

Pursuant to Article 95 item 3 of the Constitution of Montenegro I hereby issue the

**DECREE PROMULGATING THE LAW ON HYDROCARBONS TAX**

I hereby promulgate the **Law on Hydrocarbons Tax passed** by the 25<sup>th</sup> Parliament of Montenegro at the eighth sitting of the first ordinary (spring) session in 2014 on 16 July 2014.

Number: 01-822/2  
Podgorica, 22 July 2014

The President of Montenegro  
Filip Vujanović

Pursuant to Article 82 item 2 of the Constitution of Montenegro and Amendment IV paragraph 1 to the Constitution of Montenegro, the 25<sup>th</sup> Parliament of Montenegro at the eighth sitting of the first ordinary (spring) session in 2014 on 16 July 2014, passed the

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**Law on Hydrocarbons Tax**

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**I BASIC PROVISIONS**

**Subject-Matter**  
**Article 1**

- (1) This Law introduces the obligation of payment of tax on profit from Upstream Operations related to Hydrocarbons (hereinafter referred to as the Hydrocarbons Tax).
- (2) Upstream Operations, referred to in paragraph 1 of this Article, shall encompass activities related to extracting Hydrocarbons from deposits, as well as the construction and use of facilities and appurtenant equipment required for Production and delivery of Hydrocarbons, including exploration, drilling of wells, Production, Transportation or use of oil and gas for purposes of Hydrocarbons Production and other activities related to Upstream Operations, except for Transportation of Hydrocarbons in bulk by rail, air, road or water.

**Application**  
**Article 2**

- (1) This Law shall apply to the Upstream Operations carried out:
  - 1) in the offshore of Montenegro to the extent that such upstream operations are carried out in the areas subject to the sovereignty, sovereign rights and

- jurisdiction of Montenegro, and/or Facilities located on the territory under the jurisdiction of Montenegro;
- 2) in Deposits located beyond the international boundaries or median line in relation to another state, to the extent of right to extraction of Hydrocarbons conferred to Montenegro by an international agreement;
  - 3) outside the Territory of Montenegro or areas referred to in item 1 of this paragraph, which concern the landing of Hydrocarbons to the land territory of Montenegro, as well as the performing of works or construction or use of Facilities for such purpose, subject to the right of Montenegro to impose taxes on such Upstream Operations in accordance with the international public law or an international agreement;
  - 4) within the boundaries of land territory, internal waters and territorial sea of Montenegro, which concern the Transportation of Hydrocarbons from the areas specified in items 1, 2, and 3 of this paragraph, as well as other activities related to loading and unloading Facilities as part of the Production or Transportation of such Hydrocarbons.
- (2) This Law shall also apply to activities, works, treatment and/or processing of Hydrocarbons in Facilities used for Production or Transportation in the areas referred to in paragraph 1 of this Article, disregarding if the Hydrocarbons are extracted from Deposits located in such areas.

### **Exclusion of Application of other Regulations**

#### **Article 3**

Provisions of the law governing the taxation of profit of legal entities shall not apply to income from Upstream Operations.

#### **Taxpayer**

#### **Article 4**

- (1) Taxpayer shall be a business organisation or a part of a foreign entity carrying out Upstream Operations under a Hydrocarbons Production Concession Contract, as well as other persons performing Upstream Operations in accordance with an international agreement.
- (2) Taxpayer referred to in paragraph 1 of this Article shall have the status of a large taxpayer pursuant to the law governing the tax administration.

### **Taxation of Income from Other Activities**

#### **Article 5**

Income generated by a taxpayer from other activities that are not subject to taxation under this Law, capital gains including transfer or assignment of the pertaining interest under the Hydrocarbons Production Concession Contract and income from capital shall be taxed in accordance with a law governing the taxation of profit of legal entities.

## Meaning of Terms Article 6

Terms used in this Law shall have the following meaning:

