

# TAXATION OF CHARITIES IN TURKEY

(DRAFT)

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## 1. General information

### 1.1. Definition

In Turkish legal system there is no specific regulation regarding "charities" neither in the Constitution nor in private or tax law; i.e. the concept of "charity" is not regulated and defined under Turkish law. However, regulations on types of charitable institutions are maintained in the Turkish legal order.

In Turkish practice, the most important and common type of charitable institutions is the foundation (*vakif*) which may generally be defined as the transfer of benefits arising from specific private assets to public property by allocating those assets to charitable, social or cultural services<sup>1</sup>. Foundations are regulated in the Turkish Civil Code (TCC)<sup>2</sup> and the Foundations Law (FL)<sup>3</sup>. The legal definition of a foundation is provided under Article 101 of the TCC. Accordingly, a foundation is defined as "a legal personality established by natural persons or legal entities by way of allocating their assets and rights to a specific and permanent purpose".

Associations (*dernek*) can be considered as a second type of charitable institutions. The rules for associations are provided in the Turkish Civil Code and the Associations Act (AA)<sup>4</sup>. Associations are legal entities founded by at least seven individuals who join their knowledge or activities for a specific and common non-economic goal (Art. 56, TCC and Art. 2(a), AA). Associations are not separately dealt with in this report; however, most of the tax information on foundations explained here is also applicable to public benefit associations.

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<sup>1</sup> Vakıflar Kanunu Genel Gerekesi, Vakıflar Kanunu Tasarısı ve Avrupa Birliği Uyum ile Adalet Komisyonu Raporları, No.1/1054, <http://www.tbmm.gov.tr/sirasayi/donem22/yil01/ss1239m.htm>.

<sup>2</sup> Turk Medeni Kanunu, No.4721, Official Gazette of 8.12.2001, No.24607 (Eski Turk Medeni Kanunu, No.743, Official Gazette of 4.4.1926, No.339).

<sup>3</sup> Vakıflar Kanunu, No.5737 (Official Gazette of 27.2.2008, No.26800).

<sup>4</sup> Dernekler Kanunu, No.5253 (Official Gazette of 23.11.2004, No.25649)

The right to establish associations and foundations is granted under Article 33 of the Turkish Constitution<sup>5</sup>. Accordingly, "everyone has the right to form associations, or become a member of an association, or withdraw from membership without prior permission. No one shall be compelled to become or remain a member of an association. (...) The provisions of this article are also applicable to foundations"<sup>6</sup>.

Resident individuals and legal entities enjoy this constitutional right, provided that they comply with the procedure and conditions regulated in the TCC. Non-residents also benefit from the freedom of establishing foundations on legal and actual reciprocity basis (Art. 5, FL)<sup>7</sup>. Foreign individuals who have a right to reside in Turkey are entitled to found an association or be a member of an existing one (Art. 93, TCC).

## **1.2. Purpose**

Generally, there are no restrictions on the purpose of foundations. However, the purpose to which the assets are allocated must be specific, continuous and legal (Art.101, TCC)<sup>8</sup>.

Article 33 of the Turkish Constitution stipulates that the freedom of establishing associations and foundations may only be restricted by law on the grounds of protecting national security and public order, or preventing crime, or protecting public morals and public health. In addition, a general restrictive provision on the purpose of a foundation exists in Article 101 of the TCC. Accordingly, the purpose of a foundation must comply with the characteristics of the Republic as defined in the Constitution, fundamental Constitutional principles, laws, ethics, national unity and national interest, and the formation of a foundation with the aim of supporting a particular race or community is forbidden. In addition, Article 47 of the TCC stipulates, if the purpose of an entity becomes incompatible with law and ethics, the entity is not entitled to retain its legal identity.

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<sup>5</sup> Official Gazette of 9.11.1982, No.17863 (2nd issue). Official English translation published in the website of the Turkish Grand National Assembly , <http://www.tbmm.gov.tr/english/english.htm>

<sup>6</sup> See also Constitutional Court, E.2005/14, K.2008/92, 17.4.2008 (Official Gazette of 28.6.2008, No.26920).

<sup>7</sup> It must be noted that the restrictions applied on foreign nationals for their immovable property acquisitions in Turkey are also applicable to Turkish foundations established by foreign nationals. Companies and economic enterprises established by such foundations are also subject to similar restrictions (Arts.12 and 26, FL).

<sup>8</sup> See Ozsunay, Ergun, *Medeni Hukukumuzda Tuzel Kisiler*, İUHF Yayinlari, Istanbul, 1982, p.386 et.seq; Guneri, Hasan, *Turk Medeni Kanunu Acisindan Vakifta Amac Kavrami ve Amacina Gore Vakif Turleri*, Sevinc Matbaasi, Ankara, 1976, p.28 et.seq.

Foundations are generally founded for non-economic purposes<sup>9</sup>, but to realize these purposes they can engage in economic activities through enterprises. In cases where a foundation seeks for tax-exempt foundation statute, the purpose of a foundation must be one or a combination of health, social aid, education, scientific research and development, culture, environmental protection and/or forestation purposes<sup>10</sup>.

### **1.3. Procedure for the establishment**

For the establishment of a foundation, first and foremost, allocation of assets or rights to a specified purpose is required. Such assets and rights include all types of immovable and movable property, including cash, securities and bonds, and rights that have an economic value<sup>11</sup>. The value of the assets must be sufficient to realize the purpose of the foundation (Art.101, TCC). Under Article 5 of the FL, the General Directorate of Foundations (GDF), a public body affiliated to the Prime Ministry, is authorized to determine yearly the minimum asset value applicable on the establishment of a foundation (Art.5, FL)<sup>12</sup>.

