

TIPS & ADVICE: INVESTING IN TURKEY

The relaxation of reciprocal ownership laws has helped to drive investment activity in Turkey, with residential property acquisitions by foreigners has grown up by more than 50% over the first half of the year. It seems that acquisitions by foreigners and foreign direct investment flow will increase, if the market continues to hold its favourable conditions in every aspect. If you consider investing in Turkey, it would be useful to follow the tips given by Turkish market professionals on the following pages.

Acquiring property in Turkey

Due to potential increase in value and rental income, acquiring property in Turkey seems quite attractive, especially compared to European countries. Since the greatest medium and long-term benefit can be realised in residential investments, it will be helpful to consider and review the following information.



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LOCATION

Location is one of the most important issues to consider in any real estate investment. When Turkey is examined from a broad perspective, urban centres with powerful industrial sectors and local economies, such as in Istanbul, Ankara, Izmir, Gaziantep, Denizli, Samsun, Adana, and Konya, offer attractive opportunities for residential investment.

When examined on the city level, it can be beneficial to evaluate alternative investment opportunities, such as regions in the suburbs and centres developing on the outskirts of cities. Even though city centres are always attractive, the fact that prices have peaked in certain areas means it will take longer to realise a return on investment. Another reason for choosing developing centres in the suburbs with significant potential is that prices are more reasonable and they promise higher returns in the medium to long-term.

INVESTOR

The value of real estate property is affected by effective project design, the quality of the materials, workmanship, and market recognition of the project. In this respect, the investor of the project is almost as important as the location. Their customer satisfaction background and their market reputation must also be taken into consideration. Many aspects such as project design, function and management are shaped with the experience and know-how of the project investor. Even though these elements may not be considered at first, they become increasingly important over the

life of the project and give it added value.

PROJECT PHASE

Real estate investments can be made during the construction phase. In terms of an increase in value, investing during the construction phase offers advantages, but it also means that the investor is ready to bear some portion of the risk. When the economy is boomed, such risk can be predicted more easily; but it is more difficult to forecast outcomes when the economy is stagnant or filled with uncertainty. In times like these, taking advantage of opportunities in completed projects significantly reduces the risk.

PROJECT TYPE

Rent is also an important factor in residential investments. As long as residential units are not rented or used, there are operating expenses to be paid and the property suffers depreciation. So individual investors should consider this factor depending on whether the investment is a flat in an individual apartment, an individual villa or flat in a complex, a 2+1 flat or a 1+1 flat. Based on rising values, it is possible to say that properties purchased from premium projects always provide higher returns than individual properties. In terms of residential types, 1+1 flats change hands very rapidly and 2+1 and 3+1 flats rent more quickly.

MANAGEMENT

In the medium and long-term, the sustainability of the project is important for the investor. The quality of management is at least

as important as the quality of the construction of the property in the medium and long term. With qualified management services, building maintenance will be performed constantly, which prevents these types of losses. Management also works to ensure and enhance the success of the project over time, so it has a significant effect on the value and demand for the investment.

LEGAL ISSUES

It is important that all legal documents for the investment property to be in order. Also, the papers should be verified at the Municipal and Title Deed Offices where the property is located. It is essential that investors should check that if there are outstanding debts or liens of the project. They should also verify that the properties were built within the framework of zoning plans. If the investment property is still under construction, many problems can be prevented by ensuring that the construction permit has been obtained, that investor rights are protected in the sales agreement, that construction ownership deeds have been prepared, and if construction is completed, that a building-use permit (occupancy permit) has been issued, and that it has a property deed.

In light of all these issues, in order to manage investments properly and effectively, it is important to obtain help of professional domestic and international real estate consultants for quick and accurate answers to many questions and risks can be identified in advance.

Legal framework

Within the regulation of the "Law of Reciprocity", the most important problem of the "Residential Permit" has been also regulated on the amendment of the "Law of Foreigners."



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Turkey, which has become one of the most significant countries in respect of real estate purchase and sale, has taken a big step with the "Law of Reciprocity", which has regulated in 2012. In conjunction with the amendment, some of restrictions (as exceptions for certain countries in respect of real estate acquirement) have been abolished. Besides;

- Foreigners are now able to acquire 30 hectare (300,000 sqm) premises in Turkey.
- In conjunction with the amendment, not only premises with the structure, but also unstructured immovable properties can be acquired by foreigners. The premises' project, which has acquired by this manner, must be annotated at the land registry.
- The sale of real estate can be made only 10% of county-level for each county.
- Other than exceptions permitted by special legislation such as Petroleum Law, the Tourism Act, the Law on Industrial Zones, foreign legal entities cannot acquire real estate in Turkey.
- Corporations, who are 50% foreign-owned and established in Turkey are able to acquire real estate with the ratification of the Governor's Office of Urban Planning and Coordination Directorate.
- Within this framework, the amendment made purchasing real estate possible in Turkey for the citizens of all countries, except a few. Within this scope;
 - Turkey does not allow the sale of real estate to the citizens of the countries which Turkey does not recognise officially, and has

restricted in the past with the reciprocal agreements. North Korea, Cuban, South Cyprus and Syria are the some of those countries.