- 1) **Hydrocarbons** shall mean any kind of hydrocarbons occurring in their natural state in the subsoil or the seabed, in a liquid or gaseous state, as well as crude mineral oil, natural gasoline, natural gases, and other substances capable of being extracted together therewith from a Deposit;
- 2) **Deposit** shall mean an elementary and independent accumulation of Hydrocarbons within the Earth's crust, identified by exploration and confined by structural and stratigraphic boundaries;
- 3) **Exploration** shall mean operations of geological, geophysical or other forms of detailed surveys of the Earth's crust by applying an appropriate method aimed at establishing the presence of Hydrocarbons and characteristics of the Deposit, except for drilling a Well;
- 4) **Production** shall mean the operation of extracting Hydrocarbons from deposits, their separation and initial processing, preparation of oil or gas for Production, Transportation or storing, gas liquefaction, as well as bringing of Hydrocarbons to the terminals in Facilities located in the territory under the jurisdiction of Montenegro;
- 5) **Well** shall mean a borehole made in the subsoil by drilling performed for the purpose of penetrating Hydrocarbons bearing strata or for the Production, except for shallow drilling for seismic calibration purposes;
- 6) **Transportation** shall mean the shipment of Hydrocarbons by pipeline as well as the planning, preparation, construction, placing of pipelines, operation and use of a Facility for the purpose of Transportation;
- 7) **Hydrocarbons Production Concession Contract** shall mean a contract entered in writing between the Grantor and Concessionaire governing mutual rights and obligations for Exploration and Production of Hydrocarbons subject to the Law governing the Exploration and Production of Hydrocarbons (hereinafter referred to as the Law);
- 8) **Concessionaire** shall mean a business organisation which has acquired the right over the Exploration or Production by way of a Concession Contract, pursuant to the Law;
- 9) **Territory of Montenegro** shall mean onshore down to the lower part of the Earth's crust and the offshore area within internationally recognized borders of Montenegro in accordance with the public international law;
- 10) **Offshore** shall include internal waters, territorial sea, economic zone, and the epicontinental shelf of Montenegro and shall spread from the sea surface to the lower part of the Earth's crust, and other zone in accordance with the public international law;
- 11) **Installation** shall mean a floating, fixed or movable vessel, vehicle, watercraft, device, structure, plant, or equipment for the Exploration and Production of Oil or Gas except for a pipeline, vessel, vehicle or watercraft used for the purposes of transporting Oil or Gas in bulk;
- 12) **Facilities** shall mean one or more Installations, plants, structures, devices, pipelines or lines used for the Exploration, Production, Transportation or storage related to the Production of Hydrocarbons;

- 13) **Independent persons** shall mean purchasers and sellers who have no joint interests that could influence the agreed price of Hydrocarbons.
- 14) **Realisation of Hydrocarbons** shall mean disposing of Hydrocarbons with or without a consideration;
- 15) **Realisation of fixed assets** shall mean disposing of fixed assets with or without a consideration.

## II TAX BASE AND TAX RATES

### Tax Base Article 7

The base of the Hydrocarbons Tax shall be the difference of gross income generated through Upstream Operations and expenditures recognised in accordance with this Law.

### Income from Upstream Operations Article 8

- (1) Income from Upstream Operations shall be:
  - 1) Income generated from Production, Transportation, processing and/or sale or realisation of Hydrocarbons,
  - 2) Income from interest and other financial income, exchange rate differences and financial gains from Upstream Operations,
  - 3) Income from realisation of fixed assets acquired for use in activities pertaining to Upstream Operations;
  - 4) Market value of a fixed asset withdrawn from Upstream Operations;
  - 5) Monetary assets remaining on a special account for decommissioning (hereinafter referred to as Decommissioning Fund) after the Facilities' decommissioning process has been completed in accordance with the Law;
  - 6) Value of Hydrocarbons inventory/stocks.
- (2) Income for the purpose of paragraph 1 of this Article shall not be monetary assets resulting from settlements received for loss compensation to third parties due to cessation of Upstream Operations or decommissioning of Facilities.
- (3) Income for the purpose of paragraph 1 of this Article shall not be monetary assets resulting from realisation of the fixed assets destroyed due to fire or other accident, or expropriated, if the taxpayer reinvests such monetary assets within three years from the realisation of the fixed assets for procurement of new fixed assets of the same type.
- (4) In the case referred to in paragraph 3 of this Article, the taxpayer shall submit to the authority competent for tax affairs (hereinafter referred to as the Tax Authority) appropriate security instruments for reinvestment of monetary assets.

- (5) The Ministry competent for financial affairs (hereinafter referred to as the Ministry) shall stipulate a detailed procedure, types of security instruments and deadlines for providing security instruments referred to in paragraph 4 of this Article.