Foundations can be founded by a testament or a charter verified by a notary public and a court (Arts. 101 and 102, TCC). The articles of the charter must clearly state the foundation's title, legal seat, purpose, assets and rights allocated to this purpose, organs and applicable administrative procedures (Art.106, TCC). The charter is then submitted to a court for registration. By registration in the records kept by the competent local court, the foundation obtains its legal personality (Art.102, TCC).

Prior to the court's decision on registration, it is required that all foundations obtain state approval from the GDF which is a public body acting as the major supervision authority for foundations<sup>13</sup>. Upon notification of the competent court, the foundation is also registered in the central register of the GDF. Subsequently, the registration is announced in the Official

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<sup>9</sup> See Oguz, Tufan M., *Turk Hukukunda Vakif Tuzel Kisiliginin Hukuki Esaslari*, Besir Kitabevi, Istanbul, 2007, pp.2-3.

<sup>10</sup> Vakıflara Vergi Muafiyeti Tanınması Hakkında Genel Teblig, Seri No.1, Official Gazette of 3.4.2007, No. 26482.

<sup>11</sup> Uluc, Yusuf, *Vakıflar Hukuku ve Mevzuati*, Vakıflar Genel Mudurlugu Yayinlari, Ankara, 2008, p.556.

<sup>12</sup> For 2012, the minimum amount of endowment at establishment is TRL 50,000 (approx. €20,000). Vakıflar Meclisi Karari, 13.12.2011, No.865/679, <http://www.vgm.gov.tr/duyurudetay.aspx?Id=21>

<sup>13</sup> Vakıflar Yonetmeliği, Art.5 et.seq (Official Gazette of 27.9.2008, No.27010; for the latest amendment, see Official Gazette of 30.11.2011, No.28128).

Gazette (Art.104, TCC).

#### **1.4. Types**

Although there is no specific legislative provision enumerating the types of foundations<sup>14</sup>, considering the major types of special purpose foundations regulated in various laws, it is possible to make a categorization according to their purpose. Such categorizations<sup>15</sup>, albeit not limited to, include family foundations<sup>16</sup>, religious foundations<sup>17</sup>, higher education foundations<sup>18</sup>, foundations for support to personnel and workers<sup>19</sup>, social aid and solidarity foundations<sup>20</sup>, environment protection foundations<sup>21</sup> and other public benefit foundations<sup>22</sup>.

#### **1.5. International relations**

Turkish foundations are entitled to carry out international activities and cooperation, or establish branches and representative offices abroad, and set up governing high level organizations (federation or confederation), or become members of foreign organizations provided that such activities are allowed in their charter (Art. 117, TCC and Art.25, FL)<sup>23</sup> and

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<sup>14</sup> The foundations established prior to the foundation of Turkish Republic are called as "old foundations" and subject to specific legislative and administrative provisions. Such foundations are out of this report's scope. Foundations established after the foundation of the Republic are called "new foundations" established according to the Turkish Civil Code provisions. This report covers the legal situation of new foundations. For old foundations, see Uluc, p.13 et.seq.

<sup>15</sup> See Demir, Ilhan, Yeni Vakiflarin Temel Kitabi, Matsa Basimevi, Ankara, 2005, p.31 et.seq.; Güneri, p. 116 et.seq.

<sup>16</sup> Regulated in Art. 372 of the TCC.

<sup>17</sup> See Ballar, Suat, Yeni Vakiflar Hukuku, 4.Basi, Seckin, Ankara, 2008, s. 632.

<sup>18</sup> Regulated in additional Arts. 2-15 of Law No.2547 (Official Gazette of 6.11.1981, No.17506).

<sup>19</sup> Regulated in Art.110 of the TCC.

<sup>20</sup> Regulated in Art.7 of Law No.3294 (Official Gazette of 14.6.1986, No. 19134).

<sup>21</sup> See Ballar, s. 617.

<sup>22</sup> The number of new Turkish foundations existing as of 20 July 2011 is 4585. Accordingly, there are 3564 multipurpose foundations, 48 foundations for the protection of environment and 973 foundations on social aid and solidarity. <http://www.vgm.gov.tr/db/dosyalar/webicerik195.doc>

<sup>23</sup> Turkish associations are also entitled to benefit from similar international relations (Art.90, TCC and Art.5, AA).

permitted by the Ministry of the Internal Affairs upon the advice of the Ministry of Foreign Affairs<sup>24</sup>.

Foundations can receive in-kind and cash donations and grants from individuals, entities and institutions abroad. Foundations may make in-kind and cash donations to foreign foundations and associations which are established with similar purposes. However, it is mandatory that cash donations or grants are transferred and received through banks. In addition, foundations must notify the GDF of the donations and grants made to or received from abroad (Art.25, FL).

Foreign foundations<sup>25</sup> may operate, establish branches and representative offices, or incorporate high level organizations, or cooperate with existing foundations on reciprocal basis with the permission of the Ministry of the Internal Affairs upon the advice of the Ministry of Foreign Affairs<sup>26</sup>.

## **2. Tax-exempt statute**

### **2.1. Conditions**

In Turkish tax law, there is no specific provision which provides a general tax exemption applicable on charitable institutions. However, tax-exempt statute<sup>27</sup> may be granted to foundations under specific conditions, although this statute does not generate an income tax exemption and has limited impact on other obligations arising from other taxes and duties.

