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A RESEARCH STUDY

ON

**THE TAX SYSTEM OF
TURKISH REPUBLIC OF NORTHERN CYPRUS
AND
SOUTH CYPRUS**

By

HÜSEYİN ÖZÜN YAMAÇ

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PREFACE

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I. INTRODUCTION

Taxes are without any doubt one of the most important elements of today's economic life. All individuals are under the obligation of paying taxes in accordance with the specific economic conditions of their country and in accordance with their own financial strength.

In the past the two communities on the Island of Cyprus sustained their existence as two separate entities in union. Within this framework, the Island was ruled under British colonial laws during the British Colonial era. The application of these Laws brought about financial obligations. As a result of the Turkish Peace Operation in 1974, the Island was divided into two parts, namely North and South Cyprus, with the Greek Cypriot community living in the South and the Turkish Cypriot community living in the North. With the proclamation of the Turkish Republic of Northern Cyprus in 1983, a new state was created in the North with its own constitution and laws having its own ways.

However, the existing British Colonial laws continued to remain in use. But the tax laws and tax rates underwent changes in order to adopt them to the highly inflationary Turkish Lira. Which is in use as a legal tender as a result of the almost role financial links of the TRNC with Turkey.

There are 13 different Tax Laws in the TRNC at present, containing a series of rules and regulations and natifications. The Island situation of the country recessitates imports and a high degree of foreign contacts. Like all Island economies an import services sector is vital for economic survival. Apart from that, due is geographical and political reasons the TRNC is highly integrated with the economy of Turkey.

This economic dependence on Turkey is an important factor in increasing the tax revenues of the TRNC in accordance with the economic development of Turkey and its economic ties with the TRNC.

In the TRNC taxes are collected by the state in proportion to incomes which undergo a systematic calculation. In the following chapters we shall be dealing with the question of how taxes are applied in the TRNC, the economy of South Cyprus and application of taxes there and a comparison between the two systems will be made based upon concrete questions.

II. THE PLACE CYPRUS IN THE WORLD

Cyprus is the only Island in the Eastern Mediterranean, with Turkey to its North and Israel and the other Arab countries i.e. Syria, Lebanon, Egypt is its East. From early times Cyprus has been a point of attraction both as a maritime centre for trade and due to its strategic location at the crossroads of three continents Europe, Asia and Africa.

Due to this, the Island has always been a scene of conflict which has always attracted the attention of all powers both surrounding it and the world powers.

Cyprus covers a total area of 9282 sq.km. in the South the Trodos Mountains and in the North the Kyrenia Range with the Mesoric Plain in the middle. The Western Coastal Plain of the TRNC is very fertile with alluvial soils, whereby in the eastern part of the Meserya plain only dry farming is possible, i.e. mainly wheat and barley. The climate is hot and dry in summer and temperate in winter.

The TRNC with its 3355 sq.km. of area, comprising the totality Kyrenia Range in the North and almost the totality of the Meserya Plain,

with irrigation in the west and dry farming in the East, North Cyprus thus complies to the general characteristics of the whole of the Island.

An analysis of the history of Cyprus helps us to understand the present situation of the Island. Because Cyprus contained huge reserves of copper mines, it maintained a powerful trading relationship with Syria, Egypt and the Eastern Mediterranean. The name of Cyprus comes from "copper" which in an Akkadian Language was "cypr". The following table shows clearly the chronogy of the history of Cyprus.

Table (1) Cyprus chronological history

2.1- The Economy of the

Stone Age:

Neolithic I.....	7000 - 6000 BC
Neolithic II.....	4500 - 3900 BC
Chalcolithic.....	3900 - 2600 BC

Bronze Age:

Early Bronze Age...	2300 - 1850 BC
Middle Bronze Age.	1900 - 1600 BC
Late Bronze Age....	1650 - 1050 BC

Iron Age:

Geometric Period...	1050 - 750 BC
Archaic Period.....	790 - 475 BC
Classical Period.....	475 - 325 BC
Hellenistic Period...	325 - 58 BC
Roman Period.....	58BC - 330 AD
Byzantine Period....	330 - 1191
Frankish Period.....	1192 - 1489
Venetian Period.....	1489 - 1571
Ottoman Era.....	1571 - 1878
British Rule.....	1878 - 1960
Republic of Cyprus.....	1960
TRNC.....	1983 -

2.1- The Economy of the TRNC

The high degree of dependence of the economy of the TRNC upon the economy of Turkey systems from the impossibility of surrounding certain problems. The high rate of inflation of the Turkish Lira used in the TRNC as a legal tender makes a drastic reduction in expenditures and an equal increase in the income items a must. Due to this fact frequent series of economic protocols signed between the TRNC and Turkey as to the granting of loans to the TRNC and the actual amount of these credits and their conditions are of crucial importance to the economic development of the TRNC.

The scarcity and insufficiency of the incentives for production in our country is limiting the offer of incentives to foreign investors, which is necessary to secure the needed economic stability in the country.

Calculations made on estimated GNP for 1997 based upon sectoral data indicate clearly the necessity of a number of economic measures to be taken. (Table 2)

As can be clearly seen from the data, due to the lack of the necessary resources of the country to provide the necessary resources of the total consumption of the country, the existence of a series of special economic protocols between the TRNC and Turkey can be put into action in order to fill this gap with the necessary economic aid and loans to be provided by Turkey.

Table (2) 1997 GNP Conjectural realization.

