REAL ESTATE INVESTMENT TRUSTS (REIT)

APPLICATIONS IN TURKEY

1 General introduction / history / REIT type

<table>
<thead>
<tr>
<th>REIT</th>
<th>Enacted year</th>
<th>Citation</th>
<th>REIT type</th>
<th>REIT market</th>
</tr>
</thead>
</table>
| REIT | 1995         | - Capital Markets Law  
- Communiqué on Principles Regarding Real Estate Investment Companies, Serial VI No. 11- | Corporate type National Stock Exchange Commission | 11 REITs quoted on the Istanbul Stock Exchange |

A REIT (Real Estate Investment Company) regime exists in Turkey primarily under the administrative supervision of the CMB (Capital Markets Board), a regulatory and supervisory agency.

The REIT practices in Turkey started in 1995. REIT shares have been traded on the Istanbul Stock Exchange since 1997. Due to the rapid increase in the population and to internal migration, housing demands have expanded in direct proportion to real estate investment. Along with the new regulations regarding mortgage loans introduced in 2007, it is expected that the demand for real estate will increase. These developments will have a positive effect on the future of REITs.

The REIT regime is regulated in Capital Markets Law and in the related Communiqué. The regulations took place initially with the modification in the Capital Markets Law which confirms the scope of actions of REITs in 1992. After the amendment in Capital Markets Law, the detailed arrangement of REITs was made in the Communiqué on Principles Regarding Real Estate Investment Companies, Serial VI No. 11 in 1995. Furthermore in respect to tax treatment to the REITs, various provisions are presented in Corporate Income Tax Code and Income Tax Code.

Currently, there are 13 REITs registered with the Capital Markets Board and with shares quoted on the Istanbul Stock Exchange.

2 Requirements

2.1 Formalities / procedure

Key requirements

- Regulated and closely monitored by the Capital Markets Board (CMB)  
- Statutes must be in accordance with the law and the procedures of the Communiqué  
- Founders must have no records of legal prosecution due to bankruptcy or other offences  
- The statutory auditors of the company must be Turkish citizens

A REIT can be established immediately. Furthermore, existing companies can convert to REIT status by simply amending their Statutes in accordance with the legal procedures of the Communiqué. A REIT can
be established for a limited time to undertake a certain project, for a limited or unlimited time to invest in certain areas and for a limited or unlimited time without any limitation or purpose.

The CMB’s pre-conditions required for an REIT to obtain permission for establishment are as follows:

- REITs should be established in the form of a joint stock company under the registered capital system. The board of directors may increase the share capital of the company by issuing new shares up to the amount of registered capital stated in the statute. Compliance with the provisions of the Turkish Commercial Code concerning capital increases is not mandatory;
- the initial capital may not be less than the specific amount determined by the Board (currently 7,200,000 TRY),
- 100 percent of the share capital must be fully paid;
- the commercial title is to include the phrase “Real Estate Investment Company”;  
- the statute must be in compliance with the provisions of the law and the regulations of the CMB;
- the founders must be certified of never having been subject to legal prosecution due to bankruptcy or other offences.

The investment companies are classified according to asset types, valuation principles, portfolio restrictions, management principles, profit distribution principles, depository procedures and obligation principles in the event of their liquidation. All of the above shall be determined by the CMB.

The members of the board of directors and the auditing board are elected and serve in accordance with the related articles of the Turkish Commercial Code. However, at least 1/3 of the members appointed to the Board must be independent as defined in the Turkish Commercial Code.

In accordance with Article 347 of the Turkish Commercial Code, the statutory auditor of the company should be a Turkish citizen. If there is an auditing board, at least one more than half of the auditing board members must be Turkish citizens. Besides this, there should be an independent audit firm to be assigned by the General Assembly in order to audit the financials of the company on pre-determined intervals.

REITs are required to prepare portfolio tables displaying the cost of the assets and rights along with their market values. Additionally, a board of directors’ report must be prepared every three months. These statements are to be submitted to the Capital Markets Board.