Tax-exempt statute may be granted by the Council of Ministers to foundations which pursues public benefit<sup>28</sup>. According to Article 20 of Law No. 4962<sup>29</sup>, foundations that are established

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<sup>24</sup> Dernekler Yonetmeliği, Art. 21 (Official Gazette of 31.3.2005, No.25772).

<sup>25</sup> Applicable also to foreign associations conducting activities in Turkey (Art.91 TCC and Art.5, AA).

<sup>26</sup> Dernekler Yonetmeliği, Art. 22 (Official Gazette of 31.3.2005, No.25772). See Basak, Levent, "Yabancı Vakıfların Türkiye'deki Faaliyetleri, Bu Çerçevede Yabancı Vakıflar Türkiye'de Hangi Örgütlenme Modellerini Kullanabilirler?", Vergi Sorunları Dergisi, No.272, Mayıs 2011, p. 50 et.seq; Ballar, p. 541 et.seq.

<sup>27</sup> The number of tax-exempt foundations as of 20 July 2011 is 237, <http://www.vgm.gov.tr/db/dosyalar/webicerik195.doc>

<sup>28</sup> Public benefit association statute is also granted by the Council of Ministers upon the advice of the relevant Ministry and the Ministry of Finance and on the proposal of the Ministry of Internal Affairs. In order to obtain public benefit statute, an association must be operating at least for a year and must pursue public benefit (Art.27, Law No. 5253). See also Article 48 et.seq. of Dernekler Yonetmeliği (Official Gazette of 31.3.2005, No.25772).

with the purpose of expending two thirds of their income for public service may be granted tax-exempt statute by the Council of Ministers upon the proposal of the Ministry of Finance. The Law No. 4962 authorizes the Ministry of Finance to regulate the conditions and procedure for the application of tax-exempt statute. The Ministry of Finance has used its authority and released a General Communiqué on this respect<sup>30</sup>. Accordingly, for the tax-exempt statute, the following conditions must be met:

- The purpose of the foundation must be one or a combination of health, social aid, education, scientific research and development, culture, environmental protection and/or forestation purposes. The activities of such foundations must have a diminishing effect on the State's public service burden.
- The foundation must have started to operate publicly for at least a year prior to the application.
- The foundation must have complied with book keeping and accounting obligations;
- The foundations of asset value and yearly income must be at least TRL 735.000 and TRL 71.000 respectively.
- For the year prior to the application, two thirds of gross income of the foundation must have been allocated to the abovementioned public purposes. This condition must continuously be met during the tax-exempt statute<sup>31</sup>.

After the first assessment of tax exemption request by the Ministry of Finance, the opinions of GDF and other related government agencies that work in an area related to the purposes listed above are taken. These opinions need to be based on an audit that measures the contributions of the foundation by way of sharing the government's burden of public service undertakings.

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<sup>29</sup> Bazi Kanunlarda Değişiklik Yapilmasi ve Vakıflara Vergi Muafiyeti Taninmasi Hakkında Kanun, No.4962, Official Gazette of 7.8.2003, No. 25192. For prior application of tax-exempt statute, see Arts. 4 and 5 of Law No.903 (Official Gazette of 24.7.1967, No.12655).

<sup>30</sup> Vakıflara Vergi Muafiyeti Taninmasi Hakkında Genel Teblig, Seri No.1, Official Gazette of 3.4.2007, No. 26482.

<sup>31</sup> The general requirement is to expend two thirds of the yearly income for the foundation's purpose within the same year. However, surplus funds can be deferred to be expended within a maximum of three years with the permission of the Ministry of Finance. Two years of further extension may also be granted.

Furthermore, the activities of the applicant foundation from its establishment until the date of inspection are reviewed by the tax inspectors of the Ministry of Finance<sup>32</sup>.

The foundations operating under tax-exempt statute are supervised on yearly basis by the Ministry of Finance. For tax-exempt foundations, the procedural obligations such as book keeping, yearly reporting, approval of annual reports by tax advisors under oath are strictly regulated.

In cases where a tax-exempt foundation has not complied with its obligations, or has operated for other purposes, or changed its charter without permission, or an impossibility to realize its purpose has emerged, the Council of Ministers has the authority to repeal the tax-exempt statutes upon the proposal of the Ministry of Finance. In such cases, the foundation is not entitled to apply for the next five years to renew its tax-exempt statute.

## **2.2. Tax consequences**

The legal effect of the tax-exempt statute on the fiscal obligations of a foundation is limited<sup>33</sup>. The overall tax consequences of the tax-exempt statute are summarized in this part. However, the tax treatment of a foundation will be explained in detail in the subsequent chapters,

Tax-exempt statute is not applicable on corporate income tax applied on profits of business enterprises of foundations or on interest income, dividends, rents or capital gains received by the foundation itself. Nevertheless, the tax-exempt statute grants donors the right to deduct their donations to tax-exempt foundations from their taxable income to a certain extent.

Similarly, tax-exempt statute does not generate a general exemption on the value added tax applied on the supplies of goods and services of a foundation or vice versa. However, the supply of goods and services conducted for the purpose of cultural, educational and social purposes by tax-exempt foundations is exempt from value added tax. In addition, certain supplies made by taxable persons to tax-exempt foundations benefit from exemptions specified by the law.

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<sup>32</sup> For further details, see EFC Country Profile January 2011: Turkey, drafted by T.Basak Ersen, Namik Ceylanoglu, Hayati Sahin (TUSEV) (<http://www.efc.be/Legal/Documents/turkey.pdf>)

<sup>33</sup> For a general view on favorable and unfavorable aspects of granting tax exemptions to foundations, see Iseri, Ahmet, "Turk Vergi Hukuku Acisindan Vakiflar", Ankara Universitesi Hukuk Fakultesi Dergisi, Vol.27, No. 3-4, 1970, p.249 et.seq.