I. Agricultural Sector	7.6%
II. Industrial Sector	12.6%
III. Service Sector	70.5%
IV. Import Taxes	9.3%

Table (3) General Balance of the Economy

	1996	1997
	<u>Million TL</u>	<u>Million TL</u>
I. Total Resources	63,741,241.3	124,811,630.9
II. Total Investment	9,899,941.2	24,127,203.2
III. Total Consumption	53,841,300.1	100,684,427.7
IV. Public Disposable Income	10,857,559.4	21,930,818.7
V. Private Disposable Income	52,719,380.9	96,296,540.3
VI. Total Domestic Savings	9,735,640.2	17,542,931.3

Like all small Islands, the population of the TRNC shows a constant change. Even after the declaration of the TRNC, the Country continued to show a high rate of migration. Beside a high number of persons emigrating from the country, a relatively high number of young people also leave the Island with the purpose of higher education abroad. Due to anverse situations affecting the country a large number of people is leaving the Island and migrating which makes it difficult to know the exact number of the populations in the country. The last census which took place in 1995 shows the total population of the Country is 198.000 persons.

On the other hand, the total number of persons above the age of 18 in the year 1998 was 164,285, accordingly:

50,659 persons in Lefkoşa District

43,625 persons in Gazi Magosa District

28,733 persons in Girne District

23,159 persons in Güzelyurt District

18,109 persons in Iskele District

When the distribution of the population is taken according to the above districts, the level of consumption and production of end district becomes very significant.

The total labour force of the TRNC has to be considered people between the ages of 15 - 64. Accordingly to 1996 figures, this figure for the TRNC is 117,938 persons. Out of this total figure 67.7% were actually occupied in 1996, the rest being, housewives, soldiers, students, unemployed persons, person not being considered as part of the labour force, and retired persons.

Table 4 shows an eventual decrease in the total number of persons employed in the public sector. This in return indicates a decrease in the amount of resources of the budget allocated to the public sector.

Another important point is the increase shown in the construction sector, leading to an increase in the number of persons occupied in this sector which also reflect the general increase in the total population of the Country and thus the necessity of extending the activities of this sector to cover up the needs in this sector.

Table (4) Employment according to Sectors

	<u>1996</u>		<u>1997</u>	
	<u>Number</u>	<u>Percentage%</u>	<u>Number</u>	<u>Percentage%</u>
1) Agriculture	16862	21.2	16,525	20.5
2) Industry	8354	10.5	8,371	10.4
3) Construction	9807	12.4	10,241	12.7
4) Trade-Tourism	8367	10.6	8,702	10.8
5) Transport-Communication	6756	8.5	7,058	8.7
6) Financial Institutions	2456	3.1	2,575	3.2
7) Business and Personal Services	9867	12.4	10,293	12.8
8) Public Services	16899	21.3	16,972	20.9

As can be seen from the above table in the sectors showing an increase in the employment rates have also shown an increase in the volume of economic activity thus an increase in revenues. The analysis of the above table clearly indicates an increase in the employment of the construction, trade and tourism, transport and communication and financial sectors with a corresponding increase in the volume of revenues thus making possible the levying of higher taxes.

2.2- The Private and the Public Sector

The development of the economy of the country the relations with the outside world, will help improve trade and also the public sector of the country.

The improvement shown in the private sector of the Country in its present form is not attending the public sector positively. To give an example from the services sector i.e. the establishment of private universities in the country take not yet motivated the public sector to invest in this sector to eliminate its handicaps in reaching present world standards in the field of education.

The public sector has to change its old-fashion structures and adopt a more rational and planned approach in conformity with the world wide rapid developments, taking place and the private sector of the country must also follow world wide developments and adopt them according to its size and attain a certain dynamism. To give an example, the department of public works which used to asphalt the roads have not invested in modern technologies and the private sector which has heavily invested in this field of activity is during the job where by the department of public works with its outdated equipment and machines is no more in a position to do the job effectively.

III. THE CONCEPT OF TAXES

Taxes are money collected from real or legal persons according to their financial strength in conformity with laws of the country, in order to finance the public spending of the state and of the public institutions of the TRNC. Besides being as an instrument of providing a source of financing of the state, taxes are also instrumental in fulfilling social and economic functions as instruments of economic stability and affecting the income levels of real or legal persons or in financing social schemes.

According to the classical definition, taxes are divided into two groups:

- 1- Indirect Taxes
- 2- Direct Taxes

The main difference between an indirect and direct tax is the existence or absence of an intermediary person burdened with tax.

In the case of an indirect tax the financial position of the person burdened with the tax is not taken into consideration, whereas in the case of a direct tax the financial position or the capacity of payment of the person burdened with the tax is taken into consideration.

When formulating a tax system, one has also to take into consideration the aims of these taxes, which can be summarised as follows:

- Taxes are levied in order to provide financial resources; they provide the bulk of the resources of the state treasury used in financing public expenditure.

- Taxes are used as an economic instrument. A number of different exemptions enumerated in the tax laws for seing tax exempitons for economic investments end up by accelerating the fullfilment of these investments thus helping indirectly the development of the national economy.
- Taxes have a social contense; they help eliminate the wasteful use of resources, the even distribution of income amongst individual and thus the attainment of social justice.
- The global functioning of taxes; helps the better understanding of the problems created by taxes both locally and globally when present day conditions created by globalisation brought about by the technological revaluation in communications and in the international trade and the global problems of taxation brought about as a result of these changes are taken into consideration.

For taxes to have a positive social impact in a society, some principles such as the following are necessary;

a) Justice

In the collection of taxes, tax laws must provide a just implementation to all income groups based upon the principle or equality.

b) Conformity

When taxing incomes, attention must be given to their conformity with the tax rates.

c) Clarity

In order that both the people applying taxes and the tax payers can clearly know in advance the way tax laws are being made, their types, amount, their time and make of payments, the tax laws must be formulated in a very clear way, kept outside the scope of bureaucracy and when necessary the practice involved in the process must be educated.

d) Savings of Costs

In the levying and collection of taxes maximum attention must be given in order to minimise expenditures involved in the process.

3.1- The Different Kinds of Taxes in the TRNC

First of all let us talk about the different elements of the tax system of our country. These are, taxes, duties and fees respectively we have already explained what tax is, in a previous chapter.

Duties are in general used in order to define some categories of taxes which are generally used in defining indirect taxes and thus are used synonymously as such.

