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New Tax Treaty between Turkey and Germany

Turkey and Germany signed a new tax treaty on September 19, 2011. The new treaty will enter into force after completion of the legal procedures required under the local laws of each country (Turkey requires the approval of its Parliament and President). The new treaty is to be effective retroactively as of January 1, 2011. In the meantime, Germany has terminated the existing treaty as of January 1, 2011.

The new treaty generally follows the OECD Model Convention. Although not yet in force, some of the significant provisions of the new treaty are as follows:

Permanent establishment

The new treaty now explicitly provides that the furnishing of services, including consultancy services, through employees or other personnel employed by the company will give rise to a permanent establishment if activities of that nature continue (for the same or a connected project) within a contracting state for a period or periods aggregating to more than six months within any twelve-month period. The previous treaty had no comparable provision.

Dividends

The withholding rate for dividends paid to a 25% or more corporate shareholder has been reduced from 10% to 5%. The withholding rate remains at 15% for other shareholders.

Interest

The withholding rate on interest has been reduced from 15% to 10%.

Royalties

The withholding rate on royalties remains at 10%.

Collection of Withholding Taxes

The Treaty permits each source country to withhold applicable withholding taxes at the higher local country (non-tax treaty) withholding rates, which would thereby require recipients to file a refund claim with the tax authorities in the source country.

Capital Gains

Under the new treaty, capital gains are generally taxable only in the country of residence, provided the property (including shares) has been held for more than one year. The one year holding period requirement does not apply in the case of capital gains derived from the sale of shares listed on an approved stock exchange or in connection with a corporate reorganization. The new treaty contains a number of exceptions that permit the source country to tax capital gains attributable to (i) gains from the sale of immovable property (*e.g.*, real property); (ii) gains from the sale of shares where more than 50% of the share value is attributable to real property; and (iii) gains from the sale of movable property forming part of the business property of a permanent establishment or fixed base.

Independent Professional Service Income

The independent professional services article of the new treaty applies only to income earned by *individuals*. The old treaty provision also applied to companies. Under the new article, independent professional services income is generally taxable only in the individual's residence state, except that the income can also be taxed in the state where the services are performed if:

- a) the individual has a place of business regularly available to him in that other state for the purpose of performing those services or activities; or
- b) the individual is present in that other state for the purpose of performing those services or activities for a period or periods amounting in the aggregate to 183 days or more in any continuous period of twelve months.

The Protocol clarifies that payments for technical services, studies or surveys of a scientific, geological or technical nature or for engineering contracts, or for consultancy or supervisory services are covered by this article. In addition, a partner's share of income received by a partnership for performing services of a type covered by this article is covered by this article.

Other

The new treaty also contains the following additional significant provisions which were not contained in the old treaty:

The new treaty provides for the confidential exchange of information relating to taxes covered by the treaty between the tax administrations of both countries. The new treaty also provides that the tax authorities of each country shall provide assistance in collecting taxes. These provisions follow the latest OECD standard.

Our client alerts are for general informational purposes and should not be regarded as legal advice. If you would like additional information or have any questions, please contact:

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