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A NEW AUDIT MECHANISM: CALL FOR JUSTIFICATION



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Guidance that details how the Turkish tax authorities will determine whether to call a taxpayer to justify his declaration before initiating a tax audit have finally been released, almost year after this new mechanism was put in place.

Turkey introduced an audit mechanism into the Turkish Tax Procedure Code in late 2016, named the "Call for Justification". It allows Turkish tax authorities to conduct a preliminary examination to decide whether a tax audit should be initiated for a taxpayer.

However, a detailed guidance on how to implement these new audit rules has only been provided recently. On July 25 2017, a general communique to provide guidance and explain how to conduct the call for justification process was published in the Official Gazette.

What is the justification mechanism?

The justification mechanism allows the tax authority to invite a taxpayer, who has a potential to make a tax loss based on a preliminary determination, to justify their tax returns. By means of this mechanism, either taxpayers are not audited if no loss of tax is determined or taxpayers are allowed to benefit from reduced tax penalties in case a loss of tax by the respected taxpayer is confirmed.

Hallmarks to call for justification

The General Communique issued by the tax authorities indicates 16 different hallmarks to call taxpayers to justify their tax position. Some of these hallmarks include:

- No withholding tax application on the dividends allocated;
- Misapplication of previous year's losses;
- Thin capitalisation implementation;
- No interest application for the receivables from the shareholders; and
- Underreporting of real estate purchase and sales prices.

Who has authority to call a taxpayer to justify?

Under the new legislation, the tax audit board and evaluation committee at the Turkish Revenue Administration have an authority to invite a taxpayer to justify their tax position. Also, it is envisaged that evaluation committees will be established at the tax audit board and local tax offices. These committees will consist of three members.

Conditions to call a taxpayer for justification

Calling a taxpayer to justify his tax position is applicable provided that the following conditions are met:

- A preliminary determination has been made by those who authorised to conduct a tax audit or/and to collect information from taxpayers and other individuals and corporates engaging transactions with taxpayers;
- No tax audit or no dispatching to tax valuation committee has been initiated for the taxpayer; and
- No denouncement has been made about the taxpayer.

How can taxpayers will justify their tax position?

To benefit from this mechanism, a taxpayer must explain his tax position to the respected committee within 15 days after receiving the invitation letter.

The explanation can be carried out either orally or in writing. For oral explanations, the taxpayer and the committee mutually take statements down through minutes of the meeting. Written statements may be delivered by postal service or courier to the committee.

The outcome of the statements

If the committee concludes that the taxpayer's explanations justify his tax position, then the committee can decide not to initiate a tax audit on the taxpayer. In case the taxpayer admits that his tax position reasoned a loss of tax, he may benefit from the reduced tax penalty (20% of tax



loss) under the condition that he files additional declarations, pays the loss of tax and late payments interest in 15 days.

Similarly, even though the committee does not accept the taxpayer's justification he may benefit from 20% reduced tax penalty provided that the above-mentioned conditions are met. Finally, if the taxpayer does not file his tax return in 15 days, the committee will decide to initiate a tax audit.

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