Asset allocations to tax-exempt foundations are exempt from inheritance and transfer tax.

Tax-exempt foundations are exempt from real estate tax applied on their buildings provided that those buildings are allocated to the purpose specified in their charter. In addition, such foundations are also exempt from registration fees applied on the immovable property donations, acquisitions or sales.

Non-resident foundations do not benefit from any local exemption, since they are not founded in terms of Turkish law and not accepted as public-benefit foundations.

### **2.3. Constitutional consequences**

Under the Law No. 4962, tax-exempt statute is granted to a foundation by the Council of Ministers. In addition, the conditions that are sought for the tax-exempt statute are determined by the Ministry of Finance. The authority used by the executive organs to decide a foundation to be exempt from taxation has correctly been criticized in the Turkish tax literature, since such a delegation without determining the conditions in the law is incompatible with the legality principle<sup>34</sup> specified in Article 73 of the Turkish Constitution<sup>35</sup>.

## **3. Income tax obligations**

### **3.1. Tax treatment of business income**

According to the Foundations Law, in order to support and realize their goals and earn income, foundations are entitled to establish business enterprises. However, income from business enterprises must be allocated to the main purpose of the foundation (Art.26, FL). Foundations are obliged to inform the GDF about their company establishments or purchases of company shares<sup>36</sup>.

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<sup>34</sup> See Gunes, Gulsen, Verginin Yasalligi Ilkesi, 2.Basi, XII Levha, İstanbul, 20098, p.153 et.seq.

<sup>35</sup> For example, see Öz, Ersan, Vergilendirme Kanunilik ve Turk Vergi sistemi, Gazi Kitabevi, Ankara, 2004, pp.193-194; Yereli, Ahmet Burcin, " Vakiflarin Vergi Muafiyeti ve Uc Hukuki Yanlis", Vergi Sorunlari, No. 184, January 2004, p. 112; Goker, Cenker, "Vergilerin Yasalligi İlkesi Kapsamında Vakıflara Vergi Muafiyeti Taninmasi Üzerine", Mualla Öncel'e Armagan, Vol.2, Ankara Universitesi Yayinlari No.243, Ankara, 2007, p. 1045 et.seq; Ustun, Umit, "Bakanlar Kurulunca Vakıflara Vergi Muafiyeti Taninmasinin Degerlendirilmesi, Vergi Sorunlari, No. 277, October 2011, p.98; Also see Guneri, pp.293-295. For a contrary opinion, see Cagan, Nami, Vergilendirme Yetkisi, Kazanci, Ankara, 1980, pp.140-141.

<sup>36</sup> Vakıflar Yönetmeliği, Art.37 (Official Gazette of 27.9.2008, No.27010)

Under the Corporate Income Tax Law (CITL)<sup>37</sup>, foundations and associations are not themselves taxable, but the business enterprises owned and operated by them are subject to corporate income tax in the same manner as capital companies such as corporations and limited liability companies (Art.1, CITL). The income of commercial, industrial and agricultural enterprises, other than capital companies, owned by or affiliated to foundations and associations are subject to 20% CIT, provided that their activities are continuous in nature. Similar non-resident enterprises are also considered as taxable entities with respect to CIT (Art. 2(5), CITL). In respect of foundations, whether granted tax-exempt statute or not, their business enterprises do not benefit from a special privilege regarding CIT.

The supply of goods and services for consideration in the market economy is generally considered as a business activity. For a business enterprise to exist, (i) interdependence between the foundation and the enterprise in terms of capital or administration, (ii) existence of a commercial, industrial or agricultural activity and (iii) continuity of such activities are required. An activity is characterized as an exercise of business if it is pursued in a sustained manner and for the purpose of realizing sales of goods or services, regardless of existence of actual profit. Continuity of the activity does not mean many repetitions; rather, the existence of an organization and the intention to continue suffices. It is not essential for the existence of an enterprise that an activity is pursued for non-profit purposes, or the enterprise does not have legal personality, capital, permanent establishment or independent accountancy, or the prices of goods and services are equal to the cost, or no profits are actually accrued, or the profits are allocated to the foundation's purposes (Art. 2(6), CITL)<sup>38</sup>.

According to the temporary Article 2 of the CITL, which is in force from 1 January 2008 till 31 December 2015, leasing of immovable property or acquisition and disposal of securities (shares and bonds and certain capital market instruments) shall not constitute a business enterprise of a foundation or association. This provision is strongly criticized in the literature<sup>39</sup>, since such activities are not already considered under the scope of the concept of

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<sup>37</sup> Kurumlar Vergisi Kanunu, No.5520 (Official Gazette of 21.6.2006, No.26205).

<sup>38</sup> For the Supreme Administrative Court's interpretation, see Supreme Administrative Court, Unification Chamber Decision, E.1992/2, K.1994/2, 16.6.1994, Official Gazette of 3.4.1995, No.22247; For the Ministry of Finance's explanations, see Kurumlar Vergisi Genel Tebliği, Seri No.1, Official Gazette of 3.4.3007, No. 26482.

<sup>39</sup> Kirman, Ahmet, "Vakıfların Vergilendirilmesinde Vergi İdaresinin Yeni Yaklaşımları ve Gecerliliği", Mualla Öncel'e Armagan, Vol.2, Ankara Üniversitesi Yayınları No.243, Ankara, 2007, p.427 et.seq.

business enterprise by the judiciary<sup>40</sup>. On the other hand, deriving interest income from bank accounts, bonds and debentures do not constitute a business enterprise<sup>41</sup>.

