



Ministry of Finance of Georgia



Tax Reforms in Georgia

April 12, 2011

Country Overview

Area	69,700 sq km
Population (beginning of 2009)	4,385.4 thousand
Population (beginning of 2010)	4,436.4 thousand
Birth Rate (per thousand population) in 2009	14.4%
Mortality rate (per thousand population) in 2009	10.6%
Life expectancy*	
UK	80 years
US	78 years
Georgia	77 years
Romania	74 years
Turkey	72.5 years
Official language	Georgian
Literacy	100%
<i>Population with at least secondary education (1-12 grades) (% , ages 25 and older)</i>	91%
<i>Secondary enrolment ratio 2001-09 (% of secondary school-age population)</i>	90%
<i>Ratio of Population with higher education (% , ages 25 and older)</i>	29%
Capital city	Tbilisi
Currency (code)	Lari (GEL)
GDP 2010 (estimate)	US\$ 11.7 bln
GDP real growth rate 2010	6.4%
GDP per capita 2010 (PPP)	US\$ 5,057
Headline CPI Inflation 2010 (period average)	7.1%
Non-food CPI Inflation 2010 (period average)	2.7%
US\$ - GEL 2010 (period average)	1.78
External Public Debt to GDP 2010**	33.6%



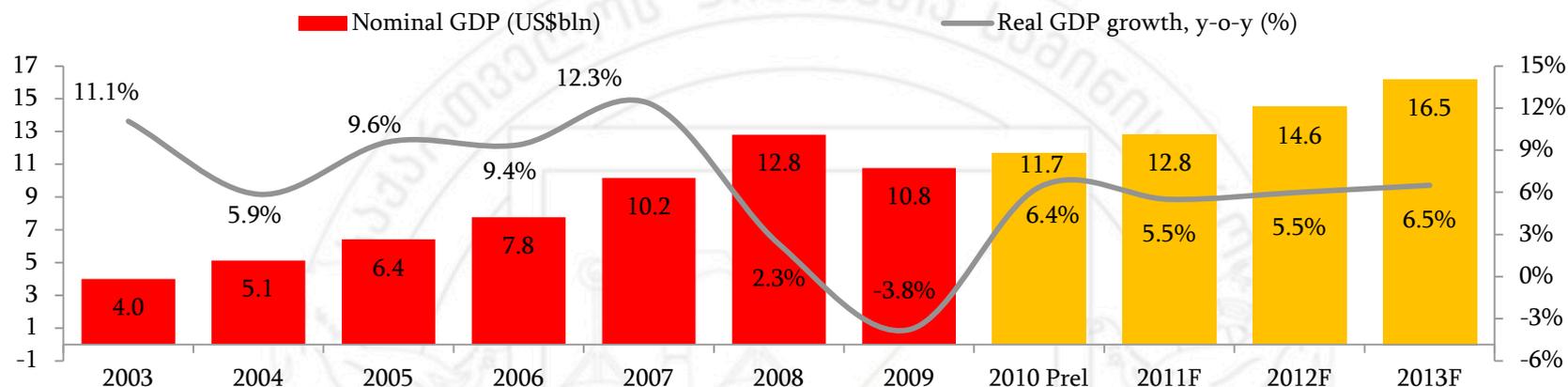
Source: Geostat, MOF, NBGsy

* Source: The World Factbook

** Includes exclusive liabilities of NBG to the IMF

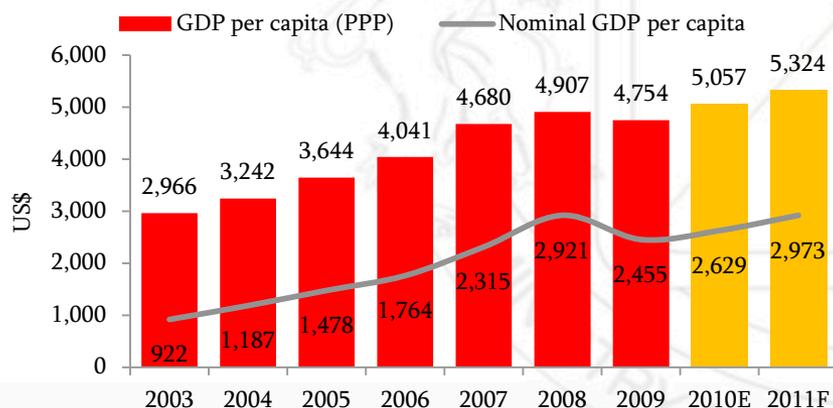
Reform Driven Economic Success

GDP



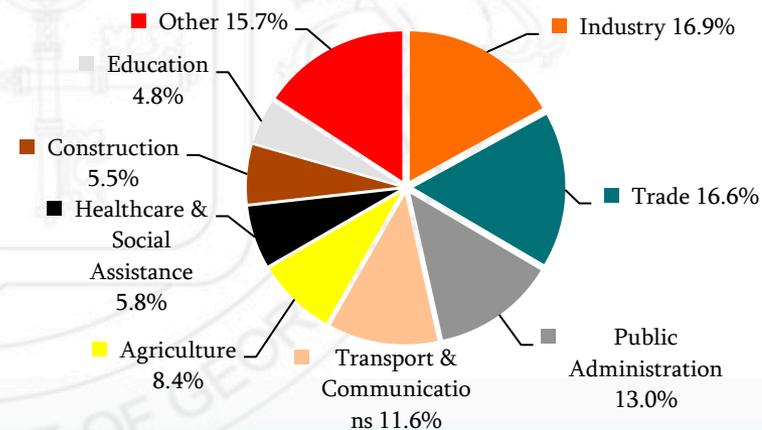
Source: Geostat

GDP Per Capita – PPP and Nominal



Source: Geostat, IMF

Components of Nominal GDP* (2010 E)



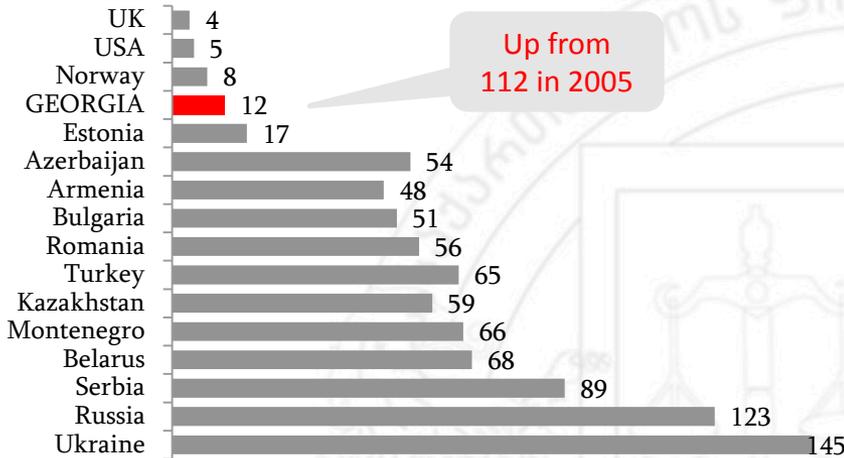
* Calculated using nominal GDP (preliminary) at basic prices