Fees are charges which persons have to pay to the state for services rendered or any other interests provided for by the state. For these services to be rendered by the state, persons have to pay them in advance.

As we have already mentioned, taxes imposed in the TRNC fall into two categories; direct and indirect taxes which are studied intensively below.

3.1.1- Direct Taxes

- a) Income Tax
- b) Corporate Tax
- c) Income & Corporation Tax (Previous Year)
- d) Inheritance Tax
- e) Motor Vehicles and Driving Licence
- f) Immovable Property Tax

3.1.2- Indirect Taxes

- a) Value Added Tax
- b) Bank Security Charges Tax
- c) Import Costum Tax
- d) Import-Export dock Tax
- e) Production Tax
- f) Duty Free private Tax

The other budget income are as follows;

- Duties and Licence
- Budget Income Exept Tax
- Service Cost and other Income
- Fine
- Public organization Income
- Treasury Property Rent Income
- Other Income

In the following chapters we shall give the estimated figures for the budget of the TRNC together with the effective figures for the years 1996-1997 which are comprised of various tax items on the income side.

The Tax Office is the authority which implements the direct and indirect taxes. The personnel of this office which are trying to implement to total of the the existing 13 different tax laws of the country occupying a special position in interpreting and applying these laws.

These 13 tax laws can be enumerated as follows:

- 1- Tax Procedure Law
- 2- Income Tax Law
- 3- Corporate Tax Law
- 4- Inheritance Tax Law
- 5- Motor Vehicles and Driving Licence Law
- 6- Immovable Property Tax Law
- 7- Bank Security Charges Tax Law
- 8- Value Added Tax Law
- 9- Stamp Tax Law
- 10- Law on the Procedures about the Collection of Public Dept.
- 11- Law on the Services of Off-Shore Companies
- 12- Law on the Services of Off-Shore Banking
- 13- Law on Double Taxation

3.2- Calculation of Taxes and Tax Rates in the TRNC

In the TRNC taxes are calculated based on income of individuals and tax rates are applied accordingly.

All income and benefits earned by real persons residing in the TRNC within a calendar year are subject to income tax.

The documentation of Appendix 1 explains the rates applied in the calculation of taxes. The different taxes applied in the TRNC such as Income Tax, Corporate Tax, Pay As You Earn (PAYE), Inheritance Tax.

Taxes are calculated as seen below:

3.2.1- The Calculation of Income Tax;

The man who worked in 1997 and annual income 1.500.000.000 TL.

	TL.	TL.
Annual Income	1500.000.000	
Social Security	<u>-</u>	
Cross Income		1.500.000.000
<u>Exemption:</u>		
Personal Reduction	(220.800.000)	
Private Reduction (20%)	(300.000.000)	
Couple Reduction	(13.248.000)	
Child Reduction	(13.248.000)	
		547.296.000
		<hr/>
Figure showing the taxable value		952.704.000
Annual Income Tax: 333.216.800		

(Appendix 2)

3.2.2- The Calculation of Corporate Tax

	<u>TL.</u>
From Profit & Loss Accounting	23.059.609
Minus: Investment Reduction	(7.730.642)
	<hr/>
	15.328.966
Plus: Not Acceptance expenditure	<u>7.784.290</u>
Year Profit	23.113.256

Corporation Tax 25%	5.778.314
Income Tax 15%	2.600.241
	<hr/>
Total Tax	8.378.555

3.2.3- The Calculation of PAYE (A)

* A woman who retired in 1997 and married once has got two children:

	<u>TL.</u>	<u>TL.</u>
Annual Income:		989.857.670
Tax Excmpt:	142.080.000	
Private Reduction 20%	197.971.534	
Per Child ½	4.262.400	
University Education	7.104.000	<u>351.417.934</u>
Figure showing the taxable value		638.439.736
Annual Income Tax	237.047.881	
Debt Balance	<u>6.548.114</u>	243.595.995
Paying Reduction Tax		226.668.775
Payable Income Tax		<u>16.927.220</u>

Calculation Rate take from 1996 Tax Rate Table Appendix 2

The Calculation of PAYE (B)

The situation is, married, his wife working and has got 2 children

	<u>TL.</u>	<u>TL.</u>
Annual Income:		1.143.036.562
Tax Exempt:	142.080.000	
Private Reduction 20%	228.607.312	
Couple Reduction	8.524.800	
Per Child ½	4.262.400	
University Education	7.104.000	390.578.512
		<hr/>
Figure showing the taxable value		752.458.050
Annual Income Tax	288.356.122	
Debt Balance	13.740.315	302.096.437
Paying Reduction Tax		<u>277.329.096</u>
Payable Income Tax		24.767.341

Calculation Rate take from 1996 Tax Rate table Appendix 2

3.2.4- Calculation of Inheritance Tax (A)

Dead date: 01/01/1997

Inheritance Active	Market Value	
	<u>TL.</u>	<u>TL.</u>
1) Immovable Property	17.000.000.000	
2) Movable Property		
a) Insurance wages	450.000.000	
b) Car	2.000.000.000	
c) Puan (1,440,922x5562.34)	<u>8.014.898.077</u>	
Total Active		27.464.898.077

REDUCTION

a) General Exemption	8.280.000.000	
b) Couple Exemption	828.000.000	
c) Other Exemption		
(2x552.000.000)	1.104.000.000	
d) Puan	<u>8.014.898.077</u>	18.226.898.077
		<hr/>
	Taxable amount	<u>9.238.000.000</u>
	Tax (see schedule Appendix 1)	2.214.500.000
** Plus: Interest amount within the 1/1/98		1.656.577.456
to 30/6/99 periods.		<hr/>
Total payable Tax amount		3.871.077.456

** Tax: 2.214.500.000

DATE

30.06.99 First year 50% = 1.107.250.000

(01.01.98) 5 months 50% = 461.354.168

 29 days 50% = 37.973.288

29.05.01 **Total interest 1.656.577.456**

Calculation of Inheritance Tax (B)

