

Instruction on the determination of transfer prices of transactions

Tax Alert

November 2022



The Montenegrin Ministry of Finance published the Instruction on the determination of transfer prices of transactions ("Official Gazette of Montenegro", No. 121/22 of 02.11.2022, hereinafter: "Instruction") on November 2nd 2022.

Namely, Montenegro introduced more detailed transfer pricing rules by amending the Law on Corporate Income Tax in January 2022 (hereinafter: "the Law"). The Instruction prescribes the method of determining the transfer prices of transactions and the contents of transfer pricing documentation. Like the Law, the Instruction stipulates the application of seven methods for determining the compliance of the transaction price with the arm's length principle, namely:

1. Comparable Uncontrolled Price Method;
2. Cost Plus Method (cost plus gross margin method);
3. Resale Price Method;
4. Transactional Net Margin Method;
5. Profit Split Method;
6. Any other method that can be used to determine the compliance of the transaction price with the arm's length principle, if it is not possible to use the above listed methods;
7. A combination of above listed methods (if necessary).

Each of the methods is explained in more detail in the Instructions, as well as the circumstances in which they are applied. When choosing a method, it is also possible to apply an aggregated approach for a larger number of individual transactions, i.e. a segregated approach in the case of complex transactions, where one transaction includes a larger number of individual transactions.

Pursuant to the provisions of the Instructions, transfer pricing documentation should contain:

1. Analysis of the Group of related parties,
2. Industry analysis, which includes a description of the activities in which business is conducted,
3. Functional analysis in which related party transactions should be described and defined in detail, including the functions they perform, the assets they engage and the risks they assume,

4. Selection of appropriate method for determining compliance of transfer prices with arm's length prices,
5. Conclusion – firstly, the amount of transfer pricing adjustments for individual transactions with each related party is determined, and subsequently by summing the adjustments amount, the total transfer pricing adjustment amount per each related party is calculated,
6. Appendix that provides an overview of the data used to determine the arm's length price or the price range determined in accordance with the arm's length principle.

The Law (Article 38 c) provides for the preparation of documentation in a simplified form if the amount of transactions with a related party that taxpayer realized do not exceed the value of EUR 75,000 in the year for which the tax return is submitted. In that case, the documentation should contain the following:

1. description of transaction,
2. transaction value and
3. a related party with whom the transaction was realized.

Regarding intercompany loans, we remind that the Law foresees the possibility of applying the arm's length interest rates prescribed by the Ministry of Finance or general rules on determining the price of transactions in accordance with the arm's length principle (by using one of the prescribed methods).

Transfer pricing documentation should be submitted by large taxpayers along with the tax return (other taxpayers are required to possess transfer pricing documentation at the time of submitting the tax return). The deadline for submitting the tax return is three months from the end of the period for which the tax is calculated. Exceptionally, until 2027 the deadline for submitting (i.e. possessing) transfer pricing documentation is June 30 of the current year for the previous year (for the financial year 2022 the deadline is June 30, 2023).

If you have any questions or you need assistance of our professionals, please contact us at tax@kpmg.rs.

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