

Annual Tax Law Bulletin on Taxation of The Digital Economy

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1. Two Pillar Approach to Tax Problems Arising from the Digitization of the Economy

With the increasing digitalization of the economy, the Organization for Economic Cooperation and Development (“OECD”) and G20 began working on the Inclusive Framework on Base Erosion and Profit Shifting (“BEPS”) because the current international tax rules are not sufficient for the taxation of multinational enterprises (“MNEs”) and are not suitable for changed business models.

As a result of lengthy negotiations to revise international tax rules and adapt them to the digital economy, under the leadership of the OECD and G20, international taxation rules including the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy adopted by consensus among the 140 members of the Inclusive Framework on BEPS in October 2021. The aforementioned new system con-

sists of Pillar 1 and Pillar 2. The rules set in the context of Pillar 1 and Pillar 2, will lead to significant changes in current international taxation standards.

A) Pillar 1

Pillar 1 establishes a new international taxation ground for a more equitable distribution of profits and taxation rights of MNEs with global revenues exceeding EUR 20 billion and profitability exceeding 10%. In the context of Pillar 1, 25% of the residual profits of companies whose profitability exceeds 10% are distributed among the market countries by the revenue-based distribution key, and these profits are taxed in the relevant countries. The companies’ profits that meet certain conditions are reallocated to the countries where the sales take place, regardless of their physical presence in these



jurisdictions. Accordingly, the countries to which taxation rights are to be allocated will be entitled to levy tax on two sources of income classified as “Amount A” and “Amount B” from the MSEs falling within the scope of Pillar 1. Pillar 1 is estimated to result in a reallocation of profits of USD 125 billion globally.

In October 2023, the OECD published the Multilateral Agreement on the Application of Pillar 1 - Amount A. In a statement issued by the OECD on December 18, 2023, the OECD confirmed that it aims to (i) finalize the text of the Multilateral Agreement by reaching a consensual solution by the end of March 2024 and (ii) hold a signing ceremony by the end of June 2024. However, there has been no progress in finalizing the Multilateral Agreement text in 2024. The OECD stated that negotiations are still ongoing.

Another important component of Pillar 1 is Amount B. While Pillar 1 - Amount A updates the international taxation framework for MNEs, Pillar 1 - Amount B simplifies existing transfer pricing rules for all taxpayers and focuses on the application of transfer pricing rules to the core marketing and distribution activities of MNEs in the jurisdictions where they operate. In addition, Pillar 1 - Amount B aims to increase tax certainty and reduce administrative and compliance costs. The public consultation collected by the OECD for the Pillar 1 - B Amount between July 2023 and September 2023 was published on September 26, 2023. The OECD’s work on Pillar 1 - Amount B was completed by the end of 2023. In addition, the

Final Report published by the OECD on February 19, 2024 includes a significant update based on the application of Pillar B. This report provides guidance aimed to simplify and facilitate the application of the “the arm’s length principle in transfer pricing. In particular, this report, published as an annex to Chapter IV of the OECD Transfer Pricing Guidelines, provides detailed guidelines for effective implementation.

According to the OECD report published on February 19, 2024, countries may choose to apply the Amount B approach under Pillar 1 for fiscal years beginning on or after January 1, 2025. Countries are not obligated to apply the B Amount, but they may either require its application for taxpayers in their jurisdictions or leave it to taxpayers’ discretion.

This approach covers transactions related to core marketing and distribution activities and aims to simplify transfer pricing and reduce disputes based on the arm’s length principle.

B) Pillar 2

Pillar 2 introduces a global minimum corporate tax, which applies if the revenue of MNEs with an annual income exceeding 750 million euros is taxed at less than 15% in another country. In this case, the global minimum tax is applied to the income arising in each jurisdiction where they operate.

Within this scope, the country of the ultimate parent business of MNE will have the taxation right where the effective tax burden of the market country is below 15%.

