

Evaluation of the negative difference arising in case of liquidation of the participated entity

As it is known, profit share (dividend), obtained in return for participation share in any other entity, is called as “participation income”.

Participation income, obtained by the entities due to participating in capital of another entity, is exempted from corporate tax according to subparagraph (a) of paragraph (1) of article 5 of Corporate Tax Law. Duplication in taxation is intended to be prevented by participation income exemption.

Participation income, mentioned under article 5/1-a of Corporate Tax Law, is indeed the profit which is return of related shares due to participating in another entity. Shareholders also benefit from arising profit. Such income is exempted from corporate tax. In contrary, the entity holding the participation share is required to incur such loss when participated entity makes a loss.

In case entities participate in capital of another entity and such participated entity is liquidated, it has been an issue discussed for a long time whether arising negative difference shall be recognized as loss and subject to deduction in terms of profit of the company or not and it is also an issue of which Turkish Revenue Administration and the Judicial Bodies cannot come to an agreement. Turkish Revenue Administration had opinions in its initial advance rulings on the case that amounts belonging to affiliate could be recognized as loss while it has changed its opinion in its recent advance rulings stating that such amounts cannot be recognized as loss. The aforementioned opinion of TRA has brought to courts and it is observed that courts also have favourable and unfavourable decisions for the taxpayers on this case.

While judicial bodies adjudge in multiple tax court decisions and in decision of Council of state dated 16.10.2001 that liquidation loss can be taken into account as expense, it delivered a judgement on 19.02.2019 that it cannot be taken into account as expense and according to its judgement dated 16.12.2019, it can be taken into account as expense.

First of all, according to Turkish Revenue Administration, such loss cannot be taken into account as expense since there is no clear provision regarding the consideration of such loss as expense for the determination of profit of the company. However, on the other hand, there is no provision regarding not taking into account such loss as expense.

In case of a contrary case of exempted income included under article 5/1-a of Corporate Tax Law, the entity holding participation share makes a provision corresponding to such loss due to loss of participated company or incurs such loss anyways. In this case, although it seems like there is a situation of participating in loss, a participated company does not legally exist and value of current shares are set to zero. In our view, shares, whose value is set to zero due to liquidation, are required to be recognized as expense since the loss arising when the shares are sold for an amount less than their book value are taken into account as expense.

In conclusion, it shall be an appropriate application for the case to be solved by the Administration in this scope, since arising loss lacks a clear legal regulation currently and taxpayers remain suspicious at this point.

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