Dead date: 01./09/1997

Inheritance Active	Market Value	
	<u>TL.</u>	<u>TL.</u>
Donation	9.000.000.000	
Bank deposits	22.000.000.000	
Premium	<u>8.000.000.000</u>	
Total Active		39.000.000.000

REDUCTION

a) General Exemption	12.168.000.000	
b) Child Exemption	811.000.000	12.979.200.000
	<hr/>	<hr/>
	Taxable Amount	<u>26.020.800.000</u>

Tax (see schedule Appendix 1) 6.410.200.000

** Plus: Interest amount within the 1/9/98

to 30/6/99 periods 2.658.476.781

Total Payable Tax amount 3.871.077.456

** DATE 30/06/1999 Tax: 6.410.200.000

01/09/1998 9 months 50% = 2.403.825.000

29/09/ - 29 days 50% = 254.651.781

Total Interest 2.658.476.781

3.3- Overview of South Cyprus Tax System

The South Cyprus economy is based on a free enterprises system with the private sector being the backbone of economic activity. An average growth of about 6% in real terms with the services sector. It accounts for about 70% of GDP and provides employment to approximately 62% of the gainfully employed population. The currency is the Cyprus pound, which, although not freely traded in international markets.

In 1994 the GDP reached \$8 bln after an annual growth 4.8% with inflation and unemployment at 4.7% and 2.7% respectively and a per capita income of about \$12,000. the budget deficit \$242 which represents 3% of GDP.

South Cyprus is an off-shore financial centre, free from the disadvantages associated with tax heaven operations. In 1994 total tax revenue reached \$1.48 bln or 60% of total public revenue, with direct and indirect taxes accounting for \$630 mln and \$850 mln or 42.5% and 57.5% respectively. The Inland Revenue Department is responsible for the administration of direct taxes which are the following:

Personal Income tax, Corporation tax, defence tax, capital gains tax, inheritance tax, immovable property tax and stamp duty it employs staff of approximately 550 and maintains around 220,000 tax payer accounts of which 87% are personal (60% employees and 27% self-employed) and 13% are corporate.

The Customs and Excise Department, which employs staff of approximately 600 is responsible for the administration of indirect taxes, namely import duties, excise duties, value added tax and temporary refugees' levy.

The income tax and corporation tax rates of 60% to 40% and 42.5 to 25% respectively. VAT was introduced on July 1, 1992, with a standard rate 5% increased to 8% on October 1, 1993, with a declared intention for a gradual increase to 15%.

3.3.1- PERSONEL INCOME TAX

The earned and unearned income of individuals is liable to personal income tax. The table as follows;

0	- \$4500	= 0
\$4501	- \$9000	= 20%
\$9001	- \$18000	= 30%
\$18000		= 40%

3.3.2- CORPORATION TAX

Corporate profits are subject to corporation tax, which accounts for about 20% of direct taxes. Chargeable income up to \$225.000 is taxed at 20%, over \$225.000 the rate is 25%. The reduction in chargeable income, due to losses brought forward from previous years and current year's investment allowances, is subject to a 10% minimum tax. Profits from the export of locally produced and manufactured goods are taxed separately at 50% of the normal rates. Off-shore corporations are taxed at 4.25%.

3.3.3- DEFENCE TAX

Defence tax accounts for about 8% of direct taxes. Individuals and corporations are taxed at rates of 2% and 3% respectively. Current year's tax for self-employed individuals and corporations is payable on the first day following the end of the first and second half of the year. In the case of wages, salaries, dividends and interest, defence tax is deducted at sources.

3.3.4- CAPITAL GAINS TAX

Capital gains tax accounts for about 2% of direct taxes. It is imposed at the rate of 20% on gains from the disposal of immovable property including gains from the disposal of shares in private companies which own immovable property.

3.3.5- INHERITANCE TAX

Inheritance tax, which accounts for about 1% of direct Taxes's levied, upon death, on the estate of individuals. The value of the estate up to \$225.000 is progressively taxed at rates from 20% to 40%; over \$225.000 the rate is 45%.

3.3.6- IMMOVABLE PROPERTY TAX

Immovable Property Tax, which accounts for about 1% of direct taxes. The property value is progressively taxed at rates from 0.2% to 0.35%.

3.3.7- VALUE ADDED TAX (VAT)

VAT, which accounts for about 45% of indirect taxes, is imposed on the provision of goods and services as well as on the importation of goods in South Cyprus. Registration is compulsory for businesses with an expected annual turnover of over \$27.000. Legislation provides for a zero rate and standard rate currently at 8%. Zero rated goods and services include exports, food, books, medicines and childrens' clothing and footwear, whereas certain goods or services including rents, medical, insurance and financial services are exempt. Return must be submitted quarterly and if output tax exceeds input tax the net balance has to be paid to the state within forty days from the end of each quarter.

3.3.8- CUSTOMS DUTIES

Customs duties, which account for about 23% of indirect taxes, are regulated by a progressive tariff system.

3.3.9- EXCISE DUTIES

Excise duties, which account for about 28% of indirect taxes, are levied on certain locally produced or imported goods such as motor vehicles, tobacco products, petroleum products and spirits and beer.

3.3.10 - TEMPORARY REFUGEES LEVY (TRL)

TRL, which accounts for about 3% of indirect taxes, is imposed on imports at general rates ranging from 2.2% to 6% on the value of goods imported.



3.4- In 1996 and 1977 Distribution of Accumulate Taxes in TRNC

As we mentioned before we shall explain the taxes.