The two key components of Pillar 2 are the Global Anti-Base Erosion Rules (“GloBE Rules”) and the Subject to Tax Rule (“STTR”). In addition, countries may also adopt the Qualified Domestic Minimum Top-up Tax (“QDMTT”) as part of the implementation of Pillar 2.

a. GloBE Rules

On December 20, 2021, the OECD published the “Global Anti-Base Erosion Model Rules (Pillar Two)” on the second step of the two-step approach approved under the OECD/G20 BEPS. The above-mentioned Model Rules include (i) the Income Inclusion Rule (IIR) and (ii) the Undertaxed Payment Rule (UTPR); these two rules are collectively referred to as the GloBE Rules.

The global minimum corporate income tax of 15% within the scope of GloBE rules is applied to MNEs that have annual revenue of EUR 750 million or more in the Consolidated Financial Statements of the Ultimate Parent Entity in at least two of the four Fiscal Years immediately preceding the tested Fiscal Year.

The GloBE Rules consist of two rules:

- (i) The Income Inclusion Rule (IIR) allows for additional tax to be collected by the jurisdiction of the ultimate parent of a company whose

income is taxed at a rate below the 15% minimum. This ensures that the effective tax rate is at least 15%. In this context, the IIR, the main mechanism for taxing “untaxed” profits, is primarily applied.

- (ii) The Undertaxed Payments Rule (UTPR) is the denial of deductions or an adjustment equivalent to under-taxation within the group company in cases where the effective tax rate is below the minimum rate of 15% by the jurisdiction where the company’s ultimate parent is located under the IIR. The UTPR is applied on a secondary basis in cases where the IIR rule cannot be fully applied. The UTPR is envisaged to be implemented by 2025.

Furthermore, in December 2022, the European Union (“EU”) adopted the EU Minimum Corporate Tax Directive (“EU Directive”). This EU Directive provides a mechanism for EU Member States to implement the Pillar 2 GloBE Rules. The EU Directive enters into force for EU Member States as of 01.01.2024.

On December 18, 2023, the OECD Secretariat published the third set of Administrative Guidelines to clarify the operation of the Pillar 2 GloBE rules, following the guidelines published in February and July 2023. Finally, the OECD published the fourth set of Administrative Guidelines in June 2024.

b. Subject to Tax Rule (STTR)

Besides the GloBE Rules, the other important component of Pillar 2 is the Subject to Tax Rule (STTR). The STTR, which is complementary to the GloBE Rules, is to be included in certain double taxation treaties with developing countries and allows the source country to recapture some of the taxation rights on intra-group payments of an MNE where the income is taxed at a rate lower than 9% in the resident country. In other words, the minimum tax rate for the STTR is set at 9% and where the nominal tax rate is less than 9%, the source country may also impose additional withholding tax on foreign payments between related parties.

Subject to Tax Rule Multilateral Instrument ("STTR MLI") has been prepared and the STTR MLI was opened for signature on October 2, 2023. In September 2024, STTR MLI was signed in Paris by Barbados, Belize, Benin, Cabo Verde, the Democratic Republic of Congo, Indonesia, Romania, San Marino and Türkiye. By 2025, the STTR MLI is expected to be signed by 10 countries.

c. Qualified Domestic Minimum Top-up Tax (QDMTT)

Another element included in the set of GloBE rules is the Qualified Domestic Minimum Top-up Tax (QDMTT). This domestic minimum tax aims to give countries priority to tax low-taxed profits earned in their jurisdiction. Jurisdictions may adopt the QDMTT to preserve source countries' right of first taxation. To the extent that a jurisdiction prefers

to apply the QDMTT, this tax is offset against the amount of tax payable in another jurisdiction under the GloBE rules. Thus, applying QDMTT under the GloBE preserves the primary taxation right for the country where the income is derived.

C) Developments in Türkiye

The bill on the ratification of the 'Multilateral Convention to Implement Tax Treaty-Related Measures to Prevent Base Erosion and Profit Shifting,' signed on behalf of Türkiye on June 7, 2017, was first submitted to the Presidency of the Grand National Assembly of Türkiye on June 2, 2020. However, the bill was deemed null and void as it was not finalized during the relevant legislative period. The bill was subsequently renewed and resubmitted to the Presidency of the Grand National Assembly of Türkiye.

