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A new tax security measure!

According to Turkish Constitution, every individual is liable to pay taxes according to their financial strength and tax responsiblty is forcibly imposed on income earners by using the public power. Therefore, the taxpayer’s warranty against public power is the principle of “rule of law” and “legitimacy in tax”.

In modern tax systems, the declaration of the income obtained by the taxpayer is essential. So at this stage, will there be a security gap in tax? Yes and against this, "tax security elements" have been placed within the tax laws.

One of the duties of companies to their sahreholders and stakeholders other than shareholders is to protect the company's share value against market volatility. Therefore, companies are allowed to buy back shares through the provision of Article 379 in Turkish Commercial Code (the TCC). According to the TCC, a company has the "right to buy back" its shares representing 10% of its capital. A company is not allowed to buy back more than 10% shares, and in case of purchase, it is required to sell off more than 10% or decrease the capital at this rate. Finally, the purpose of share buyback is not to make a gain for the corporations or to distribute dividends to the sharholders.

Recently, it’s seen that share buybacks have been used frequently in Turkey. The increase in share buyback transactions due to periods of economic crisis and Covid-19 outbreak required clarification of its taxation.

The buyback opportunity provided by the TCC has highlighted the repurchase of shares or stakes from real person shareholders holding them for over two years due to their tax advantages. In the face of this situation, “a security element for taxation in share buyback” has been included in Turkish tax legislation.

With a clause added to the Article 94 of the Income Tax Law ("the ITL") through the Law no. 7256, the buybacks of fully taxpayer (resident taxpayers) capital companies are considered as distributed dividends under certain conditions and a 15% withholding tax is stipulated on the amounts calculated in line with certain principles. The reason for the 15% tax to be applied in share buyback is that the value increase gain arising from the disposal of stocks held for more than two years is not taxed and preventing it since this transaction is considered as "tax-free dividend distribution".

In this amendment, 15% tax will be withheld to be deducted from whose tax? Nobody. Therefore, this new "tax security element" in share buybacks is different from other tax security facilities implemented.

The 15% tax to be withheld by the corporations after the amendment will lead a decrease in the assets of capital companies. Especially considering the floating stocks rates of publicly traded companies, those who will suffer most from this regulation will be the stock investors and the savings owner who use stocks for their private pension plans by investing in stocks mutual funds. Therefore, the investors hope that the President may use his authority to determine the withholding rate as 0% for the listed companies in BIST.

On the other hand, when the regulation is handled within the framework of the principle of "protection of property right in tax", it can be claimed that full taxpayers who have to pay the 15% tax have suffered losses and / or the regulation is unconstitutional".

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