Under Article 5(i) of the CITL, earnings from rehabilitation centers owned by tax-exempt foundations and public benefit associations are exempt from CIT for 5 years.

### **3.2. Tax treatment of investment income**

Although foundations and associations are considered neither corporate income tax payer nor individual income tax payer, Article 94 and Temporary Article 67 of the Individual Income Tax Law (ITL)<sup>42</sup> regulate a final income withholding tax regime applicable on investment income of such entities<sup>43</sup>.

The Foundations Law entitles the foundations to establish companies (Art.26)<sup>44</sup>. Dividends received from resident companies by foundations, whether tax-exempt statute is granted or not, are subject to a 15% final income withholding tax (Art.94(6)(b), ITL). The transfer of profits of business enterprises to the foundations are considered as a dividend distribution<sup>45</sup>.

Interest income received from bank accounts by foundations, whether granted tax-exempt statute or not, is subject to 15% final income withholding tax (Temporary Art.67, ITL). Furthermore, interest income derived from government bonds and debentures by foundations, whether granted tax-exempt statute or not, is subject to 10% final income withholding tax (Art.67, ITL).

Foundations, whether granted tax-exempt statute or not, are subject to a 20% final income withholding tax on their rental income from immovable property (Art.94(5)(b), ITL).

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<sup>40</sup> For example, Supreme Administrative Court, 4th Chamber, E.2003/1918, K.2004/2487, 8.12.2004; Supreme Administrative Court, 4th Chamber, E.2006/1335, K.2006/376, 7.3.2006; Supreme Administrative Court, 9th Chamber, E.1998/4854, K.1999/1481, 14.4.1999.

<sup>41</sup> Supreme Administrative Court, 4th Chamber, E.2005/1787, K.2005/2351, 30.11.2005.

<sup>42</sup> Gelir Vergisi Kanunu, No.193 (Official Gazette of 6.1.1961, No.10700).

<sup>43</sup> Bakanlar Kurulu Kararı, No.2009/14592 (Official Gazette of 3.2.2009, No.27130).

<sup>44</sup> See Tufekcioglu Nevzat, "Vakıfların Şirketlere Ortaklığı", Vergi Dunyasi, No. 283, March 2005, p.14 et.seq.

<sup>45</sup> Supreme Administrative Court, 4th Chamber, E.2003/948, K.2004/432, 9.3.2004. See also Supreme Administrative Court, 4th Chamber, E.2006/4937, K.2007/3286, 24.10.2007.

Royalties received by foundations, whether granted tax-exempt statute or not, are subject to 20% final income withholding tax (Art.94(5)(b), ITL).

Capital gains derived from the disposal of government bonds and debentures by foundations, whether granted tax-exempt statute or not, are subject to %10 final income withholding tax. However, the disposal of shares quoted on the Istanbul Stock Exchange is subject to a zero rate income withholding tax (Temporary Art. 67), whereas income from investment funds are subject to %10 final income withholding tax. Capital gains derived by foundations from the disposal of other shares are not subject to income tax. In addition, capital gains derived by foundations from the disposal of immovable property do not fall under the scope of ITL; i.e. they are non-taxable.

### **3.3. Tax treatment of remunerations and provident benefits**

#### **3.3.1. Employees' remunerations**

There is no specific tax privilege applied on wages paid by foundations to their employees. As an employer, foundations must withhold income withholding taxes applied on wages of the employees (Art.94, ITL).

In Turkish tax law, wages consist of money or benefits in kind which can be represented in terms of money provided to workers employed in a certain enterprise in return for their services (Art.61, ITL). The meaning of the term wage, as regulated in the Income Tax Law, covers allowances, indemnities, compensation for financial responsibility, wage raise, advances, daily attendance allowances, premiums, gratuities, reimbursement of expenses, etc. or emoluments calculated as a certain percentage of revenue, provided that it is not related to a partnership arrangement. Wages and salaries paid to employees are subject to withholding tax according to the normal rate structure; i.e. progressive tax tariff.

#### **3.3.2. Provident benefits and others**

According to Article 25(2) of ITL, provident benefits made by charitable associations and provident funds<sup>46</sup> to poor people for lifelong or certain periods are exempt from income tax.

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<sup>46</sup> Provident funds can be established in the form of foundations for social solidarity, pension or provident purposes of their members.

Provident payments made to their members by provident funds according to their charter for reasons such as death, health, disability, birth and marriage (Art.25(9), ITL) are exempt from income tax.

Payments by provident funds to their members who paid premiums or contributions for ten years or less are subject to income withholding tax (Art.94(15), ITL).

### **3.4. Tax treatment of gifts and donations**

#### **3.4.1. Foundations**

Since foundations (and associations) are not taxable themselves, gifts and donations made to such entities are not taxable.

#### **3.4.2. Donors**

Under the ITL and CITL, donations and gifts made to foundations that do not have tax-exempt foundation statute are not deductible in calculating the taxable base of donors whether individual or corporate. Under certain conditions, however, charitable donations made in cash or in kind to tax-exempt statute foundations and public benefit associations are deductible. The allowable donation, for which a receipt must be obtained, may not exceed 5% (10% for the development priority regions) of the taxable income of the donor in the relevant taxable period (Art. 10(1)(c), CITL and Art.89(4), ITL)<sup>47</sup>.

Donations in cash or in kind to tax-exempt foundations and public benefit associations for construction, maintenance and operating of schools, health centers, student hostels, children day care centers, rest homes for the elderly and nursing and rehabilitation centers may be deducted without restrictions (Art.10(1)(c), CITL and Art.89(5), ITL).