The Multilateral Convention, prepared within the framework of the 15th action of the OECD's Base Erosion and Profit Shifting (BEPS) project titled 'Multilateral Instrument,' aims to incorporate BEPS measures into double taxation agreements that are either currently in force or have been signed but are still in the process of enforcement.

In addition, to ensure full compliance with International Financial Reporting Standards, the decision numbered 75935942-050.01.04 - (01/19078) dated September 13, 2023, and titled 'International Tax Reform-Pillar Two Model Rules-Amendments to TMS12,' issued by the Public Oversight, Accounting, and Auditing Standards Authority, was

published in the Official Gazette on September 19, 2023, with number 32314.

Law No. 7524, published in the Official Gazette dated 02.08.2024 and numbered 32620, introduced local and global minimum corporate tax provisions into the Turkish tax legislation to comply with the OECD Pillar 2 rules.

On August 2, 2024, Law No. 7524 entered into force, and within the framework of the additional articles added after Article 36 of the KVK, regulations regarding local and global minimum complementary corporate tax were introduced. These regulations apply to the ultimate parent enterprises of Multinational Enterprise (MNE) groups within the scope, generally residents of Türkiye. Türkiye's local and global minimum complementary corporate income tax provisions are designed to align broadly with OECD rules. These provisions may also affect branches and/or companies operating in Türkiye that are owned by foreign investors, potentially imposing additional tax and reporting obligations in Türkiye.

For covered entities in Türkiye, the Income Inclusion Rule and Qualified Domestic Minimum Top-up Tax will apply to income earned as of 01/01/2024, while the regulations on the Undertaxed Payment Rule will apply to income earned as of 01/01/2025.

Additionally, under Article 32/C added to the KVK, a domestic minimum corporate tax application has been introduced, stipulating that corporate taxpayers' cor-

porate tax payable cannot be less than 10% of the corporate profit before deductions and exemptions.

D) Digital Service Tax

The inability to produce a globally accepted solution for the taxation of the digital economy has led many countries, including the UK, France, Austria, Italy, Spain, and India, to implement the digital service tax regarding taxing various services offered in the digital environment. In this context, the "digital service tax" in Türkiye, which aims to tax the services provided in the digital environment, came into effect on March 1, 2020.

The same legislation also stipulated that if the obligations regarding the digital service tax were not fulfilled within the time limit, the relevant persons would be notified by all means of communication and this matter would be announced on the Turkish Tax Administration website. If these obligations were still not fulfilled within thirty days following the announcement, an access ban would be imposed on the service provided by the service providers within twenty-four hours until these obligations were fulfilled. With its decision dated 18.05.2023 and numbered E.2020/11, K.2023/98, the Turkish Constitutional Court unanimously annulled the provision providing for the sanction of access blocking because (i) the sanction was like an indefinite business closure penalty, (ii) the application of the sanction only for digital service taxpayers was contrary to the principle of equality, (iii) blocking access violated

the freedom of communication, and (iv) the restriction imposed on the freedom of undertaking was disproportionate and out of proportion.

In the statement made by the United States of America (“USA”) Trade Representative Office on June 2, 2020, it was stated that a competition investigation will be launched against some countries that apply digital services tax, including Türkiye.

On October 21, 2021, the USA, Austria, France, Italy, Spain, and the United Kingdom reached a consensus to adopt the existing Unilateral Measures (“Unilateral Measures Consensus”) regarding the implementation of Pillar I. The six mentioned countries signed the Unilateral Measures Consensus and a joint statement (the “21 October Joint Statement”) was published.

Accordingly, it was stated that the digital service taxes accrued in the period between January 1, 2022, and December 31, 2023 (in case the application enters into force earlier) -during the transition period- could be deducted from the corporate taxes calculated within the scope of Pillar I in the following years. It has been regulated that digital service tax payments above the said amount can be deducted from the corporate taxes to be paid in the following years by the companies included in the scope. In return, the USA reached an agreement to remove the additional customs duties that it had applied and suspended due to the trade investigation it initiated against the said countries, including the investigations that took place before 8 October.