- o Turkey does not allow the sale of the real estate/premises along the Black Sea line, to the citizens of the Ukraine and the Russian Federation. The citizens of the Greece also are not allowed to acquire real estate in the Turkey's entire maritime boundary.

- o Within the ratification of the Ministry of Interior, Iranian citizens are able to acquire real estates in Turkey. The citizens of Iraq, can be able to acquire real estate in Turkey, within the ratification of the Ministry of Foreign Affairs.

- o Within the regulation of the "Law of Reciprocity", the most important problem of the "Residential Permit" has been also regulated on the amendment of the "Law of Foreigners." According to the amendment, if an alien acquire a real estate property with the intention of residency, a year-long residential permit will be given to the alien.

- o This permission will be checked and prolonged every year and after a certain extensity, permanent residency will be given to the relevant alien.

- o Herein, the amendment has provided some opportunities to aliens about the real estate purchase in Turkey, but the reason of the unrealized structural changes, aliens' hesitations are still resuming. Aliens, who purchase the real estate in Turkey should mind that he/she should make an extensive "Title Deed Research". Aliens should not only superintend to the relevant real estate's title, should also control the

latest zoning status of the premises. This zoning status of the premises can be supplied from the mayoralty which has located in the real estate's region. The alien, who decided to purchase a real estate which is on the project, should make a detailed review of the project and the project should also reviewed through an attorney.

Military Forbidden Zone: As it was in the old regulation, the whole regions especially Aegean and the Mediterranean Sea, were enclosed by the names of the " Military Forbidden Zone" and "Safety Zone". The sales process (for the title deed) has been lengthening due to the compulsory permission of the relevant commandership, and the existence of this period discourages aliens.

Title Insurance: The municipal corporation's and the public institution's continuous practices about the land titles and some citizen's antecedent right allegations for the land titles occur the lack of confidence against the "Turkish Title Deed System". To overcome this insecure situation, title insurance system should be established in Turkey. Allied with this system, insurance companies insure the titles for 5-10 years in consequence of the attorneys or appraisers detailed researches and reporting. The insurance companies compensate the damages during this period, the damages which they may arise in the future.

Escrow System Aliens who are purchasing real estate in Turkey generally encounter the problem as

the absence of the "Escrow System." The basic processes of the sales are not carried out through the bank and trust accounts, and it causes nuisance for aliens. Within the system which is called as "Escrow", aliens perform the purchase and sale process of the real estate securely. In the Escrow System, income from sales, deposits and other costs, attorney- fee, real estate agent fees are hold in a single and earmarked bank account, and the whole payments are spending through this account. Hereby, the sale process is terminated and the prices are paid within this account.

Evacuation problems: Because of the factors which are; indefinite periods for the tenancy contracts, the eviction actions due to non-payments or late payments, the reason of the judicial system's time extensions begin aliens to suspect in order to purchase a real estate in Turkey.

To overcome this problem, rentals should be paid through the bank accounts like in the abroad practices and there must be an amendment which regulates the "Evacuation Process." The amendment which regulates the process should includes that; if a tenant will not pay the rental in the period of time, lesser can take a letter from the relevant bank and can apply to the court through this letter. The court should analyse and ruled the evacuation decision, and the civilian authority should perform the court's decision expeditiously. If the amendment of law will be realised, the abovementioned problems will be solved.

Let's invest in Turkey, but what about taxes?

Tax is always an important item to consider for a new investment. But, of course, not the only issue to be considered for an investment decision. The Turkish tax system briefly explained below for real estate investors may provide a quick guide for foreign investors' consideration.



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Investment decisions for a foreign investor are always quite difficult. Lots of questions must be answered and lots of issues should be cleared: Where to invest? Which type of property to choose? When to invest? How much money should be considered? How to invest? And so on. Investors should also evaluate carefully the amount of taxes that will be paid.

In this article, I will give you a brief overview of taxes imposed according to the current legislation on real estate investments for both foreign corporate and individual investors.

FOREIGNERS CAN ACQUIRE REAL ESTATE IN TURKEY

Although there are several conditions need to be satisfied, foreigners can acquire property in Turkey.

