

First Step in Turkey: Liaison Office or Branch?

The ongoing financial turmoil has caused foreign investors, which contemplate entering the Turkish market, to act more prudently. The necessity of avoiding substantial tax liability and further hesitations as regards a new market have directed such investors to resort to more marginal solutions such as establishing a liaison office (*irtibat burosu*) or a branch (*sube*) as a first step prior to incorporating a separate legal entity in Turkey. Which one of these two alternatives is the right choice depends on the investor's business needs and thus should be evaluated on a case-by-case basis.

1. Nature and activities

1.1 Liaison Office

First of all, liaison office does not have a legal personality (*tuzel kisilik*). Accordingly, it can neither acquire any rights nor undertake any obligations. For instance, it cannot be a party to any commercial agreement.

The establishment of a liaison office in Turkey is carried out in accordance with the Law No. 4875 on Foreign Direct Investments¹ (the **Law**), which stipulates that the Undersecretariat of Treasury (the **Treasury**) is the supervisory authority for such process.

Pursuant to the Regulation for Implementation of the Law² (the **Regulation**), the entity founding the liaison office (*i.e.*, the investor itself) must be established in the form of a "company" in accordance with the laws of its country of origin. The major point to note is that liaison offices cannot engage in any commercial activity. The conduct of any income-generating activity in Turkey through a liaison office is strictly prohibited.

1.2 Branch

Branch does not have a legal personality, either. Branch's main advantage in comparison to liaison office is that it enables foreign investors to carry out commercial activities in Turkey.

Although branch is registered with the relevant Trade Registry as though it is a separate legal entity, it is not totally independent from its parent company. Thus, the scope of activity of a branch is limited to that of its founder. A branch, which conducts business in Turkey, does so for and on behalf of its parent company. It may be argued that branch acts as a representative of the relevant foreign company within Turkey.

2. Establishment formalities, registration with tax authority and notification to the Treasury

2.1 Liaison Office

Since liaison offices are prohibited from engaging in any commercial activity, their supervision is a must. Pursuant to the Regulation, the Treasury is empowered to authorize legal entities established abroad to open a liaison office in Turkey by issuing an establishment permit (*irtibat burosu acma izni*). The Regulation provides that applications for establishment permit shall be finalized within five (5) business days from the submission date provided that the application file is complete. Although the Regulation stipulates a list of required documents, the Treasury may always request, at its discretion, additional documentation or information while evaluating an application, which may eventually prolong the five-day period. Any establishment permit determines the scope of non-commercial activities that the relevant liaison office may carry out (*e.g.*, market research).

One should bear in mind that in the regulated sectors, the process of liaison office establishment is subject not only to the Law, but also to the applicable sector-specific legislation. The relevant regulatory body (*e.g.*, the Capital Markets Board, the General Directorate of Insurance of the Treasury, the Banking Regulation and Supervision Agency) is the competent authority in such process.

¹ Published in the Official Gazette dated 17 June 2003 and numbered 25141.

² Published in the Official Gazette dated 20 June 2003 and numbered 25205.

Once an establishment permit is issued, the liaison office has to be registered with the respective Tax Authority and obtain a tax registration number. Subsequently, it has to send a copy of its tax office registration documents (e.g., tax plate) to the Treasury within one (1) month from its registration with the Tax Authority, at the latest.

Liaison offices are also required to send annually the "Data Form for Liaison Office Activities" (*Irtibat Burolarinin Faaliyetlerine Iliskin Bilgi Formu*) to the Treasury until the end of May, at the latest. Such form aims to provide information on the liaison office's activities occurred within the previous year. Documents evidencing that the office expenses have been covered by the funds transferred from abroad have to be enclosed to such form.

2.2 Branch

Neither the Law nor the Regulation requires permission from the Treasury for the establishment, by foreign legal entities, of a branch in Turkey. Nevertheless, if a foreign legal entity intends to establish a branch in Turkey, an application has to be made to the General Directorate of Domestic Trade of the Ministry of Trade and Commerce (the **Ministry**) together with the supporting documents. Upon approval of the Ministry, the necessary documents should be submitted to the relevant Trade Registry for registration and announcement on the Trade Registry Gazette. We note that registration with the Trade Registry triggers additional expenses compared to liaison offices.

Within one (1) month from the registration with the relevant Trade Registry, an application to the relevant Tax Authority has to be made in order to obtain a tax registration number and finalize other tax-related formalities.

Finally, pursuant to the Regulation, an establishment notification has to be made to the Treasury via "FDI Operations Data Form" (*Dogrudan Yabancı Yatirimlar Icin Faaliyet Bilgi Formu*) until the end of May each year, at the latest, for statistical purposes. Information on payments made to the equity accounts of the branch has to be submitted as well to the Treasury in accordance with the "FDI Capital Data Form" (*Dogrudan Yabancı Yatirimlar Icin Sermaye Bilgi Formu*) within one (1) month following such payments.

3. Term

3.1 Liaison Office

A liaison office establishment permit may be issued for a maximum period of three (3) years. Upon its expiry, an application may be made for the extension of its term for an additional period of three (3) years. When assessing such application, the Treasury takes into account the previous years' activities of the relevant liaison office together with its future projects and objectives.

3.2 Branch

There is no restriction on the term of branches. In other words, a branch may be incorporated for an indefinite period of time.

4. Expenses and transfer of profit

4.1 Liaison Office

Any and all office expenses have to be covered by the foreign exchange imported from abroad. Since liaison offices cannot engage in income-generating activities, there would never be a transfer of profit.

4.2 Branch

As explained above, branches may conduct business in Turkey for and on behalf of their founder entity. Therefore, unlike liaison offices, branches will be subject to applicable tax schemes including corporate tax (*kurumlar vergisi*) and withholding tax.

Pursuant to the Law, foreign investors can freely transfer abroad net profits, dividends, proceeds from the sale or liquidation of all or any part of an investment, compensation payments, amounts arising from license, management and similar agreements, and reimbursements and interest payments arising from foreign loans through banks or other financial institutions.

5. Employment

5.1 Liaison Office

Although a liaison office does not have a separate legal personality, it may have (employ) personnel. However, only one (1) foreign key personnel may be employed by each liaison office.

In addition, the Income Tax Law No. 193³ (*Gelir Vergisi Kanunu*) stipulates that the payments made to a liaison office's employees are exempted from income tax provided that the conditions listed under such law are fulfilled.

5.2 Branch

There is no restriction on the number of foreign persons to be employed by branches. Therefore, apart from Turkish ones, more than one (1) foreign key personnel may work at a branch.

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³ Published in the Official Gazette dated 6 January 1961 and numbered 10700.