### 2.2 Legal form / minimum share capital

<table>
<thead>
<tr>
<th>Legal form</th>
<th>Minimum share capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Joint stock company</td>
<td>TRY 7.2 million</td>
</tr>
</tbody>
</table>

**Legal form**

The REIT must be a joint stock company. The general guidelines of joint stock companies are regulated with the Turkish Commercial Code. REIT specifics shall be determined by the Capital Market Laws and the Communiqué. The company’s name must include “real estate investment company”.

**Share capital**

The required minimum share capital for a REIT is 7,200,000 TRY (about EUR 4 million). The CMB has the authority to redefine the minimum capital requirement on a yearly basis. If the initial capital is less than TRY 50,000,000, 10% of the shares representing the initial capital must be issued for cash. If the
initial capital exceeds TRY 50,000,000, the shares that represent the TRY 50,000,000 of initial capital must be issued for cash.

The REIT may issue shares in registered or bearer forms. However, the shares representing capital in kind should be in registered form and an appraisal report should be drawn by an expert in accordance with the Commercial Code. The capital amount is to be in accordance with this report. Although the Turkish Commercial Code restricts the transfer of capital in kind shares for 2 years, REIT shares in connection with capital in kind can be freely transferred without any time limitation.

Companies shall not issue any privileged securities or real estate certificates other than shares. The nomination of candidates for Board of Directors membership is permitted. After the initial public offering, no privileges can be created (including the Board of Directors membership nominations).

### 2.3 Shareholder requirements / listing requirements

<table>
<thead>
<tr>
<th>Shareholder requirements</th>
<th>Listing mandatory</th>
</tr>
</thead>
<tbody>
<tr>
<td>Only for company founders</td>
<td>Yes</td>
</tr>
</tbody>
</table>

**Shareholder requirements**
The Communiqué and related Capital Market Laws state certain conditions for only company founders. The conditions are as follows;

- the founder shareholders may not have any payable taxes or insurance premium debt;
- there may not be any history of bankruptcy or other debt announcements against the natural person shareholders or their unlimited partner institutions;
- the founder shareholders may not be sentenced for illegal offences such as theft, fraudulent act, forgery, and etc;
- natural and legal person founders must have the sufficient financial capacity, a good reputation, and the experience required by their status;
- they should not be forbidden for operations in the meaning of Capital Market Law (this provision is valid for establishment and share transfers).

**Listing requirements**
The main objective of the CMB is to establish a consistent and far-reaching Turkish Capital Market. Thus, the listing requirement is domestic listing. Although the wording of the Communiqué and the Law does not provide a clear statement concerning the matter, the intention of the Legislation strengthens the view that the company should be domestically listed.

The REIT must apply to the CMB to register shares, which must equal at least 49% of the REIT’s issued capital. The REIT must also complete the public offering application form. The format and the procedures of this form are to be determined by the CMB. The form is to be completed with the trade registry as follows:

- if the REIT’s paid in capital is less than 50 million TRY, the form is to be completed within one year following the registration of the REIT’s articles of association;
- if the REIT’s paid in capital is greater than 50 million TRY but less than 100 million TRY, the form is to be completed within five years following the registration of the articles of association;
- if the REIT’s paid in capital is equal to or greater than 100 million TRY, the form is to be completed within five years following the registration of the articles of association.
The CMB has the authority to reassess these amounts in accordance with the Communiqué. It is possible for companies to offer their shares equal to at least 49% of their issued capital by performing one or more public offering within the specified time periods. The companies that do not complete the public offering application forms within the specified time periods or whose applications were found inappropriate (due to failure to fulfill the necessary conditions), shall lose the right to operate as REITs. Such companies are obliged to amend the provisions of their articles of association to exclude real estate investment activities. Within three months after disqualification, the companies must also approach to the Board to deregister. According to the provisions of the Turkish Commercial Code, companies which do not fulfill the requirements for amending the activities and/or approach to the Board to deregister will be regarded as dissolved.