Donations to tax-exempt foundations and public benefit associations for the restoration, maintenance and repair of historic monuments, buildings and works, or for the construction of

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<sup>47</sup> In other special laws, such as the Disaster Law No.7269 or Social Support and Solidarity Law No. 3294, there are special provisions which stipulate that donations made to certain foundations, whether tax-exempt or not, are fully deductible. For information on such special rules, see Mac, Mehmet; Jamali, Tarik, Veraset, Hibe ve Ölüm (<http://www.bdo.com.tr/vergi/dosyalar/veraset/KISIM%20II.pdf>). For updated information, see Türkiye Ucuncu Sektör Vakfı, Vakıf ve Derneklere İlişkin Kamu Yararı Raporu, İstanbul, March 2008, p.44 (<http://www.tusev.org.tr>).

libraries, museums, galleries, cultural centers, and of buildings for theatre, film and concert performances are also fully deductible (Art.10(1)(d) CTL and Art.89(7), ITL). Donations to Turkish Red Crescent Association (except its business enterprises) are deductible in full (Art.10(1)(f), CTL and Art.89(11), ITL).

Donations of food, cleansing, clothing and heating materials to foundations and associations, whether tax-exempt or not, which operate for food banking purposes are fully deductible (Art.89(6), ITL)<sup>48</sup>.

The Foundations Law stipulates that individuals and legal entities which sponsor scientific organizations, strategic researches, conferences, symposiums and similar cultural activities conducted in order to make research on, improve and support foundation culture within the country or abroad are entitled to deduct such sponsorship costs from their income and corporate income tax bases (Art.77, FL).

However, wage earners do not benefit from the abovementioned donation deductions since they are taxed on (final) withholding basis, not on assessment basis.

### **3.5. Tax treatment of liquidation**

The foundation may dissolve ipso facto if the realization of its purpose becomes impossible to achieve or to amend, or if the object of the foundation becomes contrary to the legislation (Art.116, TCC). The foundation board, the GDF, or the Public Prosecutor may request from the court the registration of its liquidation<sup>49</sup>. Any estate or rights that remain after the settlement of the debts of a liquidated foundation is transferred to the entity that is designated in the foundation's charter. If there is no such entity, the court allocates the foundation's assets to another foundation with a similar purpose (Art.27, FL)<sup>50</sup>. There is no specific tax rule for the liquidation of foundations. General rules apply in such cases.

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<sup>48</sup> See also, *Gidaların Üretimi, Tüketimi ve Denetlenmesine Dair Kanun Hükmünde Kararnamenin Degistirilerek Kabulü Hakkında Kanun*, No. 5179, Official Gazette of 5.6.2004, No.25483; *Gelir Vergisi Genel Tebliği*, Seri No:251, Official Gazette of 21.3.2004, No.25409.

<sup>49</sup> Art.19 et.seq of *Vakıflar Yönetmeliği* (Official Gazette of 27.9.2008, No.27010).

<sup>50</sup> Art.22 of *Vakıflar Yönetmeliği* (Official Gazette of 27.9.2008, No.27010).

## 4. Value Added Tax

### 4.1. Scope

For transactions conducted by non-profit organizations, general principles of the Value Added Tax Law (VATL)<sup>51</sup> apply. The VATL clearly stipulates that the legal status or nature of a taxable person is not relevant for a possible VAT liability (VATL, Art.1). Accordingly, the supply of goods and services within the scope of commercial, industrial, agricultural or independent professional activities carried out in Turkey by national and local government agencies and establishments, universities, *associations*, *foundations* and all kinds of professional organizations are subject to VAT (Art.1(3)(g),VATL). Thus, business enterprises of foundations and associations are considered as taxable persons with respect to their commercial, industrial, agricultural or professional activities<sup>52</sup>; however, certain exemptions apply to tax-exempt foundations and public benefit associations (see below).

Importation of all kinds of goods and services are subject to VAT. It is immaterial whether importation is carried out by a public or private body, any natural or juridical person, or in any manner or nature whatsoever (Art.1(2) VATL). However, importation of goods and services that are exempt from VAT if supplied in Turkey is exempt from VAT (Art. 16(1)(a), VATL). Hence, in cases where a foundation is granted an exemption for certain domestic goods or services, the importation of similar goods and services benefits from the VAT exemption<sup>53</sup>.

Leasing of the goods and rights stated in Article 70 of the ITL is subject to VAT (Art.1(3)(f), VATL). Goods and rights enumerated in the mentioned Article include immovable property such as land, buildings, mines and rights which are in the nature of immovable property; and "other goods and rights" such as all kinds of motor vehicles, machines and equipment, ships, literary, artistic and commercial copyrights, commercial or industrial know-how, patents, trademarks, licences and similar intangible properties and rights. However, leasing of immovable property and rights in the nature of immovable property is taxable only if they constitute a part of the business assets of an entrepreneur (Art.17(4)(d), VATL). Thus, leasing transactions of immovable property of a foundation or an association is not subject to VAT, unless the immovable property is included in the assets of the business enterprises of the

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<sup>51</sup> Katma Deger Vergisi Kanunu, No.3065 (Official Gazette of 2.11.1984, No.18563).

<sup>52</sup> See Mac, Mehmet, KDV Uygulamasi, 4th Edition, Denet, Istanbul, 1998, p.1.31. et.seq.

