

Constitutional Court decision on taxation of salary income

Turkey
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The Constitutional Court of Turkey has issued a Decision which repeals the highest income tax bracket applicable for the salary income.

Technical background

The income tax tariff included under Article 103 of Income Tax Code was amended with the Article 1 of Code No. 5479 to be effective as of 1.1.2006. Pursuant to this amendment, single tariff practice is introduced by accepting that salary income is of the same nature as the other income items. This is effected through the annulment of five-point discount practice in tax rates in the taxation of salary incomes. Single tariff practice is used instead of using two tax tariffs, separately applied in the taxation of salary and non-salary income. The number of income brackets within the tariff has been reduced from five to four and the amounts of these brackets have been increased.

When the former tax tariff, in which the disputed principle is included, and the new tariff are compared, it is seen that tax burden of the salary earners who are included under the scope of the first three brackets of the new tariff is lower than that of the former tariff. The tax burden of the salary earner included under the scope of the fourth bracket with 35% tax rate is higher than that of the former tariff. Besides, with the new tariff, the tax burden of salary earners has been increased whereas the burden of other income groups has been decreased.

With the arguments that income tax has been increased for middle and high income groups with the new tariff, therefore the principles of fair and equal distribution of tax burden and equality in taxation have been impaired, and equality in taxation can be achieved through applying same tax rates for those having same ability to pay and different tax rates for those having different ability to pay; based on these reasons, it is claimed that the related regulation is in conflict with the articles 2, 11 and 73 of the Turkey's Constitution.

According to the justifications explained above, with the Constitutional Court Decision dated 15 October 2009 promulgated in the Official Gazette dated 8 January 2010, the last income tax bracket with 35% tax rate has been canceled.

The Court Decision will come into effect 6 months later from 8 January 2010.

Detailed discussion

Effective date of Court Decision and arguments on the topic

The mentioned Decision of the Constitutional Court will come into effect 6 months later following its promulgation in the Official Gazette. Therefore, the Legislative Body needs to introduce a new regulation within 6 months regarding the annulled tax bracket.

As from 15 October 2009, salary income has been still subjected to current income tax rates since no new regulation has been introduced by the Legislative Body although, Constitutional Court canceled the last bracket of income tax tariff and put its objection for unfair taxation of different income groups.

At this point, a new discussion has started on whether based on the Constitutional Decision, income tax paid by salary income groups subjecting to last bracket of the income tax tariff for the periods starting from October 2009 can be paid with reservation clause and a court case can be initiated to refund the tax amount paid not in line with the Constitutional Court Decision.

When the justification of the related Decision of the Constitutional Court is reviewed, it is seen that it includes positive expressions on the lawsuits which have been already initiated and which are to be initiated until the Legislative Body introduces a new regulation, and we are of the opinion that the Decision of the Constitutional Court will have a positive effect on the Decisions of the judicial authorities.

Taxation methodology of salary income in Turkey

According to the Turkish Income Tax Code, salary income which is reimbursed by local companies should be subjected to income tax by the companies on behalf of the employees through the withholding mechanism. Income tax has to be calculated over the payroll and should be reported via monthly withholding tax return.

In case the total income of the employee consists of only salary income received from one employer (or the income derived from more than one employer by being subjected to withholding income tax but the total amount is below TRY 22.000) and subjected to income tax during the year, it is not subject to further declaration through the annual income tax return.

On the other hand, salary income received from non local companies or from more than one employer and not satisfying the conditions mentioned above shall be reported in Turkey via annual income tax return before the 25 March of the following year.

The income tax rates applicable for salary income derived in year 2009 are provided below.

Income Brackets (TRY)	Tax Rate (%)
0-8.700	15
8.700-22.000	20
22.000-50.000	27
50.000-	35

Actions to be taken by the employers and employees

Although, as noted earlier, any new legislative provisions will not have retroactive effect for year 2009 and the pertinent provision governing the current taxation rules has been repealed by the tax office (despite the fact that the repeal is not meant to take effect for some time still), it may be possible for individuals or local employers to report salary income taxes with a "reservation clause", which needs to be done in conjunction with a legal step in respect of the tax office.

For the salary income included in local payroll and subjected to income tax by the employer on behalf of the employee on a monthly basis, the company or the employee may go to Court to get back the income tax difference paid based on the last tax bracket. If the employer decided to go to Court, a court case should be filed within 30 days following the related month's withholding tax return filing date.

The employee can also apply to the Tax Office for the adjustment of the income tax paid during the year by the employer on behalf of him. The employee can apply to the Court if the Tax Office does not respond to him within a legal time period or does not respond to him in favor of the employee.

However, if the employee is liable to file annual income tax return, he should apply to the Court within 30 days following the annual income tax return filing date. To be able to initiate a Court Case, the tax return should be filed with "reservation clause".

If the local employer applied to the Court during the year, Turkish tax resident employees, whose income is consolidated in their tax returns, should be careful that the part of income tax paid by local employer and subjected to Court Case should be excluded from total income tax amount, which is reported by the employee through the annual income tax return.

Filing with "reservation clause" may provide individuals on assignment to Turkey subject to tax in Turkey with a tax refund. If taxpayers wish to pursue the approach outlined above, they are advised to consult a qualified tax professional.

For additional information or assistance, please contact your local Ernst & Young Human Capital team member or one of the tax professionals from Ernst & Young Turkey office.

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