2.4 Asset level / activity test

<table>
<thead>
<tr>
<th>Restrictions on activities / investments</th>
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</thead>
<tbody>
<tr>
<td>- Only transactions permitted by the Communiqué are allowed</td>
</tr>
<tr>
<td>- Must primarily deal with portfolio management</td>
</tr>
<tr>
<td>- 75% of the assets must consist of assets mentioned in their titles and/or articles of association</td>
</tr>
<tr>
<td>- Cannot be involved in the construction of real estate</td>
</tr>
<tr>
<td>- Cannot commercially operate any hotel, hospital, shopping center, etc.</td>
</tr>
<tr>
<td>- Cannot provide services by its personal to individuals or institutions</td>
</tr>
</tbody>
</table>

A REIT must deal primarily with portfolio management. In accordance with the Communiqué, the REIT’s portfolio is required to be diversified based on industry, region and real estate and is to be managed with a long-term investment purpose. 75% of the portfolios of the companies, established with the purpose of operating in certain areas or investing in certain projects, must consist of assets mentioned in their titles and/or articles of association. A REIT must invest at least 50% of its portfolio value in real estate, rights to real estate and real estate projects. At most, 10% of its portfolio value may be invested in time deposits or demand deposits. Investments in foreign real estate and capital market instruments regarding may only constitute no more than 49% of REIT’s portfolio value. The land and lots in the portfolio of the REIT, on which any project has not been realized for five years as of the acquisition date, may not exceed 10% of its portfolio value.

According to the Communiqué, REITs;

- cannot engage in a deposit business or conduct business and operations resulting in deposit collection as defined by Turkish Banking Laws
- cannot engage in commercial, industrial or agricultural activities other than the transactions permitted by the Communiqué,
- cannot engage in capital market activities other than its own portfolio management, limited to the investment areas permitted by the Communiqué,
- cannot in any way be involved in the construction of real estate and can not recruit personnel and equipment for this purpose.
- cannot commercially operate any hotel, hospital, shopping center, business center, commercial parks, commercial warehouses, residential sites, supermarkets, and similar types of real estate and employ any personnel for this purpose. However, if any real estate exits in the portfolio for the purpose of generating rental revenue, companies can provide the security, cleaning, general management and similar services to tenants for such real estates or independent parts thereof or can execute contracts with any operating firm for performance of these services.
- cannot provide services by its personnel to individuals and institutions for project development, project control, financial feasibility and follow-ups of legal permission (except for the projects related to the portfolio or will be related to the portfolio).
REITs can only participate in operator companies, other real estate investment companies, companies established within the context of the Build-Operate-Transfer model, companies established abroad, or companies in the operational field of real estates. The purpose of such participation would be to include certain real estate or rights to real estate as well as certain Turkish companies in the REIT’s portfolio. However, the expertise acquisition date value of the real estate to be included in the portfolio must equal at least 75% of the value of Turkish balance sheet assets. However, the value of REIT participation in the operating companies may not exceed 10% of the REIT’s portfolio value (as specified by the most recent quarterly portfolio table draw up disclosed to the public at the end of the accounting period).

A REIT cannot on his own in any way carry out the construction of real estates and cannot recruit personnel and equipment with this purpose.

2.5 Leverage

<table>
<thead>
<tr>
<th>Leverage</th>
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<tbody>
<tr>
<td>Short-term credits limited to three times the net asset value</td>
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</tbody>
</table>

In order to meet the short-term fund demands or costs related to the portfolio, an REIT can obtain credits at a rate of three times the net asset value (as described in the quarterly portfolio table). In order to calculate the maximum limit of such credits, the obligations of the company arising from financial leasing transactions and non-cash credits shall be taken into account.

A REIT can issue debt instruments within the restrictions of the capital market legislation. As for the issued debt securities, the aforementioned credits shall be deducted from the issue limit calculated according to the capital market legislation.

Companies can issue asset-backed securities based sales contracts on or on the promises to sell real estates from the portfolio.