In the announcement dated November 22, 2021, published by the Ministry of Treasury and Finance, it was stated that Türkiye and the United States agreed that the conditions applicable under the Unilateral Measures Consensus regarding the digital service tax would also be valid between Türkiye and the USA. As a result, Türkiye was included in the USA compromise with 5 countries implementing Digital Services Tax.

In July 2023, the OECD issued a statement in which the member states of the Inclusive Framework agreed to refrain from imposing a new digital services tax or similar unilateral imposition on any taxpayer between January 1, 2024, and December 31, 2024, or until a Multilateral Agreement is signed.

E) Recent Approach of USA

On Monday, January 20, U.S. President Donald Trump issued a presidential memorandum declaring that the OECD Pillar II Global Minimum Tax agreement has “no validity or effect” in the United States, effectively pulling America out of the agreement negotiated by the Biden administration with the OECD framework countries October 2021.

2. Withholding Tax in Digital Advertising Services

The withholding tax applied to the advertising services provided on the internet is another regulation introduced in Türkiye to tax digital companies.

With the Presidential Decree No. 476 published in the Official Gazette dated 19.12.2018 and numbered 30630, the online advertising services provided on the internet were included in the scope of tax withholding, and it is stipulated that payments made to the providers of such services or those who act as an intermediary for the provision of such services will be subject to tax withholding regardless of the recipients of the payments are taxpayers or not.

Accordingly, regarding the online advertising services provided on the internet, it has been regulated that the below withholding tax rates are applied to the above-mentioned payments depending on the service provider's status, as of 01.01.2019.

- 15% over the payments made within the scope of Article 94 of the Income Tax Law No. 193 (ITL) (payments made to natural persons, associations and foundations, and other persons or enterprises within the scope of Article 94),
- 0% over the payments made within the scope of Article 15 of the Corporate Tax Law No. 5520 ("CTL") (payments made to taxpayers subject to full tax liability),



- 15% over the payments made within the scope of Article 30 of CTL (payments to taxpayers subject to limited tax liability).

Nevertheless, because the aforementioned withholding tax is a tax on the commercial income of taxpayers subject to limited tax liability, and therefore constitutes a violation of the Prevention of Double Taxation Agreements concluded between the Republic of Türkiye and other relevant countries, lawsuits have been filed by taxpayers who paid these taxes, seeking to cancel and refund the taxes paid. Although these cases have been decided in favor of the taxpayers by the courts of first instance and courts of appeal, it is known that the cases are ongoing against the taxpayer due to the Council of State's stance that 'websites constitute a workplace.

3. Withholding Tax for Payments Realized through E-Commerce Platforms

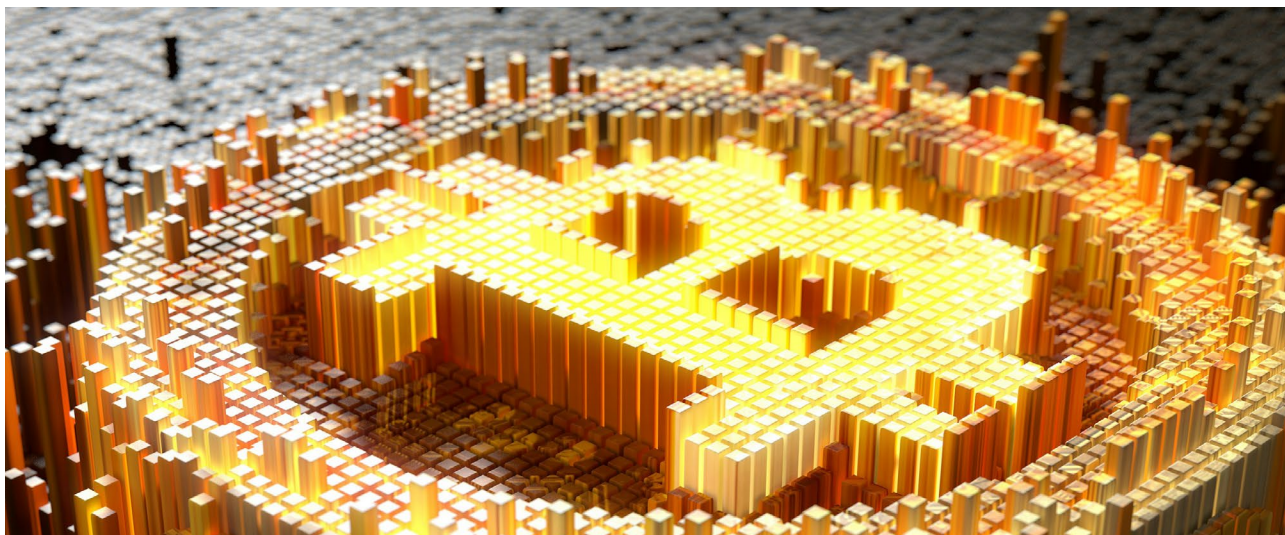
Through the regulation introduced by Law No. 7524, intermediary service providers and electronic commerce intermediary service providers have been liable to withhold tax on their payments to service providers and electronic commerce service providers due to their activities within the scope of Law No. 6563.