In the Tax System the difference between accrual and collecting amount, gives us real annual collection. (Table 5)

(Table 5) In 1996 Budget Collecting Table and Local Income Rate

	<u>1996</u> Budget million TL	<u>1996</u> Collecting million TL	<u>In the Local Income Rate</u> %
	-----	-----	-----
Direct Taxes	5.089.500	6.549.066	45.15
Indirect Taxes	4.895.000	4.732.543	32.62
Budget Income Exept Tax	1.808.913	2.716.065	18.73
Confiscates and Fine	99.000	238.031	1.65
Public Organization Income	4.000	28.587	0.19
Treasury Property Rent Income	21.260	88.945	0.62
Other Income	177.907	151.557	1.04

Total Local Income		14.504.794	

In 1997 Budget Collecting Table and Local Income Rate

	<u>1997</u> Budget million TL	<u>1997</u> Collecting million TL	<u>In the Local Income Rate</u> %
	-----	-----	-----
* Direct Taxes	11.097.700	13.796.933	43.58
- Income Tax		7.893.402	24.94
- Corporate Tax		3.140.574	9.92
- Income & Corporate Tax (previous year)		601.039	1.90
- Inheritance Tax		30.375	0.09
- Motor Vehicles & Licence Tax		1.329.592	4.20
- Immovable Property Tax		14.790	0.05
 * Indirect Taxes	 8.835.000	 11.432.110	 36.12
* Budget Income Exept Tax	3.465.170	5.042.240	15.9
* Confiscates and Fine	212.530	462.640	1.47
* Public Organization Income	4.000	5.526	0.03
* Treasury Property Rent Income	90.000	510.761	1.62
* Other Income	295.600	402.211	1.28

Total Local Income		31.652.421	

As can be seen from the tables above the percentage of the indirect taxes provided from domestic income was 45.15% for 1996 and 43.58% in 1997. This fall is due to the reason that not all tax payers paid their dues.

The Value Added Tax which was introduced on 1 July 1996 in the TRNC had the main of taking under record all economic activities in the country, by introducing VAT rates ranging from 0% - 2% and 6% - 10%.

The Value Added Tax is applied by starting with the whole sale prices and is added each time it changes hands till the ultimate consumer buys and consumes it. In this way it is designed to be a consumption tax. By providing the possibility of 5% tax return from the amount of total. Purchases on certain catagories or consumption goods which are payable for a period of four months. It is hoped that the economic activities in the country will on the whole be recorded.

Let us now see in more detail the three main forms of taxes in the TRNC, namely Income Tax, Corporte Tax and VAT.

INCOME TAX

Income tax is calculated by taking the actual income of every individual as a basis. The total number of persons in the TRNC who have to pay income tax is about 43.000.

All institutions and legal persons, civil servants have to pay income tax based upon their wages and salaries.

To give an example, the income tax of a civil servant is calculated by taking into consideration the price index and the salary adjustments. But on the other hand, a person employed in the private sector pays

income tax based upon the wages or salaries which this person has to declare to the state in advance. Therefore, if this person employed in the private sector declares his or her wages or salary and the minimum legal wage which is from income tax, this declaration is considered as valid and will first be controled after a lapse of one year's time. On the other hand, the civil servants and government employees, as explained above, have to pay their income taxes as calculated in due time, thus the state does not suffer any losses because of any eventual discrepancies.

Another point is that some income tax payers avoid giving sales receipts to their customers thus not registering these sales transactions and deliberately evading income taxes.

While the scope of the income tax is being continuously enlarged, the mechanisms of its control are also being enlarged. In a further chapter dealing with proposals, we shall also deal with the income tax and enumerate related proposals pertaining the income tax.

CORPORATE TAX

The total number of corporate tax payers in the TRNC is 19.000. The rate of corporate tax in the TRNC is 25%. In 1997, 3,140,574.000 TL of corporate tax was paid local corporations and corporations established in the TRNC. Apart from that, the off-shore banks operating in the TRNC have to pay 2% corporate taxes based upon their income earnings.

Whereas the off-shore banks have to pay only 2% corporate income tax based upon their incomes. The other corporations while deducting the costs of each item before calculating the income and then calculating the income tax in accordance with the seemingly lower tax rates, the overall corporate income taxes paid in the TRNC are thus correspondingly lower.

This shows very clearly that due to accounting or procedural errors deliberately or otherwise created, the normal amount of corporate income tax which has to be paid to the state is less than it should normally be.

Let us take the example of a company as far as its debts and credits are concerned. Let us assume that the director of company 'A' is at the same time the director of companies, B,C and D. Company 'A' gives loans to companies B, C and D thus having to pay 25% corporate taxes and at the end of the year since it must have made profits. But on the other hand Company 'A' does not have to pay these 25% corporate taxes since it shows losses on its accounts and also shows a high amount of bank interest payments because of the bank loanstaken. This example shows clearly how the common director of companies A,B,C, and D by means of providing a bank credit to Company A and in turn giving it as a loan to companies B, C and D creates a system of book-keeping which evaded corporate taxes to all of the four companies.

Value Added Tax

It refers that value added for every department such as wholesale to the consumer every stage use value added.

This Law prepared and copied by Turkey so every steps and every complex situation is conflict for other laws which are Income Tax and Corporation Tax.

The aim of that VAT is to control for every recorded paper to the business or enterprinver but today they have a pure complex problem In the market.

Who are responsible to record and give the invoice to the consumer they can not do accurate record. These cause to tax evasion.

3.5- Comparison of TRNC and South Cyprus TAX System

There are differences and almost same tax rate use in two countries. Due to the fact that within the Direct Taxes and Indirect Taxes you can easily and clearly understand the differtiation of these taxes.

As below, The Comparison Tax Rate within the TRNC and South Cyprus.

Comparison Table TRNC - South Cyprus

	<u>T.R.N.C.</u>	<u>South Cyprus</u>
Direct Taxes	45.15%	42.5% in total Local Income
Indirect Taxes	32.62%	57.5% in total Local Income
Corporate Tax Rate	25%	25%
Off-shore Tax Rate	2%	4.25%
Corporate-self-employed		
Number	43.000	58.000
V.A.T.	N/A	45% in indirect Tax
V.A.T. Rate (standard)	10%	8%

Above Table Direct taxes within the Total Local Income, the Direct taxes in TRNC 45.15% and South Cyprus 42.5%. Indirect Taxes percentage 32.62% and South Cyprus 57.5% In TRNC tax system will improve that rate because there is a big difference between the two countries. The Corporate tax rate is the same.

