

## Re-Financing Model for Angel Investment Permits

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Currently, the process for obtaining angel investment permits in Turkey is strict and at times causes practical problems for parties seeking to make or receive investments. In theory, a re-financing model is possible within the existing legal framework for angel investments which would increase the flexibility of investment timelines. Such a model could allow investors to receive tax benefits for investments made into start-ups before the investor has received an angel investment permit from the Turkish Undersecretariat of Treasury (the "Treasury").

The Treasury recently recognized and permitted the re-financing model in a particular application, allowing an investment to qualify for the angel investment tax advantages, despite the Treasury having not granted the investment permit yet. It is unclear though whether the Treasury will consistently accept such an interpretation or even amend the legislation to specifically contemplate investments which are initiated as loans to later be converted to capital.

If the Treasury recognizes the re-financing model as a permitted investment structure which qualifies for the associated tax advantages, this would be a significant step by the Treasury in supporting the Turkish angel investment ecosystem. It is likely that the increased flexibility would encourage investment volumes to increase accordingly.

The recently introduced angel investment regime is one of the most investment-mobilizing schemes in Turkey. The scheme might appear to be slightly rigid when compared to the real economic needs of start-ups. However, with flexible interpretation of the legislation, as well as certain other improvements, the process will be made easier for many prospective and ongoing investments in the short and mid-term.

Explanation of the full legal framework governing the Turkish angel investment system is outlined in this article, including an outline of the process for obtaining an angel investment permit.

## The Typical Process for Obtaining an Angel investment Permit

Typically, before making an investment into a start-up, an angel investor (holding an angel investor license) should apply to the Treasury to obtain an angel investment permit. To qualify for angel investment tax benefits, the investor must receive the investment permit before he or she makes the investment. The Treasury issues an investment permit if it is satisfied that the prospective investment, as well as the recipient (the start-up) meets the applicable legislative criteria. In practice, angel investment permits contain limited information, to the effect that the subject matter investment complies with the legislation and the investment must be completed within three months of the permit date.

Once the Treasury has issued the investment permit, the investor must complete the investment into the start-up in line with all of the information previously submitted to the Treasury. The investor must close the

transaction within three months (the legislative timeframe for investment permits).

After completing the investment, the investor must submit a series of formal documents to the Treasury which show the investment has been made in line with the terms of the angel investment permit.

The typical process above requires the Treasury to grant the investment permit first, before the investor can complete the investment. Any amount which the investor pays into the start-up prior to receiving the investment permit would not qualify for the associated tax advantages. It can be challenging for parties in the Turkish angel investment ecosystem to satisfy such strict chronological requirements and navigate the associated procedural bureaucracy. For example, such a linear process raises obstacles for an investor who seeks to invest in a start-up at a given time, or a start-up which seeks cash injection for a time-sensitive purpose (such as continuing daily operations).

## The Re-Financing Model - An Alternative Interpretation

Under the re-financing model, investment amounts that were previously injected into the start-up for operational costs and expenses could be counted as a simple repayable loan in the business plan submitted to the Treasury.

Usually, in the business plan submitted to the Treasury with investment permit applications, the proposed investment amount is allocated to future expenses. These fall in the period after the investment permit is received and the investment has been completed. Under the re-financing model though, the amount is allocated to past expenses. Once the Treasury grants the investment permit, the investor would then invest into the start-up as re-financing in order for the start-up to re-pay the loan and for the capital increase process (registration with the Commercial Registry). Through this approach, investments made into a start-up before completing the Treasury's lengthy investment permit procedures may qualify for the associated tax benefits.

The re-financing model could potentially allow a more flexible process for realizing investments into start-ups, while still ensuring the investment is eligible for the tax benefits associated with investment permits. At this stage, while the re-financing model is theoretically possible within the existing legal framework and we have limited experience with the Treasury accepting such an approach, it is unclear whether the Treasury will be consistently accept such an approach.

In the documentation submitted to the Treasury during the subsequent investment permit application, it is essential to accurately indicate the start-up's expenses or costs which will be covered from the re-financing amounts. The business plan submitted to the Treasury must list the estimated purchase prices and purchase dates of equipment, raw materials, intermediate goods, salaries and other costs. The total of those estimated costs and expenses must equal the investment amount subject to the angel investment permit application.

Under the re-financing model, it is only the chronology of events that are switched and stretched slightly in order to allow a more flexible structure for realizing investments. It is clear that an investment permit must still be obtained from the Treasury in order for the investment to qualify as an angel investment. All other closing requirements will also still apply, such as the capital increase for the new investment and formal registration requirements with the commercial registry.

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