

The future of regional management centers considering recent changes and Turkey's approach

Introduction

Foreign direct investments play an important role in the development plans of developing countries. One of the policies frequently used by these countries to increase these investments is the development of incentive policies for foreign investments.

Collaterally, regulations regarding the Regional Management Centers in Turkey have entered into force in 2012 and multinational foreign companies have started to operate as “Regional Management Centers” in Turkey as to gain benefit of opportunities.

Regional Management Centers were regulated in the form of “Liaison Offices” and were able to operate without tax burden with the adjustments made over time. However, corporation tax exemption was abolished with the law numbered 7103 that entered into force in 2018.

Legislation

Regional Management Centers in Turkey started to be implemented with Article 3/h of law No. 4875 Foreign Direct Investment Law and with the amendments made in 2012 to the Article 6 of Regulation for Implementation of Foreign Direct Investment Law. With the Law No. 6728 on the Law Regarding Amendments on Certain Laws Aimed at Improving the Investment Environment, tax exemption regulations for the Regional Management Centers were introduced and, in a sense, the incentive was solidified and reinforced.

The activities of the Regional Management Centers to be established by foreign institutions are limited to the aforementioned regulation. These activities are to provide coordination and management services such as; investment and management strategies, planning, promotion, sales, after-sales services, brand management, financial management, technical support, R&D, external procurement, testing of newly developed products, laboratory services, research and analysis, training of employees.

Tax regulations regarding regional management centers

Taxation regulations regarding Regional Management Centers have been made together with the “Law Regarding Amendments on Certain Laws Aimed at Improving the Investment Environment” No. 6728, published in the Official Gazette dated August 9, 2016.

○ Corporation tax exemption

In accordance with the clause (ö) added to the paragraph 1 of the 4th Article of the Corporation Tax Law No. 5520, Regional Management Centers are exempted from the corporation tax if they meet the following criteria:

- They must be established based on the permission obtained from the Ministry of Economy,
- All costs of legal and business center must be met by institutions not in Turkey (with the foreign exchange they bring from abroad) and

- Such expenses should not be included in the accounts of any institution which is a full or limited taxpayer in Turkey and should not be separated from its profit.
- **Why was the corporation tax exemption abolished?**

The exemption mentioned in Article 74 of the Law No. 7103 on the Law Requiring Amendments to Tax Laws, Certain Laws and Statutory Decrees has been abolished. The reason to abolish the exemption in the Tax Draft Law No. 533 and Law Requiring Amendments to Tax Laws, Certain Laws and Statutory Decrees (1/914) and the Plan and Budget Commission Report are as follows.

In accordance with the The Organisation for Economic Co-operation and Development "OECD" and "EU" standards, to ensure compliance with the international taxation principles, the framework is accepted as the 76th article by removing the tax exemption granted to the regional management centers established based on the permission obtained from the Ministry of Economy.

According to the protocols of the Plan Budget Committee, the statement issued by the Minister of Finance of the time regarding the removal the exception and stated that they removed the exemption related to the regional management centers liaison offices, and in the past, two years ago, corporation tax exemptions were introduced to the Regional Management Centers and they wanted to remove the exemption.

The article removing the corporation tax exemption related to the Regional Management Centers came into force on 1/1/2019. However, as of 1/1/2019, the date of implementation was determined as 1/1/2022 for the Regional Management Centers already established.

- **Income tax exemption**

Article 23 of the Income Tax Law regulates wages exempted from income tax. Paragraph (14) / a of the said article is as follows:

"Legal or business center in Turkey without liability to narrow the wages paid to employees of employers in rates over the next service connoisseur earnings obtained outside Turkey which the employer is exempt from income tax."

In addition to the above-mentioned law article, a special exemption clause regarding the Regional Management Centers has been added to the subparagraph (b) of the said article.

As detailed in the Income Tax General Communiqué numbered 293, published in the Official Gazette dated 2.10.2016, after the amendment made in the 23rd Article (14) / b numbered article of the Income Tax Law, the Regional Management Centers must meet the following requirements to be eligible to benefit from the income tax exemption:

- Institutions that pay wages in the capacity of an employer should not have a legal or business center in Turkey,
- The person working in a limited taxpayer institution should be an employee (paid worker) and the payment should be qualified as wage,
- The employee that the limited taxpayer institution pays wage to should be employed within the scope of the operating permit in the regional management centers established based on the permission obtained from the Ministry of Economy,

- The wage to employees that the limited taxpayer institution will provide should be granted via its foreign earnings,
- Payments of wages should be made in foreign currency.

Conclusion and our evaluations

Although the exemption in the Corporation Tax Law was eliminated with the law numbered 7103 that entered into force in 2018, no regulation was made regarding the exception in the Income Tax Law.

With the amendment in the Corporation Tax Law, application of the income tax exemption and whether the income tax exemption of a liaison office that is a taxpayer of corporation tax can continue raises some concerns.

However, the fact that the income tax exemption related to the Regional Management Centers has not been abolished can only be evaluated that it is necessary and sufficient to establish a liability in terms of corporation tax, but the income tax exception should not be affected.

Therefore, after the current changes, it is possible for the wages paid to the people working in the Regional Management Center to benefit from the income tax exemption if the exemption conditions are preserved.

We understand that the Regional Management Centers established as of 1/1/2019 will become corporation taxpayers as of 2022. Considering that the liaison office activities are carried out within the framework of the liaison office license obtained, it is uncertain how the application will be implemented after 2022, if the liaison office license period continues.

It is expected that the tax authorities will make arrangements on this issue and create a new structure for the Regional Management Centers.

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