<sup>53</sup> For example, see Supreme Administrative Court, 7th Chamber, E.1991/2686, K.1994/1143, 8.3.1994.

foundation or association. Leasing of "other goods and rights" is taxable whether or not persons exploiting them are entrepreneurs. Consequently, leasing of other goods and rights by foundations and associations are subject to VAT<sup>54</sup>.

## 4.2. Exemptions

Under the Value Added Tax Law (VATL), cultural, educational and social exemptions (without credit for previously paid VAT) are applied on the supplies of specific goods and services of tax-exempt foundations and public benefit associations. The following goods and services, when supplied by national and local public institutions, universities, political parties, trade unions, agricultural cooperative societies, *tax-exempt foundations, public benefit associations*, social security institutions and other officially qualifying organizations, in performance of their regular activities are exempt from VAT (Art. 17(1), (2) VATL):

- goods and services supplied for the purpose of promoting and encouraging scientific, artistic and agricultural activities (Art.17(1)(a), VATL);
- goods and services supplied by operating theatres, concert halls, libraries, sports facilities, reading rooms and conference halls (Art.17(1)(b), VATL); and
- goods and services supplied by operating hospitals, clinics, dispensaries (including goods and services supplied between such health institutions), human blood and organ banks, public parks, monuments, botanical and zoological gardens, veterinarian, bacteriological, serological and similar laboratories, school dormitories, orphanages and homes for elders (Art.17(2)(a), VATL).

The above exemptions generally follow the exemptions specified in Article 132 of the VAT Directive No. 2006/112/EC<sup>55</sup>, except for the educational activities<sup>56</sup> provided by the universities founded by Turkish foundations. Although such universities are characterized as public entities by the Constitutional Court<sup>57</sup>, they are not placed by the judiciary and the tax administration on the same footing as public universities in terms of VAT, therefore do not

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<sup>54</sup> In cases where the service is rendered by a person who is not an entrepreneur, the recipient of the service is assigned as a withholding agent.

<sup>55</sup> Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L347/1, 11.12.2006).

<sup>56</sup> Art. 132 (1)(i) of the VAT Directive 2006/112/EC.

<sup>57</sup> Constitutional Court, E.1990/2, K.1990/10, 30.5.1990 (Official Gazette of 9.2.1991, No. 20781).

benefit from any exemption. This application of the tax administration and the interpretation of the judiciary<sup>58</sup> are strongly criticized in the literature<sup>59</sup> in terms of equality principle guaranteed under Article 10 of the Constitution.

The following supplies of goods and services by taxable persons to tax-exempt foundations and public benefit associations are exempt from VAT:

- all kinds of supplies, made without any consideration, to the tax-exempt foundations and public benefit associations (Art.17(2)(b), VATL);
- food, cleansing, clothing and heating materials donated to foundations and associations which operate for food banking purposes (Art. 17(2)(b), VATL);
- the supply of goods and architectural services to tax-exempt foundations and public benefit associations for restoration or renovation projects of immovable property, registered as historical buildings under the Law on Protection of Cultural and Natural Wealth (the total amount of the consideration with respect to these goods and services must be at least TRL 700)<sup>60</sup>; and
- supplies made to foreign charity institutions which will deliver the purchased goods or services to the tax-exempt foundations and public associations are also exempt from VAT (Art.17(2)(c), VATL), provided that the price of the relevant goods or services is at least TRL 5,000. For this exemption to be carried out, application to the Ministry of Finance is compulsory<sup>61</sup>.

## **5. Inheritance, Estate and Gift Taxes**

### **5.1. Inheritance and Transfer Tax**

Under the Inheritance and Transfer Tax Law (ITTL)<sup>62</sup>, the transfer of any immovable and movable property, wherever situated, as inheritance or gift is subject to the inheritance and

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<sup>58</sup> For example, see Supreme Administrative Court, 11th Chamber, E.1997/785, K.1998/3508, 19.10.1998; Supreme Administrative Court, General Tax Chambers Assembly, E. 2006/150, K.2006/230, 29.9.2006.

<sup>59</sup> Sakar, Ayse Yigit, "Vakif Universitelerine Uygulanan Ayrımcılık: Katma Deger Vergisi Mukellefiyeti", in Sadik Kirbas'a Armagan, eds. Kocak, Mustafa; Teker, Suat, Okan Universitesi Yayinlari, Istanbul, 2011, p.179 et.seq.

<sup>60</sup> Katma Deger Vergisi Genel Tebliği, Seri No.96 (Official Gazette of 19.11.2005, No. 25997).

<sup>61</sup> Katma Deger Vergisi Genel Tebliği, Seri No.79 (Official Gazette of 23.12.2000, No.24269).

<sup>62</sup> Veraset ve Intikal Vergisi Kanunu, No.7338 (Official Gazette of 15.6.1959, No.10231).

transfer tax rules. The taxable persons are the beneficiaries of assets or property transferred as inheritance or gift. The transfer is subject to tax if either the transferor is a Turkish citizen or the property being transferred is situated in Turkey.

Article 3(b) of the ITTL stipulates that legal entities established for public purposes such as science, research, culture, arts, health, education, religion, charity and sports are tax exempt. Thus, foundations founded for the abovementioned purposes, whether granted tax-exempt statute or not, benefit from the exemption<sup>63</sup>; no inheritance and transfer tax applies to donations and gifts made to such foundations. Furthermore, gifts and donations made by such qualified foundations are exempt from inheritance and transfer tax, provided that they are compatible with the purpose of the foundation specified in their charter (Art.4(f), ITTL).

