

Serbia: Lending and Tax Issues

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1. Regulation of lending

Banking monopoly rules. There is a fairly strict banking monopoly law limiting lender activities in Serbia. However, there are methods of lending available to foreign lenders.

Regulatory distinction between loans and credits. Serbian law distinguishes between the credit agreement (*ugovor o kreditu*) and the loan agreement (*ugovor o zajmu*). A credit is a banking transaction. Only a bank licensed by the National Bank of Serbia may provide a credit. A loan is a civil law transaction. Any natural or legal person may provide a loan, without the need for any licence. However, loans may only be carried out on an ad hoc basis and not as the entity's main business activity.

Loans and credits by foreign lenders. Foreign lenders may grant a loan or a credit to a Serbian legal entity, but not to an individual. There are no restrictions on this activity if the loan or credit is granted from outside Serbia. A foreign lender intending to engage in credit transactions from within Serbia must set up a local subsidiary and obtain a licence from the National Bank of Serbia.

Loans by a Serbian legal entity. No Serbian legal entity may grant a loan to a non-resident. There are certain narrow exceptions to this, but these are generally not relevant to commercial transactions.

Usury laws. The Law on Obligations contains usury provisions. It purports to prohibit excessively high interest rates and states that a special law should be enacted to set a cap on interest rates. No special law has ever been enacted. However, the courts are still able to attack excessively high interest rates by applying the general legal principle on equality of mutual consideration, contained in the Law on Obligations. A contract would be deemed void if a person gains an unfair and manifestly disproportionate advantage for itself or for a third party by exploiting the state of need or severe material hardship of another person or that person's dependence or lack of experience. Theoretically, this provision also applies to commercial relations. In practice, however, courts rarely interfere with an interest rate agreed between two commercial parties.

Other regulatory issues.

Consents. All cross-border loans and credits and security arrangements must be registered with the National Bank of Serbia as a condition to drawdown. The minimum repayment period for a loan or credit taken by a Serbian resident from a foreign lender is 12 months plus one day from the drawdown. No foreign lender may make any loan or credit to a Serbian natural person in Serbia.

Security. A Serbian legal entity may not grant security to a foreign lender for a loan taken by a foreign resident (including its parent) (subject to certain narrow exceptions of no general relevance). There is otherwise no restriction on a foreign lender holding the benefit of security created by a Serbian entity over assets in Serbia in relation to its own debt.

Regulatory. The Serbian supervisory regime relating to banking activities is detailed and covers:

- capital adequacy;
- control of ownership and management, including notification requirements;
- foreign exchange risk;
- large exposures;
- liquidity; and
- money laundering.

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2. Tax issues

This section provides a general overview of withholding tax issues in Serbian lending transactions.

Withholding taxes.

On interest. Interest paid to a foreign lender by a Serbian borrower is subject to a withholding tax at the rate of 20%, unless otherwise stipulated by a double tax treaty between Serbia and the country of the foreign lender.

On interest on intra-group loans. Interest on intra-group loans is subject to a withholding tax at the rate of 20% for payments to foreign members of the group. Serbian companies which receive interest will have that income taxed at 10% under corporate income tax rules. Rules on transfer pricing and thin capitalisation will also apply. There are no exemptions on intra-group lending available.

On dividends. Dividends received by a non-resident legal entity from a Serbian legal entity are subject to a withholding tax at the rate of 20%, unless otherwise stipulated by a double tax treaty.

Dividends received by a non-resident natural person from a Serbian legal entity are subject to 10% withholding tax, unless otherwise stipulated by a double tax treaty.

On liquidation proceeds. Liquidation proceeds (on a voluntary liquidation or winding up) are taxed as capital gains, at the rate of 20%, unless otherwise stipulated by a double tax treaty.

On guarantee and letter of credit fees. A company may pay guarantee or LC (letter of credit) fees to a non-resident without triggering a withholding or similar tax.

On payments under a guarantee. A guarantor may pay out under a guarantee to a foreign beneficiary without triggering a withholding or similar tax.

Stamp duty. No stamp duty, documentary tax or notarial fee is payable on the execution of the credit loan agreement or on enforcement of a credit or loan agreement or a guarantee (apart from court administrative fees payable in enforcement proceedings).

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3. Exchange controls

All cross-border loan and credit agreements and their security arrangements must be registered with the National Bank of Serbia as a condition to drawdown. There are some foreign exchange restrictions. These include a minimum repayment period of 12 months plus one day from drawdown for a loan or credit taken by a Serbian resident from a foreign lender.

No foreign lender may make any loan or credit to a Serbian natural person in Serbia.

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4. Lender liability

There is no established concept of "big pocket" liability in Serbia. The theory of piercing the corporate veil is included in general corporate law. This makes shareholders personally liable for the obligations undertaken by the company if they have misused the company for illegal and fraudulent purposes or disposed of the company's assets as their own. There is, in theory, a general rule on tort liability in specific circumstances, whereby a wealthy entity may be held liable for damage caused by a related entity. The main heads of lender liability are:

Breach of obligation to lend. The terms of the loan commitment should be examined and ordinary contract law applied as to the commitment and its termination. There are no special rules enabling a lender to terminate a credit agreement and refuse to make funds available. However, Serbian banks regularly include in their loan or credit agreements a unilateral right to cancel the loan or credit. Legal experts consider that this practice could be challenged, at least in a situation where cancelling the loan or credit is not justified on objective grounds. The general rule of contract law is that a party cannot unilaterally withdraw from a binding agreement. However, there is no published court case on the issue.

Abusive credit. There is no concept of abusive credit in Serbia whereby a bank is liable to third parties by continuing to give credit to an insolvent

debtor without informing the third parties of the situation and thereby, it is alleged, inducing false credit.

Credit references. In Serbia, credit references are issued by the Credit Biro, a unit of the Association of Serbian Banks, a legal entity regulated by the Serbian Law on Banks. There are no explicit rules or case law on liability for credit references.

Control of borrower. There is no explicit law, and no published case law, on a bank's liability on the grounds of intrusive interference in management.

Lender as adviser. There is no explicit law on this issue. However, where a lender holds itself out as advising the borrower on the suitability of a credit or loan or transaction to be financed by its credit or loan, it could be held liable for negligent advice based on general laws on tort liability.

Misrepresentation. A lender could incur liability for misrepresentation in accordance with general law.

Environmental damage. Theoretically, a lender will not generally be liable for environmental damage simply as a result of holding the benefit of security over land or property where environmental damage occurs. However, if a lender takes possession or becomes the owner of the title to the land during enforcement proceedings, it could be held liable for environmental damage. Mortgages over land and property are enforced typically by auction or private sale, and therefore it is extremely unusual for a lender to take possession. A lender could incur liability for environmental damage if it acquires, in the context of enforcement of security, ownership title over land or a production facility or similar real estate which causes damage or pollution of the environment. There are no rules or precedents on lender liability in the context of financing an environmentally damaging activity.

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