With the Presidential Decree No. 9286, the referred withholding tax rate is determined as 1%. The decision will be effective on January 1, 2025.

The essence of the mentioned regulation targets electronic commerce conducted through e-commerce platforms. Considering the offsetting opportunity granted later, it can be said that the withholding tax is envisaged as a tax security mechanism and provides an early collection opportunity for the administration. However, whether an effective tax burden arises on the seller depends on the seller's tax position (whether they are in profit or loss) and should be evaluated accordingly.



4. Taxation of Crypto Assets



Crypto assets appear as one of the applications of distributed ledger technologies that allow records to be kept in a distributed and decentralized manner. Considering the different application aims of crypto assets, it is seen that their legal characteristic is determined differently in different legal systems.

The Regulation on the Non-Use of Crypto Assets in Payments (the 'Regulation'), the first regulation in Türkiye regarding crypto assets, was published by the Central Bank of the Republic of Türkiye and entered into force on April 30, 2021. Under Article 3 of the Regulation, crypto assets are defined as intangible assets that are virtually created using distributed ledger technology or similar technology and distributed over digital networks, but cannot be considered money, electronic money, payment instruments, securities, or capital market instruments.

The Regulation in question is a limited piece of legislation, designed solely to determine the methods and tools to be

used for payments.' Additionally, it is noted that the same definition is provided in the Guide on 'Basic Principles Regarding the Obligations for the Prevention of Money Laundering and the Financing of Terrorism for Crypto Asset Service Providers,' published by the Financial Crimes Investigation Board.

In addition, the Istanbul 24th Enforcement Law Court provided another definition of crypto assets in its decision dated April 19, 2021, numbered E.2021/586, K.2021/675. In the decision, crypto assets are considered within the scope of commodities or securities and are accepted as a form of digital or virtual currency, meaning they could be subject to sequestration.

At present, there is no specific regulation in Turkish tax legislation regarding how income derived from crypto assets will be taxed, particularly for individuals who do not earn income from commercial activities.

Law No. 7518 on the Amendment of the Capital Markets Law, which entered into force on July 2, 2024, defined 'crypto asset.' In line with the Regulation and MASAK guidelines, a crypto asset is defined as 'intangible assets that can be created and stored electronically using distributed ledger technology or similar technology, distributed over digital networks, and capable of expressing value or rights.' The law also regulates crypto asset service providers, activities of crypto asset platforms, custody of crypto assets, and the requirement to obtain permission from the Capital Markets Board ('CMB').

If crypto assets are considered 'intangible assets' under tax legislation, this definition may be incorporated into Article 70 of the Income Tax Law No. 193 ('ITL'). In this case, the gains arising from the disposal of these assets could be taxed as capital gains by Article 80 of the ITL. However, there is currently no tax regulation in this regard.

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