is subject to the principle of full liability in terms of his/her own country, which is the case; that country has the right to tax all of its income both in its own country and in foreign countries.

If there is no exemption regulation or a provision for avoiding double taxation, that country may also have the right to taxation over the income obtained in Turkey and the exceptions have to be considered.

If he/she is insured in his/her own country, he/she is not subjected to insurance in Turkey.

## **15. FOR EXAMPLE, IN A SCENARIO WHERE THE 20% SHAREHOLDER IN THE CAPITAL COMPANY WILL RECEIVE A DIVIDEND AT THE RATE OF HIS/HER SHARE FROM THE PROFIT OF THE COMPANY AT THE END OF THE YEAR IF THE COMPANY RECEIVED THE DIVIDEND WITHIN THE FRAMEWORK OF CORPORATE TAX BEFORE THE DIVIDEND IS RECEIVED**

### **a. Is this subject to income tax?**

Yes, it is taxable in Turkey according to income tax law.

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- b. For example, if the company has a profit of 100 units, these 100 units of earnings are taxed within the framework of corporate tax. Secondly, after that taxation process, 100 units remained 80 units, these 80 units were distributed as dividends, and the income tax is being paid on top of that. Will there be double taxation here?**

There will be no double taxation here. In the case of double taxation, more than one tax of the same type is levied on a transaction subject to a tax, whereas here there is more than one type of tax.

## **16. REGARDING THE TAX DIMENSION OF THE SERVICE INVOICES FOR THE GROUP COMING FROM ABROAD, WHAT IS THE TRANSFER PRICING? BECAUSE THIS IS APPLIED TOO MUCH, ESPECIALLY TO CHINESE COMPANIES.**

The hidden capital corporate tax law is regulated in Article 12. The rationale of this regulation is as follows:

Article 12 on Monetary Movements; The portion of the debts used by the institutions directly or indirectly by obtaining them from their partners or persons related to the partners, in excess of three times the equity capital of the institution at any time during the accounting period, is covered for the relevant accounting period is considered as capital.

The interest paid for the borrowed debt is used as hidden capital, and cannot be written off as expense. If the foreign resource is received from partners or related persons, there are conditions required in the article, and if it does not meet those conditions, the interest cannot be written off as expense.