In addition, the transfer of assets to tax-exempt foundations, either upon their formation or with respect to subsequent transfers, is exempt from the inheritance and transfer tax (Art.4(k), ITTL). However, the Foundations Law stipulates that immovable and movable properties endowed to a foundation upon or after its establishment are exempt from inheritance and transfer tax (Art.77, FL). Therefore, a foundation does not necessarily have the tax-exempt statute to benefit from the exemption.

## **5.2. Real Estate Tax**

Real estate tax imposed by the municipalities under the Real Estate Tax Law (ETL)<sup>64</sup> is composed of the building tax and the land tax. The taxpayer is a legal person or individual who owns the property or the usufruct or enjoys the benefits like an owner. Foundations having tax- exempt statute benefit from real estate tax exemption for their buildings<sup>65</sup>, provided that the buildings are allocated to the main purpose specified in their charter and neither leased nor rented to third parties (Art.4 (m), ETL)<sup>66</sup>. Foundations without tax-exempt status do not benefit from real estate tax exemption for their buildings<sup>67</sup>. However, albeit not

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<sup>63</sup> Supreme Administrative Court, 7th Chamber, E.1997/2690, K.1998/3166, 6.10.1998; Supreme Administrative Court, 9th Chamber, E.1990/2731, K.1991/3337, 20.11.1991.

<sup>64</sup> Emlak Vergisi Kanunu, No.1319 (Official Gazette of 11.8.1970, No.13576).

<sup>65</sup> Buildings of public benefit associations also benefit from real estate tax exemption, provided that the building is not owned by or allocated to the associations business enterprises (Art.4(e), ETL).

<sup>66</sup> See Supreme Administrative Court, 9th Chamber, E.2005/5384, K. 2006/1313, 13.4.2006.

<sup>67</sup> Nevertheless, whether granted by tax-exempt status or not, foundations founded to support Turkish Armed Forces also benefit from the exemption for their buildings (Art.4(n), ETL).

granted specifically to foundations, those entities may benefit indirectly from another exemption specified in Article 4(f) which stipulates that hospitals, dispensaries, rehabilitation, diagnosis and treatment centers, sanatoriums, student dormitories, alms houses, orphanages, infirmaries, day nurseries, libraries and similar buildings are exempt from real estate tax, provided that they are operated for non-profit purposes<sup>68</sup>.

There is no exemption for the land tax for foundations.

## **6. Other Taxes**

### **6.1. Customs Duties**

According to Customs Law (CL)<sup>69</sup>, the importation of certain goods, devices and equipments used for scientific and health purposes by tax-exempt foundations and public benefit associations is exempt from customs duties, provided that no commercial purposes is sought and they are used only for the purposes of those entities (Art.167(7), CL). Such goods include scientific devices, equipment and goods used for education, science and cultural purposes, equipments and devices used for health diagnosis, treatment and research and animals, biological and chemical materials used for scientific research purposes etc.

### **6.2. Stamp Duties**

Particular documents related to contracts, bills and other commercial transactions listed in Stamp Duty Law (SDL)<sup>70</sup> are subject to stamp duty<sup>71</sup>. In general, foundations are regarded as taxable persons with respect to their transactions and are covered by the stamp duty tax. However, there are two exceptions to this rule. Firstly, the charter of a tax-exempt foundation drawn up during its establishment is exempt from stamp duty tax. Second exception provides

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<sup>68</sup> Supreme Administrative Court, 9th Chamber, E.1995/103, K.1995/2989, 14.11.1995; Supreme Administrative Court, 9th Chamber, E.1984/1829, K.1985/424, 13.3.1985.

<sup>69</sup> Gumruk Kanunu, No.4458 (Official Gazette of 04.11.1999, No. 23866).

<sup>70</sup> Damga Vergisi Kanunu, No.488 (Official Gazette of 11.7.1964, No.11751).

<sup>71</sup> Kirman, Ahmet, 488 Sayili Damga Vergisi Kanunu Serhi, Kozan, Ankara, 1992, p.2 et.seq.

that all documents drawn up by foundations, whether tax-exempt or not, which are established to support Turkish Armed Forces is exempt from stamp duty tax (Art. 9, SDL)<sup>72</sup>.

### **6.3. Motor Vehicle Tax and Special Consumption Tax**

No specific exemptions or privileges are granted to foundations with respect to motor vehicle tax<sup>73</sup> and special consumption tax<sup>74</sup>.

### **6.4. Municipal Taxes**

No specific exemptions or privileges are granted to foundations with respect to municipal taxes<sup>75</sup>, such as advertisement tax and environment tax or building construction fees paid to municipalities.

### **6.5. Deed Fees**

Under the Fees Law<sup>76</sup>, it is stipulated that the tax-exempt foundations are exempt from notary fees during their establishment. Donations to tax-exempt foundations are also exempt from notary fees (Art.38). In addition, tax-exempt foundations are exempt from title deed fees applied on the registration of immovable property and rights in rem (Art.59). Foundations that do not have tax-exempt statute are not entitled to any fee exemptions.

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<sup>72</sup> However, all documents drawn up by public benefit foundations benefit from a general stamp duty tax exemption. See Annex to SDL, Art.17.

<sup>73</sup> Motorlu Tasitlar Vergisi Kanunu, No.197 (Official Gazette of 23.2.1963, No.11342).

<sup>74</sup> Ozel Tuketim Vergisi Kanunu, No.4760, (Official Gazette of 12.6.2002, No.24783).

<sup>75</sup> Belediye Gelirleri Kanunu, No.2464, (Official Gazette of 29.5.1981, No.17354).

<sup>76</sup> Harclar Kanunu, No.492 (Official Gazette of 17.7.1964, No.11756).