2.6 Profit distribution obligations

<table>
<thead>
<tr>
<th>Operative income</th>
<th>Capital gains</th>
<th>Timing</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Minimum 20% as first dividend ratio</td>
<td>Will be regarded within the distributable profit</td>
<td>Annually</td>
</tr>
<tr>
<td>- Articles of association indicate the dividend ratio</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Operative income
According to the Communiqué specifications regarding dividend distributions by publicly held joint stock corporations, it is required that the articles of association indicate the dividend ratio.

The first dividend ratio cannot be less than 20% of the remaining distributable profit (the profit leftover after the necessary deductions of legal, tax, fund and financial payments, as well as prior year loss deductions, are made). The dividend distribution may not exceed half of the amount remaining after subtracting the reserves required to be set aside according to law and the articles of association as well as funds designated for taxes.

Dividend distributions shall be completed by the companies by the end of the fifth month following the end of their accounting periods. Under normal conditions, the general assembly may decide to distribute the yearly income of the company to its shareholders in the form of advance dividends prior to the year-
end closing. However, the Capital Markets Law has a specific provision for the listed companies which, under certain conditions, enables them to distribute dividends prior to the year’s end.

**Capital gains**

Capital gains from the disposal of shares or real estate fall under the income of REIT. For this reason, the profit generated from such operations will be included in the income and will be regarded within the distributable profit. Furthermore, all of the income from such operations is exempt from corporate tax at REIT level.

### 2.7. Sanctions

<table>
<thead>
<tr>
<th>Penalties / loss of status rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Modification of the articles of association to exclude real estate investment trust operations</td>
</tr>
<tr>
<td>- Possible company liquidation</td>
</tr>
</tbody>
</table>

There are no specific provisions within the legislation. However, it may be considered that the exemptions provided to REITs will be lost by the loss of the REIT status. Each case has to be examined on its own.

If companies can not meet the requirements of investing in real estate, the rights supported by real estate and real estate projects in the ratio of at least 50% of their portfolio value, they should apply to the CMB. After making an evaluation, the Board may provide a single extension period of one year. However, if companies still fail to achieve this minimum 50% ratio at the end of this extension period, they are required to apply to the Board in order to modify their articles of association to exclude real estate investment trust operations. If companies do not fulfill these changes, they shall be regarded as dissolved in accordance with the Turkish Commercial Code. The specific REIT exemptions will no longer be applicable. To determine whether REIT exemptions will apply to the period before the loss of status, the specifics of each case will be considered.

In case the REIT dividend distributions are incomplete according to the legal procedure, the CMB can enforce the REIT to distribute the shortfall amount to the shareholders in cash, along with interest which would be calculated using the Turkish Central Bank’s short-term advance interest rate. If legal requirements are met, the right is reserved to pursue legal actions against the REIT’s members of the Board of Directors for the incomplete distribution of dividends.

### 3 Tax treatment at the level of REIT

#### 3.1 Corporate tax

<table>
<thead>
<tr>
<th>Current income</th>
<th>Capital gains</th>
<th>Withholding tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax-exempt</td>
<td>Tax-exempt</td>
<td>Credit/refund may be possible</td>
</tr>
</tbody>
</table>

**Current income**

REITs established in Turkey are exempt from the general applicable 20% corporate income tax for all of their income. The exemption is applied to all of REITs income without disparity. There may also be income subject to a withholding tax.

**Capital gains**

Capital gains are, in principle, deemed the commercial income of an REIT and are thus regarded as corporate tax-exempt.
Withholding tax
REITs may have income subject to withholding taxes to be taxed at source. Credit/refund may be possible.

Other taxes
The tax exemption applies to corporate income tax only.

Accounting rules
Since REITs should be listed on the Turkish Stock Exchange, the accounting rules designated by the Capital Markets Board and the Turkish Board of Accounting Standards are applicable to REITs. In principle, income recognition for tax purposes is on accrual basis.