- For real persons, reciprocity (i.e. only the nationals of a country where Turkish nationals may acquire real estate may acquire real estate in Turkey) and some other limitations such as size and location would apply. The reciprocity obstacle has already been solved by the government, and in principle there are no problems for foreign nationals to directly obtain real estate in Turkey. But, it is strongly suggested to consult an advisor for the procedures before making an investment decision.
- For foreign companies, on the other hand, it is not possible to purchase Turkish property directly. But, indirect investment is possible by establishing or acquiring Turkish

companies (100% foreign ownership of a Turkish company is possible) Also, a procedure is applied for property acquisition by foreign owned companies and again I would strongly suggest consulting a legal advisor.

TAXATION OF ANNUAL INCOME

For Corporate Investors: As mentioned above, for a corporate foreign investor, the only way to acquire property in Turkey is to establish a new Turkish company or acquire shares of an existing company in Turkey. That Turkish company (owned either wholly or partly by foreign investors and holding real estate) is subject to corporate tax at the rate of 20% of its annual profits. These profits can be derived from all types of income including rental income or capital gains that will be obtained in the case the property is sold. Profits after corporate tax (and upon setting aside legal reserves) can freely be distributed to the shareholders. Profit distributions to non-resident shareholders are subject to 15% corporate withholding tax. However, the withholding tax rate can be reduced to 10% and even 5% by virtue of Double Tax Treaties.

For Individual Investors: If a foreign individual investor buys Turkish property for his/her own use, there will be no additional tax burden since there will be no income derived from the property. But, if that individual obtains "rental income" from that property, or decides to sell that property and obtains "capital gain" the yearly rental income and the capital gains

will be subject to "income tax" at a rate between 15% and 35%.

OTHER TAXES RELATED TO REAL ESTATE TRANSACTIONS

Apart from corporate and income taxes, the main taxes related to real estate are transactional taxes such as Value Added Tax (VAT), Title Deed Charge, Stamp Tax (ST) and Property Tax (PT).

VALUE ADDED TAX

The buying and selling of real estate is subject to Turkish VAT at 18%. However, there are certain VAT exemptions. For instance, the sale of real estate by resident corporations that are not real estate traders and have held the property for a period of at least two years and the sale of real estate by individuals who are not dealing with real estate trading.

Also, apart from 18% rate, 1% and 8% VAT rates are also available for the sale of residential units having a net area less than 150 sqm. Since the VAT that will be paid during the acquisition of property will be a cost for an individual investor, the applicable VAT rate would be very important. So, in order to determine the applicable VAT rates for the above mentioned residential properties, I strongly suggest consulting a tax advisor.

The application of VAT rates for individual and corporate taxpayers is the same. But, while VAT paid at the time of acquisition would be a cost for individual investors as mentioned above, the VAT for corporate taxpayers will be offsetable against calculated VAT for rental and/or sales

income. For corporate taxpayers, should there be a difference between input (VAT rate at the time of acquisition) and output (VAT amounts, at the time of rent and/ or disposal) VAT rates a VAT refund would be possible.

TITLE DEED CHARGE

The acquisition of a legal title of a Turkish property is subject to a 2% title deed charge on whichever is higher between the property tax value or the transaction amount for both individual and corporate taxpayers. The same charge will apply when the property is sold. This charge is applied separately for the buyer and the seller. Thus, the total title deed charge burden over the property transaction at acquisition/ sale would be 4%.

STAMP TAX

Stamp tax is calculated over the sales price of the real estate property indicated in the asset purchase agreement (if any) at a rate of 0.948%, with a ceiling of TRY 1,487,397.70 for the year 2013. According to the current legislation each and every originally signed copy of an agreement is separately subject to stamp tax at the same rate. On the other hand, this stamp tax can be avoided if the sales agreement is concluded in front of the title deed registrar. Also, according to the current legislation, no stamp tax is applied for the agreements signed between two individuals.

PROPERTY TAX

Property tax is levied on the owner of real estate at 0.2% on buildings. If the buildings are used for residential

purposes it is reduced to 0.1%. In a few cases, i.e. retired citizens' domiciles, the tax rate is 0%. Property tax rate for land is 0.1%, whereas the rate for arable land is 0.3%.

Furthermore, the effective property tax rates are increased from 0.1% to 0.2% for residences and from 0.2% to 0.4% for other buildings that are within the borders of metropolitan areas.

WHERE TO START?

Tax is always an important item to consider for a new investment. But, of course, not the only issue to be considered for an investment decision. The Turkish tax system I briefly explained for real estate investors may provide a quick guide for foreign investors' consideration.

Please note that, although in principle there is no difference between local and foreign investors for the application of taxes in Turkey, foreign investors may benefit from the advantages of double tax treaties to reduce their Turkish tax burden especially on capital gains.

The starting point to understand the taxes to be applied would be to carry out a due diligence for tax and legal issues. As mentioned above, it may be possible to avoid stamp tax or avoid or reduce to VAT burden at the time of acquisition. Also, it would be possible to exit the Turkish market without a capital gains burden for an individual property owner or a foreign company shareholder.