Off-shore Tax rate is higher than TRNC. I think it's reasonable to that rate, because the Country who gives permission to establish off-shore bank must take high-commission. So TRNC must be move up that rate.

In Corporate number, in South Cyprus there are 58.000 tax payers but in TRNC there are 43.000 tax payers. In these circumstances much more taxpayer more tax collection, and above the rate or tax is important. Abart from this comment the important factor of consumer tax which is VAT the standard rate in TRNC 10% but South Cyprus is 8% and also within the Indirect Tax percentage is 45% in TRNC is not applicable yet.

IV. PROPOSALS

It can be clearly seen from the above analysis that the taxation system of the TRNC is mainly based upon the income tax. This necessitates the registration of all incomes and a system of controls so that all incomes are registered. But this is a colossal task which is difficult to register and control. This situation leads to huge losses of income for the state i.e. due to the non realisation of the collection of all income taxes.

Another method of tax collection would be an expenditure tax, which would provide more taxes for the state, allowing the state to spend more money in providing services to the public. This system of expenditure taxes also provides more justice to the tax payers, as people pay taxes each time that they purchase something i.e. make expenditures. As compared with the income tax and the problems of registration and collection attached to it are considered, the expenditure tax which one pays automatically each time that one undertakes purchase transactions, is a more effective way of collecting more taxes.

One of the biggest problems in the TRNC nowadays is the emigration of the youth in large numbers due to the lack of job opportunities. A large number of people are employed in the public sector, largely in order to artificially employ people in order to slow down the actual wave of emigration. But this is resulting in a huge idle capacity in the public sector, as far as human resources is concerned. It would be advisable to canalize this idle capacity into the private sector by giving long term low interest rate credits to young people and also by paying a substantial part of the wages and salaries of these people and the other persons likewise employed in the private sector from public funds. This will lead on the

one hand to an increase in the efficiency and quality in the running of the public sector and also will inject new life into the stagnating private sector. As an overall result, due to better allocation of public resources the economy of the TRNC will be accelerated thus creating more jobs, which means a correspondent decrease in emigration of specially the young people forced to leave the country due to cronic unemployment in the private sector.

The rapid globalisation of the world economy has brought about the urgent matter of creating a global taxation system. In the light of this rapid change, the TRNC is forced to urgently and seriously reconsider and reformulate its tax laws and tax systems to readjust them in order to be in footing with these global changes. All this necesitates a network of computerized systems inter-related with the internet system. But to give one example, trade and business transactions done via the internet is also increasing rapidly in the TRNC. If the TRNC wants to collect taxes from these transactions it has to put into place such systems as described above.

V. CONCLUSION

Our country being an strategic Island in the Eastern Mediterranean and the TRNC having special economic relations only with Turkey is making the application of a consistant monetary policy very difficult due to the overall economic problems faced by Turkey and due to the political non-recognition of the TRNC in the world arena.

While talking about creating new jobs in the TRNC, we have to attach importance to the services sector, which has a big place in the economy of the country. The allocation of incentives to sectors like tourism and industry shows us clearly that a clear-cut policy of providing sufficient incentives to the services sector of the country will automatically result in creating new jobs. But in order to attain this goal appropriate changes must be made to the rules and regulations in the allocation of incentives.

While comparing the direct and indirect tax of the TRNC with that of the Greek Cypriot Administration in South Cyprus, one can clearly see the low level of direct and indirect taxes in South Cyprus as compared with those in the TRNC. Another striking difference between the TRNC and South Cyprus is that while in South Cyprus 4.5% commision is taken from off-shore banks, this percentage in the TRNC is only 2%.

The existance of non-recorded economic activity in our country, if any, does not in general create any major problems is our small-scale island economy. On the contrary, if any drastic measures are to be taken in order to register everything, this will lead to a dramatic liquid money shortage and thus affect the small shop owners and the artisans very negatively.

The law on the elimination of non-recorded economy, the so-called "black money" in Turkey has been passed mainly due to the EU pressure on Turkey. But the application of this law will lead to the elimination of "hot money" from Turkey, the exodus of hot money to EU countries which will lead to the outflow of this hot money thus a corresponding decrease in bank accounts and investments taking place in the country based on hot money, i.e. "black money". At the end of the day, the application of these laws will mainly benefit the EU countries and not Turkey.

Likewise, it is advisable that the TRNC should stop warring about the so-called "black money" and allow the free flows and in flux of foreign investments into the TRNC.

When compared with South Cyprus where on the average, a 8% VAT (Value Added Tax) is being levied whereas in percentage for the TRNC is 10% and in South Cyprus a zero percent VAT is applied to health, basic food-stuffs and education.

It can clearly be seen that as from 1 July 1996, the date of application of the VAT in the TRNC, an effective control of the economy has been achieved through an effective registration of transactions. Dependent upon this fact, a repayment of let's say 2% of the VAT paid generally on all food-stuffs will help a lot the effective enforcement of the VAT in the TRNC.

Parallel to the successful application of the VAT in the TRNC, a corresponding increase in the income tax collected will be achieved, while a large part of the economy will thus, be registered. This will of course lead to an increase in public revenues.

Besides the income tax, the corporate taxes will also be more effectively collected due to the same reason, namely with the enforcement of the VAT the corporations will be forced to run their book-keeping and accounts systematically and regularly thus showing in their accounts realistic amounts which will serve as a good bases for income tax, thus helping to minimise tax evasion.