3.2 Transition regulations

<table>
<thead>
<tr>
<th>Conversion into REIT status</th>
</tr>
</thead>
<tbody>
<tr>
<td>In principle, no tax privilege</td>
</tr>
</tbody>
</table>

There is no privileged exit taxation rule for capital gains realized on real estate if sold to a REIT. However, there is a specific limited exemption rule stipulated in the Corporate Income Tax Code and applicable only for resident companies. According to this rule, under some certain conditions, 75% of the gains derived from the disposal of real estate may be exempted from corporate taxes. This is not a special rule for real estate disposals to REITs. However according to Corporate Tax Code the earnings that a company, which is engaged in the trading of real estate property or their rental, obtained from the sale of such assets, are not eligible to the exception.

3.3 Registration duties

<table>
<thead>
<tr>
<th>Registration duties</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Title deed fee of 3%</td>
</tr>
<tr>
<td>- Stamp duty of 0.75%</td>
</tr>
<tr>
<td>- Transfer may be subject to VAT</td>
</tr>
</tbody>
</table>

Real estate disposal is subject to a Title Deed Fee of 3%. Both the seller and the buyer are obliged to pay this fee equally (50% - 50%) before the disposal can be made at the Title Deed Office. This fee is calculated over actual consideration to be paid for such real estate; however the consideration shall not be less than the tax value of such real estate. Real estate transfer could also be subject to VAT.

Additionally, specific sales agreements (if any) will be subject to 0.75% stamp duty if an amount is stated on the agreement.
4 Tax treatment at the shareholder’s level
4.1 Domestic shareholder

<table>
<thead>
<tr>
<th></th>
<th>Corporate shareholder</th>
<th>Individual shareholder</th>
<th>Withholding tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends and capital gains from share disposal subject to standard corporate income tax rate (20%)</td>
<td>- 50% of dividend subject to individual income tax (15% to 35%)</td>
<td>General view: N/A</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Capital gains in principle tax exempt</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Corporate shareholder**
Dividends from a REIT are subject to taxation at the level of the corporate shareholder at standard corporate income tax rate (20%).

Capital gains from REIT share disposal by fully taxable companies are subject to a corporate tax of 20%.

**Individual shareholder**
Dividends distributed to resident individuals are subject to taxation at individual income tax of up to 35%. Tax rate applied on income obtained from dividends varies from 15% to 35% according to the income level (progressive tax). 50% of the income is exempted from the income tax.

Capital gains from REIT share disposal by fully taxable individuals are not subject to a withholding tax, nor must be declared, if held for more than two years.

**Withholding tax**
In principle the income generated by REIT is exempted from corporate tax and exempted income would be subject to corporate withholding tax, which in return replaces the dividend distribution withholding tax. Specifically for REIT the corporate withholding tax rate as well as the dividend distribution withholding tax is 0%. Although there were opposing opinions in the previous application, the new Corporate Tax Code and the Communiqué related thereto affirms the general view that withholding tax for REIT is 0%.

4.2 Foreign shareholder

<table>
<thead>
<tr>
<th></th>
<th>Corporate shareholder</th>
<th>Individual shareholder</th>
<th>Withholding tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>0% withholding tax</td>
<td>0% withholding tax</td>
<td>0% withholding tax</td>
<td></td>
</tr>
</tbody>
</table>

**Corporate shareholder**
See above explanations for domestic shareholder.

**Individual shareholder**
See above explanations for domestic shareholder.

**Withholding tax**
See above explanations for domestic shareholder.
5 Tax treatment of foreign REIT and its domestic shareholder

<table>
<thead>
<tr>
<th>Foreign REIT</th>
<th>Corporate shareholder</th>
<th>Individual shareholder</th>
</tr>
</thead>
<tbody>
<tr>
<td>No tax privilege</td>
<td>No tax privilege</td>
<td>No tax privilege</td>
</tr>
</tbody>
</table>

**Foreign REITs**
As a general rule, non-resident corporations deriving rental income in Turkey will be subject to a 20% withholding tax.

**Corporate shareholder / Individual shareholder**
In general distributions are subject to taxation in Turkey, but credit of foreign levied withholding tax may be possible. However the Controlled Foreign Company Regime should be taken into account.

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