### **Upstream Operations Expenditures**

#### **Article 9**

- (1) Upstream Operations expenditures shall be capital costs, operating costs, funds paid into the decommissioning fund and financing costs.
- (2) Capital costs, referred to in paragraph 1 of this Article, shall be the costs resulting from purchase or other acquisition of Facilities for Production or Transportation of Hydrocarbons, including Installations and structures such as platforms, subsea installations or Facilities, terminals, umbilicals, required appurtenant equipment and other moveable property that makes an integrated part of, or is related to such Facilities, including also Exploration costs which are recognised in accordance with the Hydrocarbons Production Concession Contract.
- (3) Operating costs referred to in paragraph 1 of this Article shall be costs of wages of employees and other forms of work engagement related to the Upstream Operations, costs of consumables, costs of services as well as other costs that are recognised pursuant to the Hydrocarbons Production Concession Contract.
- (4) The funds paid into the Decommissioning Fund, referred to in paragraph 1 of this Article, shall be the funds paid on behalf of future expenditures for decommissioning of Facilities for Production, treatment, processing, or Transportation of Hydrocarbons.
- (5) Expenses incurred for healthcare, education, scientific, religious, cultural, sports, and humanitarian purposes, shall be recognized as expenses in the amount not exceeding 1% of the total income, except for expenses incurred by training needs for domestic personnel in institutions financed from public revenues pursuant to the Hydrocarbons Production Concession Contract.
- (6) All expenditures recognised in accordance with paragraphs 1 to 5 of this Article and Article 10 of this Law must be documented.
- (7) The Ministry shall adopt a detailed regulation for determining income referred to in Article 8 of this Law and expenditures referred to in paragraphs 1 to 5 of this Article and Article 10 of this Law.

### **Financing Costs**

#### **Article 10**

- (1) Net financing costs related to the performance of Upstream Operations incurred in respect of interest-bearing borrowings shall be financing costs within the meaning of paragraph 1 Article 9 of this Law.

- (2) Net financing costs referred to in paragraph 1 of this Article shall include expenditures for interest as well as the difference of currency gains and currency losses on the borrowings.
- (3) If currency gains exceed interest related expenditures and currency losses, such amount shall be net financial income and shall be deemed income in accordance with Article 8 paragraph 1 item 2 of this Law.
- (4) Interest and pertaining costs towards a creditor with the status of an affiliate shall be recognised against expenditures in the amount that does not exceed the costs of interest in the free market.

### **Not Recognised Expenditures Article 11**

The following shall not be recognised as expenditures:

- 1) Deductions in respect of depreciation of goodwill;
- 2) Losses or adjustments of value in respect of depreciation of fixed assets;
- 3) Fee for produced oil and gas for monthly extracted Hydrocarbons payable in accordance with the Law;
- 4) Annual fee for the area used under the Production Concession Contract payable in accordance with the Law;
- 5) Sales commission, discounts or costs of the transfer of Hydrocarbons between affiliates;
- 6) Expenditures incurred as a result of loss compensation to third parties arising out of cessation of Upstream Operations or decommissioning;
- 7) Expenditures in respect of settlements received for losses incurred in accordance with the Law;
- 8) Pecuniary fines and penalties related to the violation of Hydrocarbons Production Concession Contract or a special law;
- 9) Interest and penalties for untimely payment of liabilities;
- 10) Interest paid to non-residents, if paid at the rate higher than ordinary commercial rate.

### **Depreciation of Expenditures Article 12**

- (1) Capital expenditures referred to in Article 9 paragraph 2 of this Law shall be recognised at an annual rate of 20%.
- (2) Notwithstanding paragraph 1 of this Article, the expenditures referred to in Article 9 paragraphs 3, 4 and 5 and Article 10 of this Law shall be recognised in the year of their occurrence.
- (3) The first year for depreciation of expenditures referred to in paragraph 1 of this Article shall be the year of occurrence of such expenditure.

- (4) The Ministry shall stipulate in details the manner of depreciation of expenditures referred to in paragraph 1 of this Article.

### **Recognition or Carrying Forward Losses**

#### **Article 13**

- (1) Losses in respect of Upstream Operations resulting from recognised expenditures referred to in Articles 9 and 10 of this Law may be carried forward against profits from future accounting periods within the time period not exceeding 10 years and without interest calculated on the balance at the end of the tax period.
- (2) In case of joint business activities that resulted in a loss, the total uncovered loss referring to the Upstream Operations shall be recognised to the taxpayer in proportion to the taxpayer's share in the joint business activity, if such losses may not be established based on the documents.
- (3) In the event of status changes of the taxpayer who incurred a loss, the total uncovered loss related to Upstream Operations may be carried forward from such taxpayer to the acquiring party.

