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Montenegro

On the 27th of February 2012, the Montenegrin Parliament enacted amendments to the Law on Corporate Income Tax, the Law on Personal Income Tax and the Law on Contributions for Mandatory Social Security Contributions. These amendments were published in the Official Gazette of Montenegro no. 14/12 dated the 7th of March 2012 and came into force that same day.

I. Amendments to the Law on Corporate Income Tax

The duration of the tax exemption period for investment in underdeveloped regions has been extended

Under the Montenegrin Law on Corporate Income Tax (the "CIT Law") companies that invest in underdeveloped regions in Montenegro were entitled to a full exemption from corporate income tax for a period of 3 years. Under the latest amendments to the CIT Law, the period for a tax exemption has been extended to 8 years, and starts to run from the date of the registration of the company or a branch in the relevant commercial registry. A Tax exemption is not available for companies operating in the primary production sectors concerning agricultural products, transportation and shipbuilding, fishing and the steel industry.

Certificates of tax residency finally introduced

Up until the latest changes of the CIT Law, in Montenegro there were no prescribed procedures and forms under which Montenegrin tax authorities could issue a certificate of Montenegrin tax residency for the purposes of the application of double tax treaties. The lack of a prescribed form of certificate of tax residency was a source of significant problems for Montenegrin tax residents who wanted to utilise tax benefits available to them under the double tax treaties. Likewise, Montenegro does not have any established form in which foreign authorities should issue their certificates of residency for foreign tax residents that have operations in Montenegro and who want to use the beneficial tax treatment in Montenegro that is available under the double tax treaties.

Amendments to the CIT Law have, for the first time, introduced an obligation on the Montenegrin Tax Authority to issue certificates of tax residency, and have prescribed that the form and content of the certificates will be prescribed by the Ministry of Finance. It is not entirely clear from the relevant provisions whether the Ministry of Finance will merely prescribe the form of the certificate of Montenegrin tax residency, or if they will also include the form of the certificate to be issued by the foreign tax authorities for the purposes of the utilization of tax benefits available to foreign tax residents in Montenegro. Likewise, since it is only formally introduced in the CIT Law, which governs the tax obligations of legal persons, it remains unclear as to how the Montenegrin Tax Authority will deal with the certificates of tax residency which may be requested by natural persons.

It is reasonable to expect that the relevant regulations of the Ministry of Finance will introduce more clarity on this matter. Up until now, the Ministry of Finance has not issued these regulations and at this point it is quite uncertain when their adoption is to be expected.

II. Amendments to the Law on Personal Income Tax

Non-residents now taxed on income generated in Montenegro

Up until the latest amendments to the Law on Personal Income Tax (the "PIT Law"), individuals who did not have the status of tax residents in Montenegro were only subject to taxation in Montenegro if they had a permanent establishment in Montenegro. Naturally, this has significantly reduced the number of foreign citizens who paid tax in Montenegro, since even where relevant income was clearly sourced in Montenegro, it could not be taxed unless the activities of foreign citizens were such to create a permanent establishment in Montenegro (which effectively meant that the foreign citizens had been establishing a branch in Montenegro since so far this was the only form of the permanent establishment recognized by Montenegrin Tax Authority).

Under the latest amendments to the PIT Law reference to the existence of a permanent establishment is removed from the text of the relevant provision defining the scope of the tax liabilities of non-residents. Even though after this change the language of this provision remains somewhat unclear, it is evident that the intention is to have non-residents subject to tax on income generated in Montenegro, so as to consistently apply the source principle in relation to non-resident natural persons.

Relevant regulations as well as the practice of the Montenegrin Tax Authority still remain somewhat unclear as to the procedure and forms which should be used by those foreign nationals who generate income in Montenegro, but who do not have the status of Montenegrin tax residents (as is ultimately the case with foreign nationals who do have the status of Montenegrin tax residents) in order for them to fulfill their tax obligations in relation to various types of income subject to taxation in Montenegro under the general rules, and it may be expected that this will continue to be a matter of some controversy until this problem is resolved in a clearer manner by the relevant tax regulations.

Dividends and shares of profits now subject to tax

Under the latest amendments to the PIT Law, dividends and shares of profits are now also deemed as income from capital and taxed accordingly. Up until the latest amendments these dividends and share in profits were not included in the list of income from capital subject to taxation (interest, the share of profits paid to members of management and employees and the use of a company's assets for private purposes of the shareholders of the company). Income from capital is taxed at a general tax rate of 9%.

Rules governing taxation of capital gains from the sale of immoveable property and sale of shares improved and clarified

Amendments to the PIT Law elaborate on the number of issues relevant for the establishment of a tax base for tax on capital gains, including capital gains generated from the sale of immoveable property and the sale of shares in limited liability companies and joint stock companies.

Rules governing taxation of capital gains generated from the sale of immoveable property now include a clearer definition of the immoveable property that is subject to capital gains tax, and have detailed provisions concerning the establishment of the acquisition value and the sale price of immoveable property for the purposes of the establishment of capital gains subject to taxation. Amongst other things, the sale price of immoveable property now includes, besides the price at which the property was sold, the documented costs of reconstruction and costs associated with the sale of immoveable property. If the sales price is lower than the market price than the Tax Authority has the right to assess tax in accordance with the market price. In this case the market price of the property will be established in accordance with the methodology prescribed for the assessment of the value of immoveable property for the purposes of property tax. The acquisition value of the immoveable property for the purposes of capital gains tax is the price at which the property was acquired, adjusted in accordance with the annual price index.