Source: Geostat

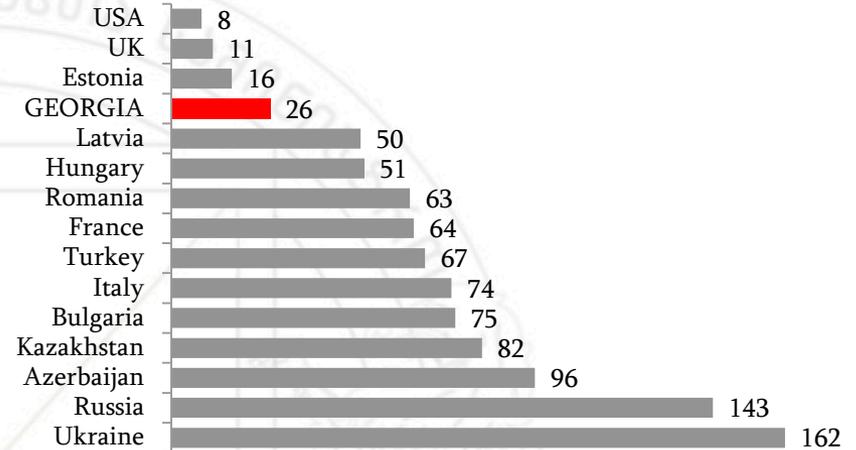


Reforms - Creation of Favourable Market Environment

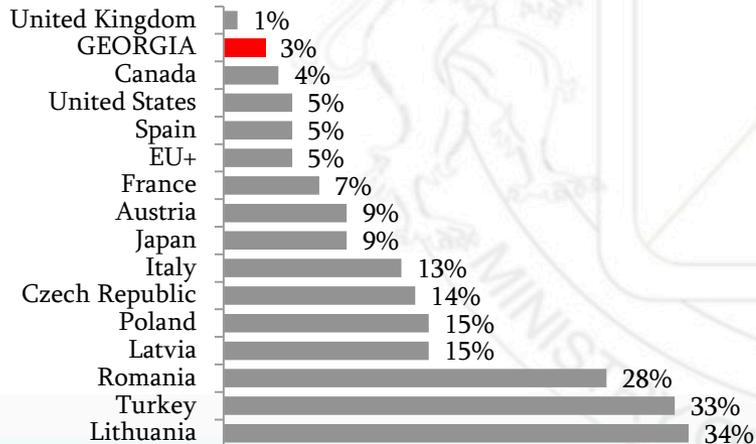
Ease of Doing Business, 2011 (WB-IFC Doing Business Report)



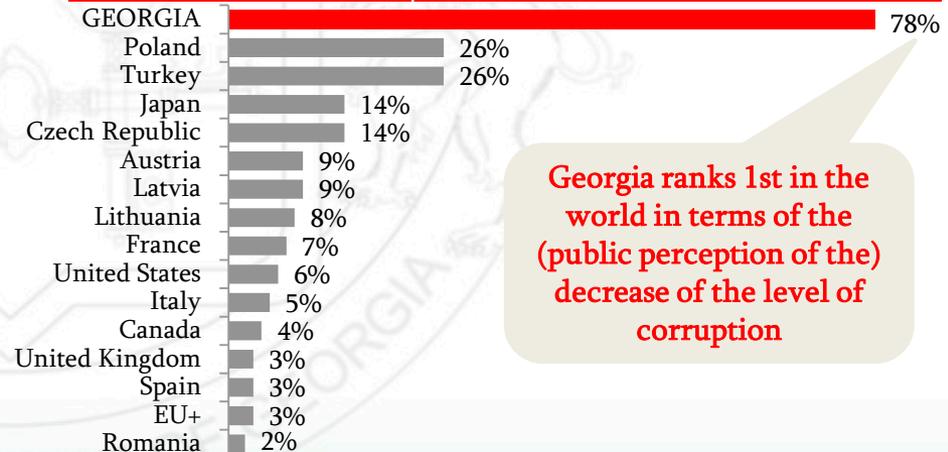
Economic Freedom Index, 2010 (Heritage Foundation)



TI 2010 Global Corruption Barometer: % admitting having paid a bribe within the last 12 month



TI 2010 Global Corruption Barometer: % of the surveyed claiming the corruption level has decreased



Georgia ranks 1st in the world in terms of the (public perception of the) decrease of the level of corruption



One of the Best Low-Tax Jurisdictions

	'04A	'05A	'06A	'07A	'08A	'09A	'10A
Number of Taxes	21	7	7	7	6	6	6
VAT	20%	20%	18%	18%	18%	18%	18%
Income Tax	12-20%	12% flat	12% flat	12% flat	Social Tax + Income Tax 32%	Social Tax + Income Tax 25%	20%
Social Tax	33%	20%	20%	20%	-	-	-
Corporate Profit Tax	20%	20%	20%	20%	15%	15%	15%
Dividend & Interest Income Tax	10%	10%	10%	10%	10%	5%	5%

- No payroll tax or social insurance tax
- No capital gains tax
- No wealth tax, inheritance tax or stamp duty
- Foreign-source income of individuals fully exempted
- Tax rates reduction timetable has been further accelerated in 2008

Note: since 2005 7 taxes were left out of 22 and from 2008 only 6 are imposed

Tax Reforms



- Phase I: 2004-2007
 - Fight against corruption
 - Eliminating red tape
 - Deep cut
 - Basic institutional changes
- Phase II: 2007-2009
 - Improving institutional capacity
 - Implementing collection enforcement reforms
 - Further reduction of tax burden
- Phase III: 2010-2011
 - Deep and comprehensive policy reform
 - Finishing customs reforms
 - Prioritizing services
 - Sharp reduction in tax compliance costs through IT enhancement



Tax Reforms Phase 1

- Drastically reduced formal tax burden (elimination of 15 type of taxes, lowering the rates and leaving them all flat)
- Removing all unnecessary and ineffective intervention from the Government into private businesses;
- Adoption of simple and fair rules of play and warranty its follow up from every single entity
- Bringing tax and customs agencies under the ministry of finance
- Phase I resulted into tax collection growth from the budget tax revenues of 12% to GDP in 2003 to 21.6% to GDP at end of 2007