### **Determining Income from Upstream Operations**

#### **Article 14**

Income from the Upstream Operations referred to in Article 8 paragraph 1 items 1 and 6 of this Law shall be determined based on the contracted price or the tax reference price established in accordance with Article 15 of this Law (hereinafter referred to as the Reference Price) if the contracted price is different from the Reference Price.

### **Determining the Reference Price**

#### **Article 15**

- (1) Reference Price shall be a price at which Hydrocarbons could be traded between independent persons at a free market.
- (2) The state administration authority competent for Hydrocarbons affairs (hereinafter referred to as the Ministry of Economy), with previous consent of the Government of Montenegro, shall determine the Reference Price for Hydrocarbons extracted in the areas referred to in Article 2 of this Law, on quarterly bases by the 15<sup>th</sup> in a month upon expiry of each quarter and publish the same in the Official Gazette of Montenegro.
- (3) The Reference Price shall be determined based on the achieved and quoted prices for Hydrocarbons of the same or a corresponding type in the free market, with necessary adjustments for differences in quality, costs for Transportation to relevant markets, delivery date, payment date and other terms and conditions, as well as

based on achieved and quoted prices for Hydrocarbons products, with necessary adjustment for refining, and other comparable prices or valuations of Hydrocarbons that may be available.

- (4) In the process of determining the Reference Price, the prices achieved between affiliates or other elements that could influence determination of the lower level of contracted price than the price that is formed between independent persons in the free market shall not be used.
- (5) The Ministry of Economy with the consent of the Ministry shall stipulate a detailed procedure and manner of determining the Reference Price.

#### **Tax Rates Article 16**

- (1) The rate of the Hydrocarbons Tax shall be 54% of the tax base.

#### **Separate Accounting Records Article 17**

- (1) A taxpayer shall be obliged to keep separate accounting records in order to separately present the results from business activities pertaining to the Upstream Operations.
- (2) In accordance with paragraph 1 of this Article, the taxpayer shall be obliged to compile and submit separate financial statements pursuant to the law governing accounting and auditing.

### **III CALCULATING AND PAYING THE HYDROCARBONS TAX**

#### **Tax period Article 18**

- (1) Tax period for calculating the Hydrocarbons Tax shall be a financial year.
- (2) Financial year shall be a calendar year, except in case of liquidation or commencement of business activities during the year.
- (3) The Hydrocarbons Tax shall be calculated upon expiry of the financial year, or other tax period for tax assessment, based on the tax base generated during such period.

#### **Annual Tax Return Article 19**

- (1) Taxpayer shall be obliged to submit the annual tax return for the period for which the Hydrocarbons Tax is calculated to the Tax Authority.
- (2) The return referred to in paragraph 1 of this Article shall be submitted by no later than four months upon the expiry of the period for which tax is calculated.
- (3) In addition to the return referred to in paragraph 1 of this Article, the taxpayer shall submit audited financial statements in accordance with the law governing accounting and auditing.
- (4) The Tax Authority shall determine the amount of the annual Hydrocarbons Tax by way of a decision within 45 days as of the day of expiry of the deadline referred to in paragraph 2 of this Article.
- (5) The taxpayer shall pay the difference between the tax determined by a decision referred to in paragraph 4 of this Article and instalments paid for the relevant tax period, within 15 days as of the day the decision is delivered.
- (6) If a taxpayer has entered into several Hydrocarbons Production Concession Contracts as the same legal entity, it shall be obliged to lodge a single annual tax return.

### **Provisional Tax Return Article 20**

- (1) Taxpayer shall be obliged to submit to the Tax Authority a provisional return for calculation of the instalment Hydrocarbons Tax, including estimated income for the current tax period, within 30 days as of commencement of Production or Transportation of Hydrocarbons, or generation of income from Upstream Operations.
- (2) The taxpayer referred to in paragraph 1 of this Article shall be obliged to lodge the return referred to in paragraph 1 of this Article to the tax authority by 31 January of the current year.
- (3) The tax authority shall determine the amount of instalment by means of a decision within 15 days of the day the return referred to in paragraphs 1 and 2 of this Article is lodged.
- (4) The Ministry shall stipulate the form and substance of the provisional tax return referred to in paragraph 1 of this Article and annual tax return referred to in Article 19 of this Law.

