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LIMITATION ON FINANCING EXPENSE DEDUCTIONS HAS BECOME EFFECTIVE

With the regulation made in Article 41 of the Personal Income Tax (PIT) Law and Article 11 of the Corporate Income Tax (CIT) Law by the Law No. 6322, the limitation on financing expense deductions, which was previously implemented and abolished on 01.01.2004 by the Law No. 5024, was re-established with some amendments.

Pursuant to the mentioned regulation, CIT taxpayer businesses whose utilized foreign liabilities exceed their equity, except for credit institutions, financial institutions, financial leasing, factoring and financing companies, are unable to **deduct the portion determined by the Council of Ministers (currently by the President)**, so as not to exceed 10% of the total of the expense and cost items related to the utilized foreign liabilities made under the title of interest, commission, delay interest, dividend, F/X differences, etc. as an expense in determining tax base.

Although the effective date of the mentioned Law article was 01.01.2013, since a decision was not taken within the scope of the authority granted in the relevant articles by the Council of Ministers and then by the President in the previous periods, the said regulation regarding the limitation on financing expense deductions did not become effective until 1.1.2021.

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With the Presidential Decree No. 3490 published in the Official Gazette dated 04.02.2021 and numbered 31358, the rate in the above-mentioned articles was determined as 10% to be applied to the earnings derived within taxation periods starting from 01.01.2021.

Accordingly, PIT taxpayer and CIT taxpayers (except for credit institutions, financial institutions, financial leasing, factoring and financing companies) whose utilized foreign liabilities exceed their equity are unable to deduct 10% of the total expense and cost items (except for items recorded within investment expenses) related to the utilized foreign liabilities made under the title of interest, commission, delay interest, dividend, F/X differences, etc. as an expense in determining the PIT and CIT bases for the taxation periods starting from 1.1.2021.

Although the regulation has entered into force as it stands, it is required to clarify the implementation details with the regulation to be made by the Tax Administration due to the uncertainty of the issues such as the following.

- What exactly should be understood from the concept of foreign liabilities utilized,
- Which date shall be considered for comparison,
- Whether the VAT corresponding to the financing expense limitation can be deducted if the financing expenses of the foreign liabilities utilized are subject to VAT.

It is expected that the Ministry of Treasury and Finance will make a regulation on the subject based on the authority obtained from the article.

Kind regards.