Tax Reforms Phase 2

- Institutional transformation – creation of the Revenue Service
- Upgraded infrastructure – major renovation of the customs checkpoints and tax service centers
- Setting up comprehensive IT solutions for tax collection – creation of taxpayers united database (tax+customs), ASYCUDA, etc
- In 2008 corporate income tax reduced from 20% to 15%
- Payroll taxes (PIT and social tax) merged into one and W.A. tax rate reduced from 27% to 25%
- In 2009 reforms carried out towards reduction of tax burden:
 - Income Tax rate reduced from 25% to 20%
 - Tax rates for dividends and interest payments reduced from 10% to 7.5%
 - Creation tax free regimes for industrial zones and warehouses

Tax Reforms Phase 3



- New tax code based on the best international practices;
- Introduction of internationally accepted methods and practices;
- Introduction of different taxation regimes for taxpayers according to their needs - SMEs;
- Further elimination of bureaucratic barriers;
 - Sharp reduction in tax compliance costs through IT enhancement – www.rs.ge – e-services
 - Final shape of Georgian customs – risk based, minimal human interference, streamlined clearance (10 minutes rule)



Effective Management and Improved Administration

Effectively functioning public institutions and rule of law led to a dramatic reduction of informal activities

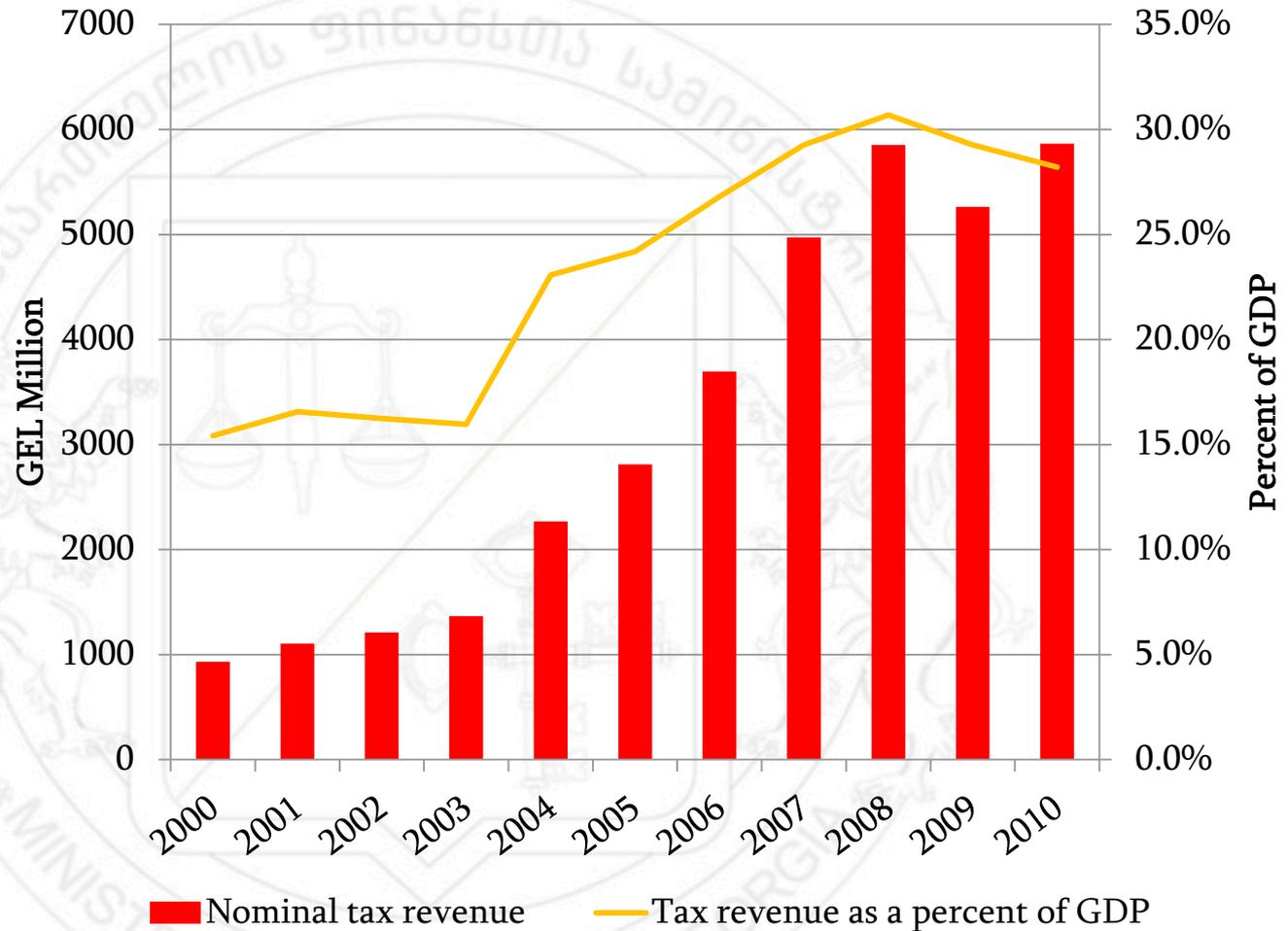
	Before Tax Reform	After Tax Reform
Number of taxes	22	6
Potential tax revenue as a percent of GDP	40-45%	28-30%
Actual tax revenue as a percent of GDP	15.6%	23.4%
Compliance Rate	35%	78-85%

Note: *Compliance Rate (Actual tax revenue/Potential tax revenue) increased due to Tax Code legislation, improving tax administration and reduced corruption level in tax services, decreased inefficiency.*