Appendix (1) Inheritance Tax Table

<u>Definition of Reduction</u>	<u>1/1/97 - 31/8/97</u>	<u>1/9/97 - 31/12/97</u>
Upon the Estate Cost		
1) General Exemption	8.280.000.000	12.168.000.000
2) Couple Exemption	828.000.000	1.216.800.000
3) Child Exemption	828.000.000	811.120.000
4) Other Exemption	552.000.000	

SCHEDULE (1/1/94 - 31/12/94)

A) 0 - 100.000.000 TL.	5%
B) 100.000.001 - 300.000.000 TL.	10%
C) 300.000.001 - 600.000.000 TL.	15%
D) 600.000.001 - 900.000.000 TL.	20%
E) 900.000.000 - ABOVE	25%

1992 - 1999 YILLARINA AİT VERGİ MATRAHLARI VE VERGİ ORANLARI

1992 Yılına Ait MATRAH VE VERGİ ORANLARI					1996 Yılına Ait MATRAH VE VERGİ ORANLARI				
BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi	BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi
7,000,000.-	0,000,001.-	1,750,000.-	% 25	1,750,000.-	80,000,000.-	0,000,001.-	20,000,000.-	% 25	20,000,000.-
7,000,000.-	7,000,001.-	2,100,000.-	% 30	3,850,000.-	80,000,000.-	80,000,001.-	24,000,000.-	% 30	44,000,000.-
7,000,000.-	14,000,001.-	2,450,000.-	% 35	6,300,000.-	130,000,000.-	160,000,001.-	45,500,000.-	% 35	89,500,000.-
10,000,000.-	21,000,001.-	4,000,000.-	% 40	10,300,000.-	185,000,000.-	290,000,001.-	74,000,000.-	% 40	163,500,000.-
12,000,000.-	31,000,001.-	5,400,000.-	% 45	15,700,000.-	400,000,000.-	475,000,001.-	180,000,000.-	% 45	343,500,000.-
	43,000,001.-		% 50		875,000,000.-	875,000,001.-		% 50	
	43,000,001.- ve yukarısı için								
	43,000,001.- ve yukarısı için								
1993 Yılına Ait MATRAH VE VERGİ ORANLARI					1997 Yılına Ait MATRAH VE VERGİ ORANLARI				
BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi	BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi
14,000,000.-	0,000,001.-	3,500,000.-	% 25	3,500,000.-	155,000,000.-	0,000,001.-	38,750,000.-	% 25	38,750,000.-
14,000,000.-	14,000,001.-	4,200,000.-	% 30	7,700,000.-	155,000,000.-	155,000,001.-	46,500,000.-	% 30	85,250,000.-
14,000,000.-	28,000,001.-	4,900,000.-	% 35	12,600,000.-	240,000,000.-	310,000,001.-	84,000,000.-	% 35	169,250,000.-
14,000,000.-	42,000,001.-	5,600,000.-	% 40	18,200,000.-	345,000,000.-	550,000,001.-	138,000,000.-	% 40	307,250,000.-
25,000,000.-	56,000,001.-	11,250,000.-	% 45	29,450,000.-	740,000,000.-	895,000,001.-	333,000,000.-	% 45	640,250,000.-
	81,000,001.-		% 50						
	81,000,001.- ve yukarısı için								
	81,000,001.- ve yukarısı için								
1994 Yılına Ait MATRAH VE VERGİ ORANLARI					1998 Yılına Ait MATRAH VE VERGİ ORANLARI				
BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi	BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi
15,000,000.-	0,000,001.-	3,750,000.-	% 25	3,750,000.-	310,000,000.-	0,000,001.-	77,500,000.-	% 25	77,500,000.-
16,000,000.-	15,000,001.-	4,800,000.-	% 30	8,550,000.-	310,000,000.-	310,000,001.-	93,000,000.-	% 30	170,500,000.-
25,000,000.-	31,000,001.-	8,750,000.-	% 35	17,300,000.-	480,000,000.-	620,000,001.-	168,000,000.-	% 35	338,500,000.-
35,000,000.-	56,000,001.-	14,000,000.-	% 40	31,300,000.-	700,000,000.-	1,100,000,001.-	280,000,000.-	% 40	618,500,000.-
45,000,000.-	91,000,001.-	20,250,000.-	% 45	51,550,000.-	1,500,000,000.-	1,800,000,001.-	675,000,000.-	% 45	1,293,500,000.-
	136,000,001.-		% 50						
	136,000,001.- ve yukarısı için								
	136,000,001.- ve yukarısı için								
1995 Yılına Ait MATRAH VE VERGİ ORANLARI					1999 Yılına Ait MATRAH VE VERGİ ORANLARI				
BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi	BİRİM MATRAH	Kümülatif Matrah	Birim Vergi	ORAN	Kümülatif Vergi
50,000,000.-	0,000,001.-	12,500,000.-	% 25	12,500,000.-	350,000,000.-	0,000,001.-	70,000,000.-	% 20	70,000,000.-
50,000,000.-	50,000,001.-	15,000,000.-	% 30	27,500,000.-	350,000,000.-	350,000,001.-	87,500,000.-	% 25	157,500,000.-
80,000,000.-	100,000,001.-	28,000,000.-	% 35	55,500,000.-	500,000,000.-	700,000,001.-	150,000,000.-	% 30	307,500,000.-
115,000,000.-	180,000,001.-	46,000,000.-	% 40	101,500,000.-	800,000,000.-	1,200,000,001.-	280,000,000.-	% 35	587,500,000.-
250,000,000.-	295,000,001.-	112,500,000.-	% 45	214,000,000.-	1,550,000,000.-	2,000,000,001.-	620,000,000.-	% 40	1,207,500,000.-
	545,000,001.-		% 50						
	545,000,001.- ve yukarısı için								
	545,000,001.- ve yukarısı için								

1992 - 1999 Yıllarına ait Gelir Vergisi Yükümlülerine Tanınan İndirim ve Muafiyetler.

