The entry strategy and key issues to consider when establishing operations in Turkey (Part Two)

Any market entry strategy should begin with a thorough understanding of the costs and benefits of doing business in Turkey

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Foreign investment has been considered as an important driving force of stable economic growth in the last few decades in Turkey. Especially in the last ten years, we have seen a considerable increase in the foreign investment in Turkey through large or medium sized M&A deals, joint ventures of Turkish and foreign investors and start-up foreign investments in all sizes and in various sectors. Although total foreign direct investment inflows to Turkey prior to 2003 were just $15 billion, between 2003 and 2013 it reached $124 billion and, by increasing 28 percent as compared with the same period of 2013, according to the Central Bank of the Republic of Turkey, Turkey attracted $6.8 billion worth of foreign direct investments in the first half of 2014. Especially the year 2012 was excessively active in terms of investments in Turkey with the legislative changes and new foreign investment incentive scheme launched by the government of Turkey.

The new foreign investment incentive scheme is vital for Turkey's 2023 vision and national development strategy, which foresees Turkey becoming one of the top ten world economies by the year 2023. It is foreseen that this aim will be achieved with financial and technical support from foreign investors and companies, as well as domestic investors and companies; therefore the government has taken numerous steps to make the business environment as attractive as possible.

The new investment incentive scheme provides different advantages depending on the region where the investment is made by creating six distinct quadrants and by enhancing investment incentives in underdeveloped regions that face challenges such as high unemployment. The sectors to be supported in each region are determined in accordance with regional potential and the scale of the local economy, while the intensity of support varies depending on the level of development in the region. Through this scheme the investors have started to direct their focus on and, as business develops, open subsidiaries and make further investments in the regions and cities other than big metropolitans such as Istanbul, Ankara, Bursa and Izmir.

Many incentives such as exemption from corporate tax, VAT and social security premiums in different rates depending on the region have recently come into force. The rates are even higher in the organized industrial zones which provide infrastructure and also in other social facilities, in order to promote establishment and development of industry. Additionally, special tax rules apply to private equity companies regulated by the Capital Markets Board. To this end, such companies may be exempt from corporation tax and the dividend distributions of those companies, whether they are distributed or not, may be subject to 0 percent withholding tax.

Furthermore, long awaited new Turkish Commercial Code numbered 6102 (the TCC) and the new Turkish Code of Obligations numbered 6098 (the TCO) entered into force and replaced their outdated predecessors in 2012 with the aim to modernize the Turkish commercial landscape. For instance, many changes have been introduced in relation to corporate governance including single shareholding in joint stock companies and limited liability companies, one member boards, online board meetings and transparency provisions.

Since in general (excluding certain exceptions) there are no rules requiring Turkish participation in the capital or management of a company with foreign capital, a company may be established with 100 percent foreign capital and foreign investors are free to invest directly in Turkey, while being subject to equal treatment with domestic investors. Accordingly, the changes and incentives set out above are also being applied to their investment structures and thereby allow more flexibility if the investment structure is planned correctly.

The new incentive scheme and the legislative amendments have made the relevant laws closer to the European and American legislation, and by providing them the opportunity to operate in a more familiar legal environment, have provided comfort to the fund providers coming from the U.S. jurisdictions — as well as other foreign jurisdictions. Also, Turkey's slow but continued movement toward membership in the European Union has created momentum to adopt European business regulations and standards in Turkey, therefore making it easier to conduct business in this market. Similarly, Turkey's emerging economy, massive market size, competitive and skilled labor force, favorable geographical position, growing consumer middle class, solid banking sector, and the dynamism of its entrepreneurial class have made Turkey an attractive and growing market for the U.S. exporters. So far, over 1,000 American firms, across all industry sectors, have preferred Turkey to establish their operations and thereby to access business opportunities throughout Europe, Central Asia, the Caucasus, the Middle East and even Africa.

In addition to its advantages, one must recognize that Turkish market may also be complex and challenging from time to time. As to the challenges of investing in Turkey; depending on the sector to be operated in, there might be some special sector-related rules to be applied to the foreign investors as well as the local investors. For instance, certain M&A transactions in the energy sector are subject to approval of the Energy Market Regulatory Authority or certain transactions in terms of insurance institutions are subject to approval of the Treasury. Thus, establishing operations in the regulated sectors such as energy, insurance, banking and technology, media and telecommunications may be subject to certain licenses, approvals or permits granted by administrative authorities. Apart from these sector-specific administration processes, the administration process in relation to basic investment is quite straightforward in terms of legislative framework. However, for developed investments which require extensive construction, there are various permits to be obtained and there may be administrative hurdles to overcome which arise from the approach and unresponsiveness of the administrative bodies. Also, there are certain specific issues relating to the work and residence permits of foreign employees which must be taken into consideration by the foreign investors who wish to employ foreign employees in Turkey.

In light of these points, while there are many significant opportunities in Turkey for foreign investors — including U.S. corporations — there are also obstacles impeding entrance into the market. Any market entry strategy should begin with a thorough understanding of the costs and benefits of doing business in Turkey. One of the most successful and efficient ways to access the market quickly is to work with an experienced local partner. This partner could be in the form of a local representative, liaison office, agent or distributor who can provide knowledge of the local regulatory framework, language assistance and valuable business contacts. Considering the fact that Turkey's economic landscape will be a very different place in the upcoming years with its rapidly growing economy and skilled labor force, doing business in Turkey — with its many and varied opportunities — should be regarded as highly rewarding for those who are well prepared and operate with an informed knowledge of the market.

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