Effective Management and Improved Administration



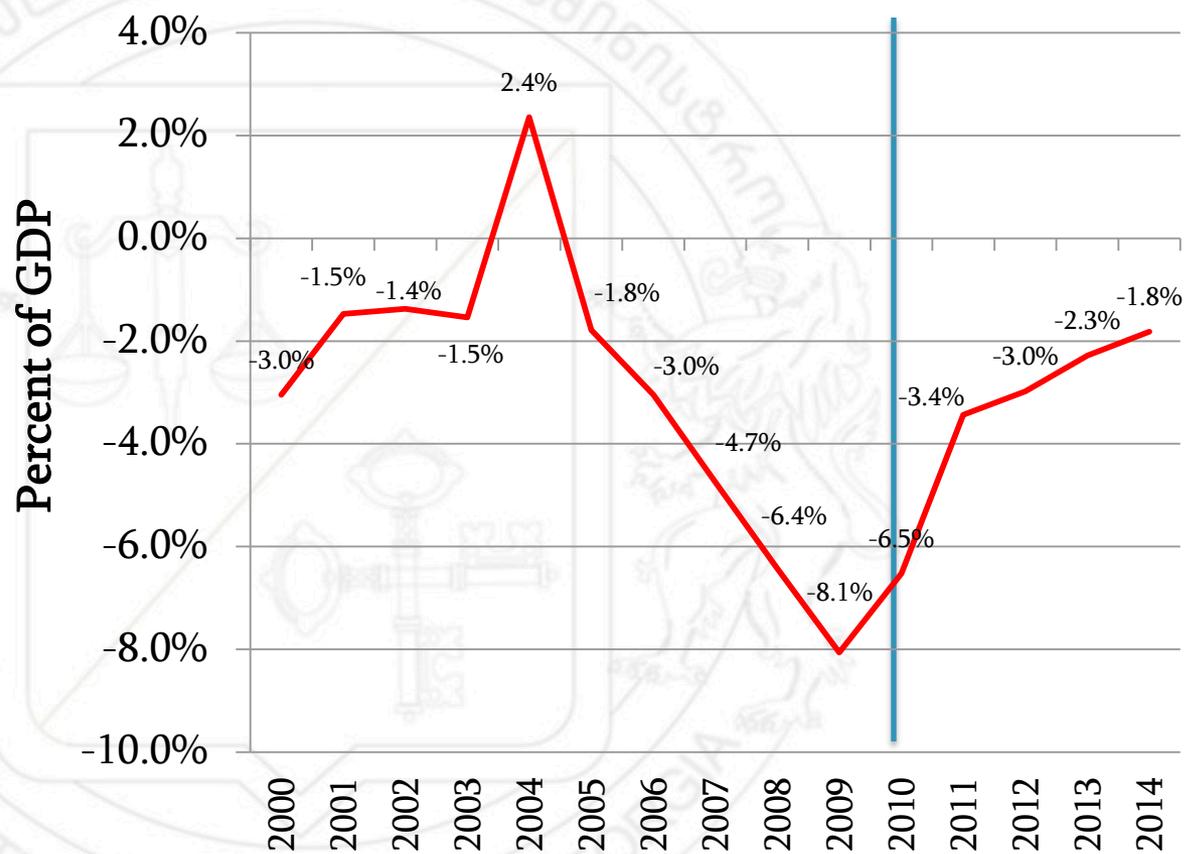
At the same time better administration and simplified business regulations provoked rapid growth of tax revenues



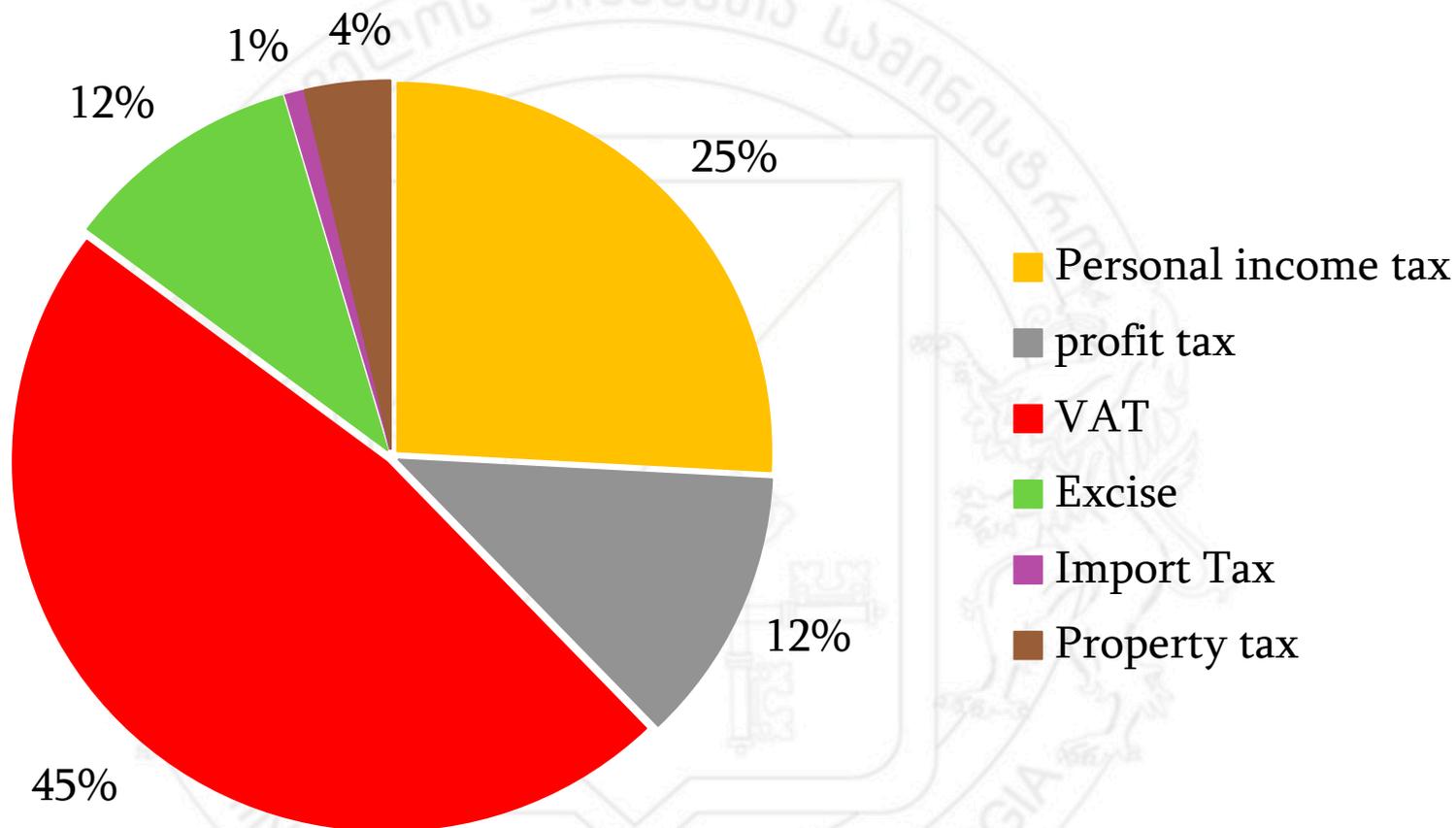
Fiscal Challenges

Conventional deficit (cash)

- Financial crisis coupled with Russian intervention resulted economic slowdown and expansion of budget deficit
- Our challenge remains to shift back the deficit on sustainable level by increasing tax base and moderating expenditure side



Composition of Tax Revenues Year 2010





Recent Innovations for Taxpayers

- Electronic Filing System implemented in 2008 and significantly improved in 2009
- All declarations and invoices are available in electronic form
- Registration in the system is based on taxpayer's request

