058176/EU XXVI. GP
Eingelangt am 15/03/19

Council of the
European Union

Brussels, 15 March 2019
(OR. en)

7561/19

FISC 198

OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Code of Conduct Group (Business Taxation)
Subject:	Turkey's Regional Headquarters regime (TR004) – Final description and assessment

ROLLBACK REVIEW PROCESS (JANUARY 2019)

Art. 74 of the "Law on Amendments in Tax Laws and some Other Laws and Decree Laws" N° 7103 (published in the Official Gazette dated 27 March 2018 and numbered 30373) has repealed Paragraph 1-ö of Art. 4 and Paragraph 9 of Art. 17 of Law 5520 dated 13 June 2006 (Corporate Income Tax Law), which established the preferential tax treatment for Regional Headquarters. The amendments introduced by Law 7103 entered into force on 1 January 2019. On this basis, the regime can be deemed abolished.

Art. 93 of the Law N° 7103 sets forth that a grandfathering period is granted to companies that entered into the Regional Headquarter regime before 1 January 2019. The duration of the grandfathering period is in line with the practice of the Code of Conduct Group, being the period expiring on 31 December 2021.

The Code of Conduct Group meeting of 30 January 2019 approved the rollback of the regime. This conclusion was endorsed by the ECOFIN Council on 12 March 2019.

Annex 1: Assessment of the old TR004 regime in 2017 (standstill review)

Annex 2: informal English translation of the final legislation

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ANNEX 1

Assessment of the old TR004 regime in 2017 (standstill)

a. Description

With effect from 9 August 2016, regional headquarters founded by non-residents in Turkey with the permission from the Ministry of Economy are exempt from corporate income tax, subject to two conditions:

- all expenses of the regional headquarters must be borne by foreign headquarters, and

- expenses borne by foreign headquarters must not be attributed to any company in Turkey, whether resident or non-resident.

In addition, the salaries paid in foreign exchange to the personnel of the regional headquarters are also exempt from income tax as of 1 September 2016.

b. Preferential features/ Benefits available under the Regional headquarters regime

Standard rate of the corporate income tax is 20%. Regional headquarters are exempt from corporate income tax.

Therefore, a preferential tax treatment is granted to regional headquarters companies.

c. Possible concerns/ What is the problem under the Code?

A regime limited to foreign tax payers and/or to operations outside the territory of the jurisdiction (ring fenced regime) does not meet criteria 1 & 2 of the Code of Conduct which prohibit this type of ring fencing. The Regional headquarters regime is targeted to foreign enterprises or activities with foreign entities/markets since tax advantages are granted only to foreign enterprises or in respect of transactions carried out with non-residents.

Another important Code criterion used to assess the harmfulness of a regime is its transparency (criterion 5). A measure is considered as not transparent when it is not laid down in law but granted on a discretionary basis. The Regional headquarters regimes does not seem transparent to the extent the conditions for granting the concessions are not clear and at the discretion of the Government (the Ministry of Economy).

Source of information

IBFD

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d. Assessment by FHTP:

Out of the scope

Assessment by COCG:

	1a	**1b**	**2a**	**2b**	**3**	**4**	**5**
Turkey – Regional headquarters (TR004)	V	V	V	V	V	X	X

V = harmful

X = not harmful

Explanation

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The Regional headquarters are exempted from corporate tax. The general tax rate in Turkey is 20%. Therefore, the measure provides for a lower level of taxation and is potentially harmful.

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1 contains two elements. The first element is whether the measure is exclusively available to non-residents or transactions with non-residents (criterion 1a). The second element is whether it is only or mainly used by non-residents or for transactions with non-residents (criterion 1b).

1a) Criterion 1a concerns the *de jure* application of the measure.

1b) Criterion 1b is used to complement the assessment under criterion 1a which only looks at the literal interpretation of the measure. It takes account of the de facto effect of the measure. Where the majority of taxpayers (or counterparties to transactions) benefiting from the measure are in fact non-residents the measure will fall foul of criterion 1b.

The beneficiaries of the measure may be non-resident. Only the operations with non-residents are exempted from corporate tax.

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Criterion 2 – Ring-fencing:

"*whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base*"

As regards criterion 2 the division between criteria 2a and 2b is done in the same way as in the case of criterion 1 (i.e. *de jure* interpretation and *de facto* analysis). In general, a measure is caught by criterion 2 if the advantages are ring-fenced from the domestic market so that they do not affect the national tax base. In most cases, the evaluation against criterion 2 follows closely that of criterion 1.

2a) What has been written under criterion 1a often applies analogously to criterion 2a.

2b) On the basis of the explanations provided above and the marking under criterion 1b, the evaluation of criterion 2b often follows the same reasoning.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

It is not clear the scope of services that beneficiary must carry out.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The measure does not contradict any internationally embraced principle.

Criterion 5 - Transparency:

"*whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way*"

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

The conditions to be granted an exemption look clear.

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Overall assessment

"*Without prejudice to the respective spheres of competence of the Member States and the Community, this code of conduct, which covers business taxation, concerns those measures which affect, or may affect, in a significant way the location of business activity in the Community*"

In the light of the assessment made under all Code criteria, the regime is considered as overall harmful.

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ANNEX 2

Informal English translation of the final legislation

Law No. 7103:

ARTICLE 74 – Paragraph 1-ö of Article 4 and Paragraph 9 of Article 17 in Corporate Income Tax Law No. 5520 dated 13/6/2006 are repealed.

ARTICLE 93 – (1) f) The provision of the Article No. 74 of this Law repealing Paragraph 1-ö of Article 4 of The Tax Law No. 5520 enters into force on 1/1/2019 (to be implemented beginning from 1/1/2022 for the already established regional headquarters as of 1/1/2019).

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