### **Instalment Payment of Hydrocarbons Tax Article 21**

- (1) Taxpayer shall pay the Hydrocarbons Tax quarterly during a year in form of instalments based on the decision referred to in Article 20 of this Law.
- (2) The instalment referred to in paragraph 1 of this Article shall be paid by the 15<sup>th</sup> day of the month following the expiry of each quarter.
- (3) The instalment of the paid tax referred to in paragraph 2 of this Article shall be considered a credit against liabilities under the annual tax return.
- (4) If the taxpayer pays more tax in the form of instalments during a year than it is obliged to pay under the annual tax return, the excess paid tax shall be refunded upon his/her request or shall serve as an instalment for the following period.

### **Belonging of the Hydrocarbons Tax Revenues** **Article 22**

Revenues from the Hydrocarbons Tax shall belong to the Budget of Montenegro and to the Hydrocarbons Fund established in accordance with a special law, in proportion 15:85.

The Government of Montenegro shall submit a Proposal Law on Hydrocarbons Fund to the Parliament of Montenegro no later than 31 December 2014.

## **IV CONFIDENTIAL INFORMATION AND APPLICATION OF OTHER REGULATIONS**

### **Confidential Information** **Article 23**

- (1) Information that the tax authority has about a taxpayer shall be deemed confidential and may be made available to the competent state authority in accordance with law.
- (2) A competent state authority shall be obliged to keep the received information confidential in accordance with paragraph 1 of this Article.
- (3) Tax authority may provide information regarding a taxpayer to a competent authority of a foreign country upon its request, provided there is reciprocity, if confidentiality of information is ensured in such country at least to the level of protection stipulated by this Law, or to other authority in accordance with an international agreement.
- (4) Tax authority may determine conditions and restrictions in using information referred to in paragraph 3 of this Article.
- (5) The Ministry may stipulate which information is considered confidential in terms of paragraph 1 of this Article and the manner for providing such information.

## **Application of Other Regulations Article 24**

The provisions of the law governing the tax procedure shall apply accordingly to the relations not specifically governed by this Law (inspection/control, appeal procedure, enforced collection, interest and other).

## **V PENALTY PROVISIONS**

### **Article 25**

- (1) A pecuniary fine ranging from 10,000 euro to 40,000 euro shall be imposed for an offence on a legal entity if it:
- 1) Fails to lodge with the tax authority an appropriate security instrument referred to in Article 8 paragraph 3 of this Law for reinvestment of monetary assets (Article 8, paragraph 4)
  - 2) Fails to keep separate accounting records referred to in Article 17 of this Law for separate presentation of results of business activities pertaining to the Upstream Operations and fails to compile and submit separate financial statements (Article 17);
  - 3) Fails to lodge the annual tax return with the competent tax authority within four months from expiry of the period for which tax is calculated and fails to submit financial statements along with the return (Article 19, paragraphs 1, 2 and 3);
  - 4) Fails to pay the difference between the annual tax assessed by the decision referred to in Article 19 paragraph 4 of this Law and paid instalments for the tax period referred to in Article 18 of this Law within 15 days from the day of delivery of the decision (Article 19, paragraph 5);
  - 5) Fails to lodge the provisional return for the calculation of the instalment Hydrocarbons Tax with the tax authority within 30 days from the day of commencement of Production or Transportation of Hydrocarbons, or generation of income from Upstream Operations (Article 20 paragraph 1);
  - 6) Fails to lodge the provisional return for calculation of instalment Hydrocarbons Tax referred to in Article 20 paragraph 1 of this Law to the tax authority by 31 January of the current year (Article 20 paragraph 2);
  - 7) Fails to pay tax quarterly in the form of instalments by the 15<sup>th</sup> in the month following the expiry of each quarter (Article 21 paragraph 2).
- (2) A responsible person in the legal entity shall also be imposed on a pecuniary fine ranging from 3,000 euro to 4,000 euro for the offence referred to in paragraph 1 of this Article.

## **VI TRANSITIONAL AND FINAL PROVISION**

**Entitlement to Revenues until the Establishment of the Fund**  
**Article 26**

By the time the fund referred to in Article 22 of this Law has been established, the revenues in respect of Hydrocarbons shall belong to the Budget of Montenegro, in their full amount.

**Deadline for Adoption of Enabling Regulations**  
**Article 27**

Enabling regulations for implementation of this Law shall be adopted within 12 months as of the day this Law enters into force.

**Entering into Force**  
**Article 28**

This Law shall enter into force on the eighth day following the day of its publication in the Official Gazette of Montenegro.

Number: 16-02/14-1/10  
EPA: 414 XXV  
Podgorica, 16 July 2014

25<sup>th</sup> Parliament of Montenegro  
The Speaker of the Parliament  
Ranko Krivokapić