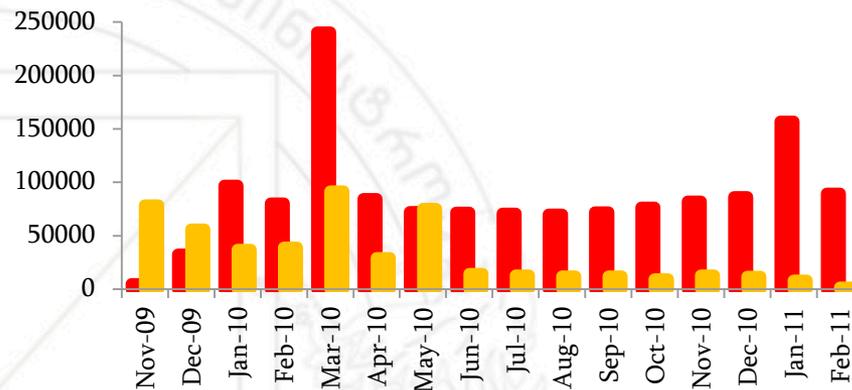
Tax Administration

Compliance Facilitation and Services

- Robust e-filing and e-payment systems
- Unified Cards for Customs and Tax Liabilities
- Principle of “Good Faith”
- Special Treatment of Micro and Small businesses
- Electronic VAT Invoices
- Electronic Administration System
 - Risk Based Selection of Taxpayers for Control
 - Electronic Assignments for Tax Officers
 - Electronic Performance Monitoring
- Risk Based Tax Audit
- Advance Ruling
- Accelerated Services
- Personal Tax Agent

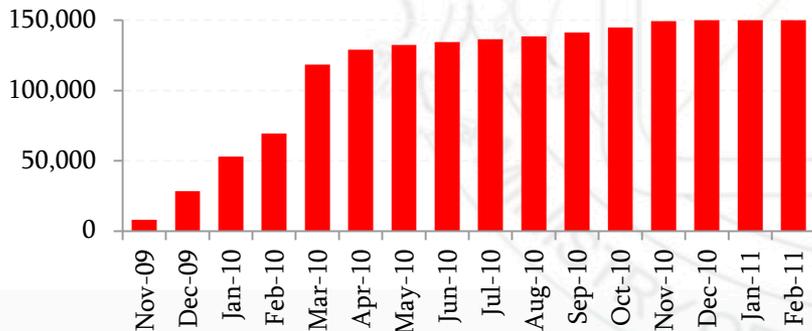
Monthly Declaration Statistics

■ Number of e-filings ■ Number of hard copy declarations

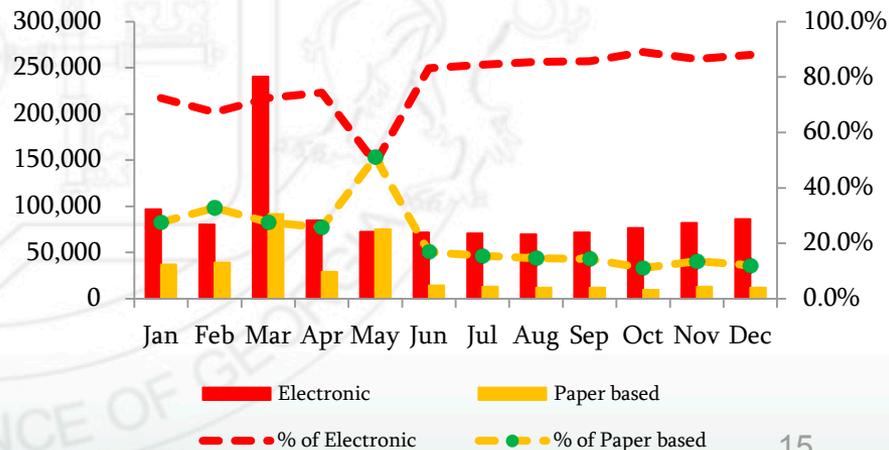


e-filing: Number of Registered Users

■ Number of Registered Users



e-filing vs. hard copy declarations





Purpose of the New Tax Code

The new tax legislation will simplify Doing Business in a following ways:

- Increase public trust towards Tax System;
- Formation of Stable and Sustainable Tax environment;
- Encouraging business legalization;
- Simplification of legal Provisions – Removing ambiguities;
- Reduction of Tax Compliance burden – Simplification of Tax Administration;
- Evenly distribution of tax burden;
- Using the best international tax practices, EU directives.



Unification of tax and customs codes

- Incorporated Tax and Customs Code unifies taxpayers tax and customs assets/liabilities, by which companies can transfer excess amount available on tax card to cover customs liability and contrary;
- Incorporated Tax and Customs Code will be more Systematic & User-Friendly
 - Simplified Reporting Procedures, especially by E-filing
 - Consolidated Tax Profile for Customs & Tax Issues
 - Less Bureaucratic System to Navigate
 - More Fair Regulation Implemented
 - Quicker Resolution to Administrative Issues
 - Easy Resolution to Overpayments
 - More Flexibility in Managing Liabilities and Cash Flows
 - Reduces Administrative Burden of Compliance
 - Reduce Taxable Income & Pay less Taxes

Customs Clearance Zone (GEZI)



- Customs Clearance Zone (GEZI) is a large clearance centre - unprecedented for Georgia, covering several hectares with special parking area for hundreds of trucks.
- It's possible to serve simultaneously an unlimited number of importers within an hour instead of days 24 hours in a week.
- For clearance of the goods the importer will not have to hire a broker, agent/declarant or other intermediary and incur high costs for their service.
- It is possible to postpone the service fee payment for 5 days upon clearance of the goods in the customs clearance zones. The fees have been halved in comparison to existing ones.

Customs Risk Management



- New system of declared goods' checks implies risk-based customs control mechanism which greatly diminishes time needed for customs clearance of cargo.
- There were higher chances of corruption before as 100% of goods were physically examined by a customs officer.
- Now the customs risk management software decides which goods have to be checked based on predetermined selection criteria. Therefore, importers need only 1 hour to go through all customs clearance procedures.
- Customs risk management system eliminates any chance of concluding deals between a customs officer and an importer and this is an effective mechanism against corruption. It also saves administrative resources.
- Goods go through 4 different color corridors (program uses 4 colors: blue, green, red and yellow for different types of customs control) – almost the same approach is used for human movement.
- There are several risk profiles in the system in order to prevent import of non-declared goods, manipulation with HS codes and to protect intellectual property rights.
- Under Customs Risk management system it is possible to offer simplified customs clearance procedures to organizations associated with low customs risk such as government agencies and diplomatic organizations.