Tax on capital gains will not be due if the natural person who sold the property used the relevant property as his/hers only or main place of residence.

As for the taxation of capital gains generated by natural persons from the sale of shares, the law now specifies that the acquisition value of a share in a limited liability company is equal to the price at which the share was purchased, or to the sum of the initial and subsequent capital contributions made by the seller-shareholder in the company, in cases in which the company whose share is sold was originally established by the seller.

For shares in joint stock companies, the acquisition value of the shares in joint stock companies which are not listed on the stock exchange is the price paid by the seller, if the seller can document such a price. If the seller cannot document the price paid, then the acquisition value is equal to the nominal value of the shares. In cases in which the seller acquired the shares of the same issuer in several transactions at different prices, the acquisition price will be established under the FIFO method, in chronological order as to when the shares were acquired.

Scope of persons required to file annual income tax return narrowed down

The Montenegrin system of taxation of personal income is based on some form of "synthetic" system of taxation where all income generated by an individual over the course of a calendar year is taxed at the end of the year, under a unique tax rate of 9%. On certain types of income paid to natural persons by legal entities (such as salaries, dividend, etc.) tax is paid on each individual payment of income, by the legal entity on a withholding basis. Given that in these cases it is superfluous to also file an annual tax return, the amendments to the PIT Law clarify the cases where natural persons are required to file an annual income tax return (so as that in other cases this obligation does not exist). Under the latest amendments to the PIT Law, the obligation to file annual income tax return exists in the following cases:

- For sole entrepreneurs who pay tax on their real income;
- For individuals who generate income from immoveable property;
- For individuals who generate capital gains;
- For income generated abroad;
- Non-resident natural persons on income for which tax due is not paid by the legal person on a withholding basis.

Under the latest amendments to the PIT Law, the form and content of the annual tax return will be prescribed by the Ministry in charge for finance, instead of the competent tax authority, as it was provided earlier. This tax return has to be filed in one copy directly, either by mail or electronically.

A tax exemption for income generated from production activities in underdeveloped regions is introduced

The latest amendments to the PIT Law introduced a tax exemption for natural persons who invest in underdeveloped regions of Montenegro, equivalent to the similar tax incentive granted to legal persons. Effectively, this exemption is given to natural persons registered with the relevant commercial registry as sole entrepreneurs; as this is the only form in which a natural person may independently conduct business activities on a permanent basis in Montenegro.

Tax exemption status is granted for a period of 8 years, starting from the date of the commencement of business activities. The exemption applies only to the income generated from production activities and does not apply to sectors of primary agricultural production, ship building, fisheries and the steel industry.

Tax relief for the employment of new employees abolished

Up until the latest changes to the PIT Law, natural persons (sole entrepreneurs) were entitled to a reduction in tax for each newly employed person, in an amount equal to the amount of the gross salary paid to the employee. The latest amendments to the PIT Law completely abolished this incentive.

Sole entrepreneurs

Amendments to the PIT Law abolished the limitation on the deductibility of expenses for social security contributions paid by the sole entrepreneurs for its employees. Up until the latest amendments, only 50% of social security contributions were recognized as a tax-deductible expense.

III. Amendments to the law on contributions for mandatory social security insurance

No obligation to pay contributions for social security insurance for fringe benefits

The latest amendments to the Law on Contributions for Mandatory Social Security Contributions (the "SSC Law") prescribe that Montenegrin employers are no longer required to pay social security contributions on in-kind benefits given to employees, such as the giving of goods, gifts, and other similar benefits, unless such benefits are given as compensation for unpaid salaries.

Maximum base for the calculation of social security contributions increased

The amount of the maximum annual base for social security contributions for 2012 is now increased to EUR 50,000. It is also prescribed that the Ministry of Finance will prescribe the terms and the procedure for the cessation of the payment of social security contributions, or the refund of the excess social security contributions paid during the year over the amount due on the maximal annual base prescribed by the law.

The amendments also clarify that a request for a refund of the excess social security contributions may be filed by employees for contributions due by the employees, and by employers for social security contributions due by the employer.

Tax base for the calculation of contributions for mandatory social security contributions clarified

The amendments now clarify that income subject to social security contributions on salaries is equal to the gross amount of salary including the salary for work performed, time spent at work, increased salary, compensation of salary and other personal income established by the law, collective bargaining agreement and employment agreement which is subject to salary tax. Under the earlier text of the SSC Law, it was not specified that the salary subject to taxation is the gross amount of salary. The minimal amount of income subject to social security contributions is equal to the minimal monthly base for the calculation of social security contributions prescribed by the law, as was the case under the earlier text of the PIT Law.

Tax base for the calculation of contributions for social security contributions for sole entrepreneurs changed

The amendments to the PIT Law have changed the tax base for the assessment of contributions for social insurance for sole entrepreneurs who pay tax on income from business activities on a lump-sum basis. The base is now equal to the lump-sum amount of income established by the Tax Authority for the purpose of the payment of personal income tax, instead of 50% of the average monthly salary in Montenegro as was the case under the earlier text of the PIT Law.

If you have any questions or concerns, please contact us on the following email address:

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