1992 - 1999 Yıllarına ait GCM Vergisi Tutarları

Sıra No.	İNDİRİMİN CİNSİ	YASA MADDESİ	KİŞİSEL İNDİRİM ORANI	YILLIK İNDİRİM VE MUAFİYET MİKTARLARI							
				1992	1993	1994	1995	1996	1997	1998	1999
1	KİŞİSEL İNDİRİM	12 (1)		7,750,000.-	13,200,000.-	28,800,000.-	90,500,000.-	142,080,000.-	220,800,000.-	482,400,000.-	816,000,000.-
2	ÖZEL İNDİRİM (Safi Kazanç üzerinden) * A- Ücretliler ile Götürü Vergilendirme B- Yukarıdakiler dışındakilere * Her türlü gider ve muafiyetler ile sosyal güvence katkıları indirildikten sonra.	14 (1) 14 (2)	- -	% 20 % 10	% 20 % 10	% 20 % 10	% 20 % 10	% 20 % 10	% 20 % 10	% 20 % 10	% 20 % 10
3	EŞ İNDİRİMİ A- Birlikte yaşayan eş için B- Boşanmış eş ödenen NAFAKA	12 (2) 12 (3)	% 6 % 4	465,000.- 310,000.-	792,000.- 528,000.-	1,728,000.- 1,152,000.-	5,430,000.- 3,620,000.-	8,524,800.- 5,683,200.-	13,248,000.- 8,832,000.-	28,944,000.- 19,296,000.-	48,960,000.- 32,640,000.-
4	ÇOCUK İNDİRİMİ (**) A- i) 16 yaşından küçük eğitim görmeyen, ii) İlk öğretimde olan, iii) Evlenmemiş ve geliri olmayan kız, (yaş haddi aranmaz.) B- i) 20 yaşından küçük KKTC'de orta öğretimde olan, ii) Yedek Subaylık dışında askerlik yapan, iii) 18 yaşından küçük KKTC dışında orta öğretimde olan, iv) Sürekli sakat ve yetersiz olan, C- 18 yaşından küçük, 27 yaşından büyük olmayan Yüksek Tahsildeki çocuk için, (KKTC'de veya dışında) D- Üç ve daha fazla çocuk sahibi olan yükümlüler için, ödenecek VERGİ miktarından yapılacak indirim oranı i) Üçüncü çocuk için ii) Sonraki her çocuk için (ilâve olarak) ** Eşlerin aynı ayı gelirleri olması halinde çocuk indirimleri eşler arasında eşit bölüştürülerek hesaplanır.	13 (1) (A) " " 13 (1) (B) " " 13 (1) (C) 13 (1) (D)	% 5 % 6 % 10 - -	387,500.- 465,000.- 775,000.- % 15 % 5	660,000.- 792,000.- 1,320,000.- % 15 % 5	1,440,000.- 1,728,000.- 2,880,000.- % 15 % 5	4,525,000.- 5,430,000.- 9,050,000.- % 15 % 5	7,104,000.- 8,524,800.- 14,208,000.- % 15 % 5	11,040,000.- 13,248,000.- 22,080,000.- % 15 % 5	24,120,000.- 28,944,000.- 48,240,000.- % 15 % 5	40,800,000.- 48,960,000.- 81,600,000.- % 15 % 5
5	SAKATLIK VE YAŞLILIK İNDİRİMİ : A- i) Çalışma gücünün en az %50'sini, ii) Çalışma gücünün en az %100'ünü, kaybedenlere, B- 65 Yaşını doldurmuş yükümlülere,	15 (1) 15 (1) 15 (2)	% 15 % 30 % 5	1,162,500.- 2,325,000.- 387,500.-	1,980,000.- 3,960,000.- 660,000.-	4,320,000.- 8,640,000.- 1,440,000.-	13,575,000.- 27,150,000.- 4,525,000.-	21,312,000.- 42,624,000.- 7,104,000.-	33,120,000.- 66,240,000.- 11,040,000.-	72,360,000.- 144,720,000.- 24,120,000.-	122,400,000.- 244,800,000.- 40,800,000.-

Sıra No.	İNDİRİMİN CİNSİ	YASA MADDESİ	KİŞİSEL İNDİRİM ORANI	YILLIK İNDİRİM VE MUAFİYET MİKTARLARI							
				1992	1993	1994	1995	1996	1997	1998	1999
6	SOSYAL KONUT İNDİRİMİ Sosyal Konut edinme faizi indirimi (Başka bir konutu olmayan ve KKTC'deki Banka ve Kooperatiflerden borçlanılan veya Devlet Sosyal Konut Projesi Fonunun tahakkuk ettirdiği bir önceki yıla ait faizler). Ayrıca, Dairenin onayının alınması koşuluyla Sosyal Konut nitelikli kişisel konut inşaatlarına da benzeri indirim tanınmaktadır.	8 (2)	300.000 TL'ni aşmamak ve Vergi Dairesinin onayını almak koşuluyla.	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-	(azami) 300,000.-
7	SOSYAL GÜVENCE GİDERLERİ Sosyal Güvence Katkıları toplamının (Sosyal Sigorta ve İhtiyat Sandığı ile onaylı Emekli Sandıkları) i) İşveren katkı payı ii) Yükümlü katkı payı	BKK (EK-1/513/86) BKK(E-882-92) 7 (1) (e) 7 (1) (f)		% 17 % 11	% 19 % 13	% 19 % 13	% 19 % 13	% 19 % 13	% 19 % 13	% 19 % 13	% 19 % 13
8	DİĞER GİDERLER i) Belediye Meslek Vergisi ii) Hayat Sigortası Primleri	7 (1) 4/98	İlgili yılda ödenen miktar kadar. Her ay kesilen Sosyal Güvence katkı payı ile sınırlı.								

E - 882 - 92 sayılı Bakanlar Kurulu Kararı uyarınca bahse konu oranlar 1 Temmuz 1992 tarihinden geçerli olmak üzere % 17'den % 19'a; % 11'den % 13'e yükseltilmiştir.

NOT : Aylık ücretlerin hesaplanmasında özel indirim dışındaki indirimlerin 1 / 12'si (on ikide biri) esas alınır ve Aylık Vergi Cetveli hesaplanır.

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