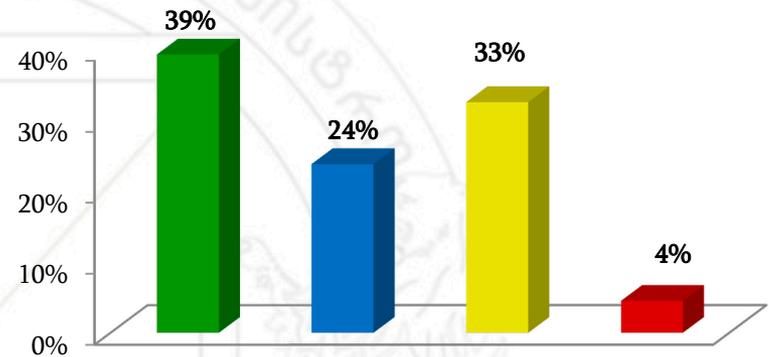
Color corridors selected by customs risk management software

Relevant color corridors selected by customs risk management Software for each customs regime
(1st quarter of 2011)

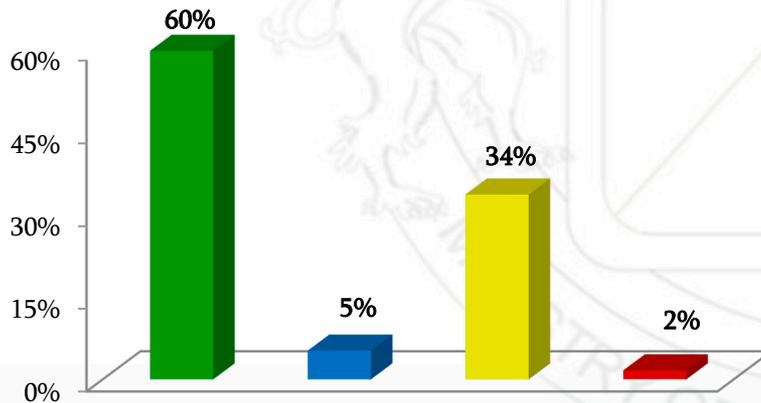
Meanings of Color Corridors

- Green corridor - *Immediate release without examination*
- Yellow corridor - *Documentary check*
- Red corridor - *Physical examination on of goods and documents*
- Blue corridor - *Examination at a later stage (post audit)*

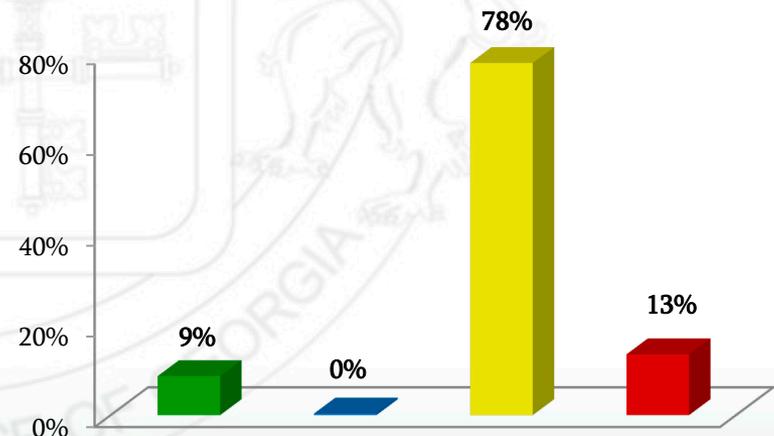
Import



Export



Warehouse



Informational Technology Zones



- Persons involved in IT activities have a right to apply for the status which will be awarded in no later than 10 business days in case certain requirements are met.
- Tax benefits apply to the Provision of Services outside of Georgia by a person of the virtual zone who is exempt from:
 - ✓ *corporate profit tax*
 - ✓ *VAT*
 - ✓ *export duties*
- Application for a status of a IT zone person must be submitted electronically at vz.mof.ge



Free Industrial Zones

- Free Industrial Zones is a unique opportunity for businesses to process, produce and export goods with a minimum tax burden.

Benefits include:

- exemption from corporate income tax, interests and dividends withholding taxes, VAT on exports, property tax and some other tax benefits
- With Georgian Free Trade Agreements, one can export goods free of trade barriers to global markets consisting of more than 350 million consumers;
- From Georgia to EU markets one can export more than 7,200 goods free of any trade barriers under the GSP+ (Globalized System of Preferences) arrangements.
- Two Free Industrial Zones have already been established in Georgia – Kutaisi Poti Free Industrial Zones



Free Warehouse Company

- The Free Warehouse Company, from a taxation perspective, is designed as an integral logistical unit for international transit companies.
- This Free Warehouse Enterprise categorization can be effectively used by international cargo companies, regional large network distributors and any company desiring to transport goods between Central Asia and global markets in the fastest and least costly manner possible.

Tax Benefits include:

- Exemption from corporate income tax applied to income received from re-exporting goods from free warehouses via the Free Warehouse Company;
- Exemption from VAT on the supply of goods by a Free Warehouse Company to a VAT payer in a free warehouse.



International Financial Company

- Companies can improve their tax effectiveness by obtaining the special status of an international financial company.
- International Financial Company is a financial institution carries out most of its services with parties outside of Georgia and its activities are tax exempt.
- Companies involved in providing financial services such as Wealth management, Asset management, Financial intermediation and other similar activities can effectively use the status and privileges of an International Financial Company.

Corporate income tax exemptions apply to:

- Profits received from financial services provided by an International Financial Company;
- Gains from sale of securities issued by an International Financial Company
- Dividends paid by an International Financial Company.



ADVANCE RULINGS

Tax authority issues 2 types of advance rulings:

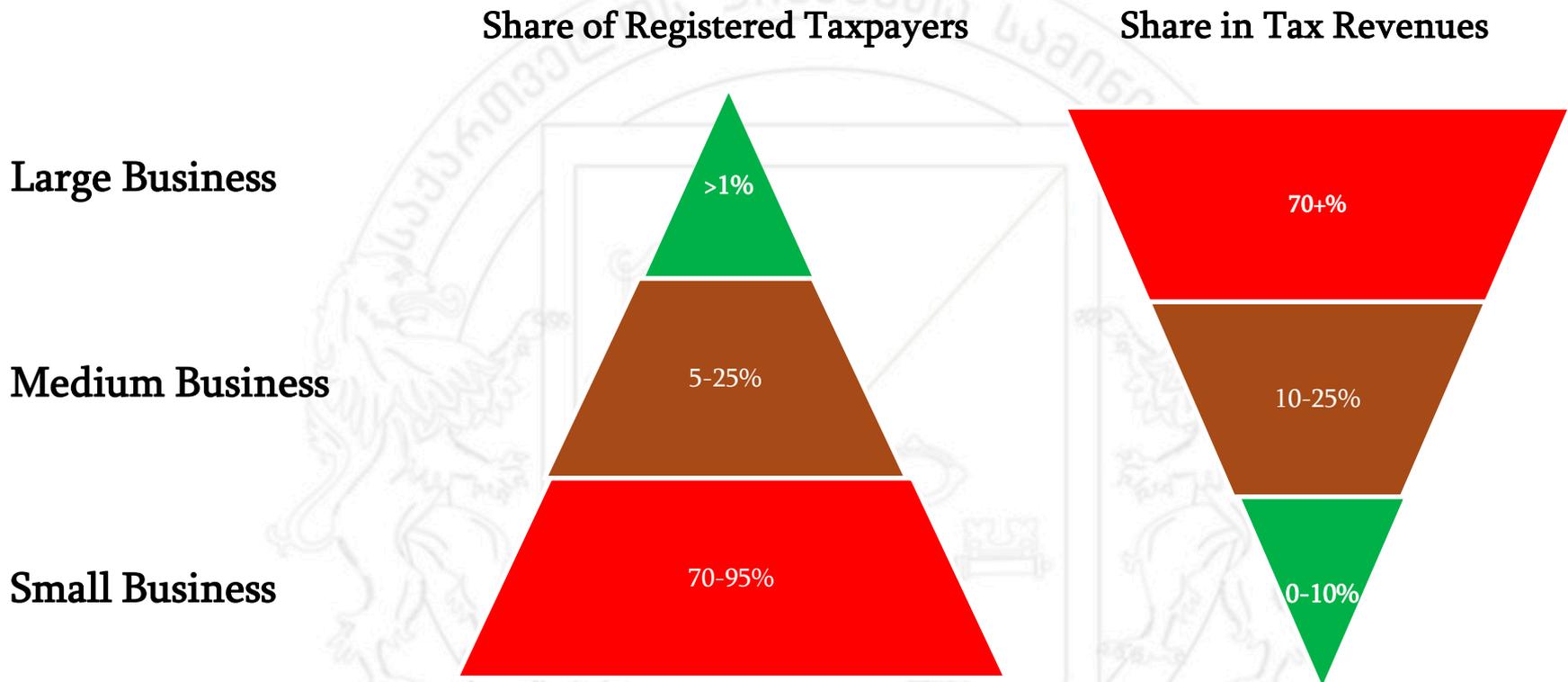
➤ Advance private rulings

- An advance tax ruling is a written statement given by the Tax authority to a taxpayer stating how it will interpret and apply specific provisions of tax law to a definite transactions the taxpayer is contemplating
- An advance tax ruling is binding upon the Tax Authority. This means that if the transaction was carried out substantially as set out in the request, taxpayer will not be subject to any additional tax or sanctions.

➤ Public tax rulings

- In case of decision of tax appeals council and other relevant administrative body which changes and/or establishes tax practice different from existing one, the Ministry of Finance is obliged to issue relevant legislator interpretation act – Public Tax Ruling

Contribution of SME and large businesses to tax revenues





Micro Business

Micro business - entity with income less than to GEL 30,000

- Micro Business is exempted against any tax

Expected results:

- Employment
- Reduction of poverty through self-employment
- Full legalization of business

Small business - Entity with income less than GEL 100,000

Taxation Procedures:

- Will be taxed with one single tax;
- Tax rate of 3% or 5% of income;
 - In case of 5% Tax Rate - runs only simple "purchases and sales journal" and cash registers;
 - In case of 3% Tax Rate – entity must provide invoices for at least 60% of its income.
- Removing requirements of book keeping in conformity with international standards.



Advance tax ruling

Advance Tax Ruling

- Important mechanism in the world tax system in order to increase taxpayer's procedures efficiency and comfort;
- Person, who acts according with advance tax ruling, the Georgian Tax Authority may not be imposed taxes or tax sanctions.
- An application to request an advance ruling must be in written form. The tax authority has the right to request the submission of additional documents. As a rule, the tax authority is obliged to issue an advance ruling within **60 days** of receipt of the application.

Advantages

- Taxpayer is given the opportunity to take a preliminary decision from the Tax Authority of future reports on the basic financial operations and structuring;
- Encouraging local entrepreneurs and foreign investors;
- Simplify relationship between businesses and tax authorities.

International practice of advance tax ruling



- Procedure was imposed in various countries on different steps of development;
- ATR has similar principles in all economies, excluding price and time limits;
- The focal objective of ATR is to establish close contacts between the taxpayer and tax authority in order to better fulfill all the tax procedures;
- Nowadays, ATR is used in more than 40 Countries.

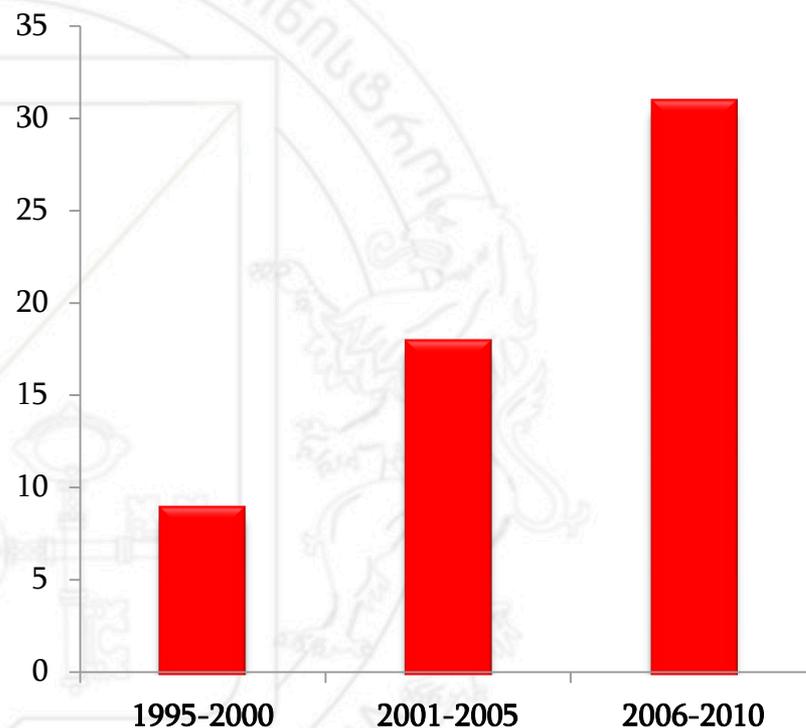
COUNTRY	Public rulings		Private rulings			
	Public rulings are issued	Binding/ not binding on revenue body	Private rulings are issued	Binding/ not binding on revenue body	Time limits for private rulings	Fees for private rulings
<i>1) OECD countries</i>						
Australia	✓	Binding	✓	Binding	✓ / 1	×
Austria	✓	Binding	✓	Binding	✓ / 1	×
Belgium	✓	Binding	✓	Binding	✓ / 1	×
Canada	✓	Binding	✓	Binding	✓ / 1	✓
Czech Repub.	✓	Binding	✓	Binding	×	✓
Denmark	✓	Binding	✓	Binding	✓ / 1	✓
Finland	✓	Binding	✓	Binding	✓	✓
France	✓	Binding	✓	Binding	✓ / 1	×
Germany	✓	Binding	✓	Binding	×	✓
Greece	✓	Binding	✓	Binding	✓ / 1	×
Hungary	✓	Binding	✓	Binding	✓ / 1	×
Iceland	✓	Binding	✓	Binding	✓ / 1	✓
Ireland	✓	Binding	✓	Binding	✓ / 1	×
Italy	✓	Binding	✓	Binding	✓ / 1	×
Japan	✓	Binding	✓	Not binding	×	×
Korea	✓	Binding	✓	Binding	×	×
Luxembourg	✓	Binding	×	-	-	-
Mexico	✓	Not binding	✓	Not binding	✓ / 1	×
Netherlands	✓	Binding	✓	Binding	×	×
N. Zealand	✓	Binding	✓	Binding	×	✓
Norway	✓	Not binding	✓	Binding	✓ / 1	✓
Poland	✓	Not binding	✓	Not binding	✓	✓
Portugal	✓	Binding	✓	Binding	×	×
Slovak Rep.	✓ / 1	Binding	✓ / 1	Binding	✓ / 1	×
Spain	✓ / 1	Binding	✓	Binding	✓	×
Sweden	✓	Binding	× / 3	Binding	× / 1	✓ / 1
Switzerland	✓	Binding	✓	Binding	×	×
Turkey	✓	Binding	✓	Binding	×	×
UK	✓	Binding	✓	Binding	✓	×
USA	✓	Binding	✓	Binding	×	✓
<i>2) Select non-OECD countries</i>						
Argentina	✓	Binding	✓	Binding	✓	×
Bulgaria	✓	Binding	✓	Not binding	✓ / 1	×
Chile	✓	Binding	✓	Binding	×	×
China	✓	Binding	✓	Binding	×	×
Cyprus	✓	Binding	✓	Binding	✓ / 1	✓ / 1
Estonia	✓	Binding	×	-	-	-
Latvia	✓	Not binding	✓	Binding	✓	✓
Malaysia	✓	Binding	✓	Binding	✓ / 1	✓
Malta	✓ / 1	Not binding	✓	Binding / 1	×	×
Romania	✓	Binding	✓	Binding	✓ / 1	×
Singapore	✓	Binding	✓	Binding / 1	✓ / 1	✓
Slovenia	✓	Binding	✓	Binding	✓ / 1	× / 1
South Africa	✓	Binding	✓	Binding	✓ / 1	✓

Sources: IBFD and country survey responses

International Taxation

- DTAs help to widen Georgia's economic space and strengthen its position as a hub for business.
- The main objective of a DTA is to minimize tax barriers to the flows of trade and investment between two treaty countries.
- The number of DTAs were doubled in 2009-2010.

Statistic of DTA's in Force





International Taxation

- Georgian draft of the “Agreement for the Avoidance of Double Taxation on Income and on Capital” is based on 2008 OECD Model Tax Convention on Income and on Capital.
- “Double Taxation Agreement” between Georgia and another country serves to prevent double taxation of income earned in one country by a resident of the other country. It also makes clear the taxing rights between Georgia and its treaty partner on different types of income arising from cross-border economic activities between the two countries.
- The main principle of Georgian DTAs is taxation based on **residency** – person shall be taxable in a **country of residence** on its worldwide income.
- If certain types of income are taxed in a **country of source**, Georgia gives tax credit to eliminate double taxation.



International Taxation

- Georgian draft of the “Double Taxation Agreement” includes different provisions of 2008 OECD Model Tax Convention. Dividends and interest must be taxable according to residency.
- For instance, if Georgia’s resident company receives dividends from Singapore's resident company, it will be taxable only in Georgia.
- According to new changes introduced in Georgian tax code in 2009, withholding tax rates of dividends and interest are 5%. These incentives encourage to flow investment and to improve business climate in Georgia.

Agreements for the Avoidance of Double Taxation



Currently Georgia has 30 active Double Taxation Agreements with major trade partner:

EUROPEAN UNION



Austria



Belgium



Bulgaria



United Kingdom



Germany



Denmark



Estonia



Ireland



Italy



Latvia



Lithuania



Luxembourg



Malta



Czech Republic



Netherlands



Poland



Romania



Greece



France



Finland

OTHER STATES



Azerbaijan



Turkey



Turkmenistan



Iran



Singapore



Armenia



Uzbekistan



Ukraine



China



Kazakhstan



Double Tax Treaty Withholding Tax Rates

EUROPEAN UNION

Country	Permanent Establishment	Dividends	Interest	Royalties
Austria	6 month	0% / 5%	0%	0%
Belgium	9 month	5%	5%	5% / 10%
Bulgaria	9 month	5%	5%	10%
United Kingdom	6 month	0% / 5%	0%	0%
Germany	6 month	0% / 5%	0%	0%
Denmark	6 month	0% / 5%	0%	0%
Estonia	9 month	5%	5%	10%
Italy	6 month	5%	0%	0%
Ireland	6 month	0% / 5%	0%	0%
Lithuania	9 month	5%	5%	10%
Latvia	6 month	5%	5%	10%
Luxembourg	6 month	0% / 5%	0%	0%
Malta	6 month	0%	0%	0%
Netherlands	6 month	0% / 5%	0%	0%
Poland	6 month	5%	5%	10%
Romania	9 month	5%	5%	5%
Greece	9 month	5%	5%	5%
France	24 month	5%	0% / 5%	0%
Finland	6 month	0% / 5%	0%	0%
Czech Republic	6 month	5%	5%	0% / 5% / 10%

OTHER STATES

Country	Permanent Establishment	Dividends	Interest	Royalties
Azerbaijan	6 month	5%	5%	10%
Turkey	12 month	5%	5%	10%
Turkmenistan	6 month	5%	5%	10%
Iran	12 month	5%	5%	5%
Singapore	6 month	0%	0%	0%
Armenia	6 month	5%	5%	5%
Uzbekistan	6 month	5%	5%	10%
Ukraine	12 month	5%	5%	10%
Kazakhstan	6 month	5%	5%	10%
China	6 month	0% / 5%	5%	5%

Global Forum on Transparency and Exchange of Information for Tax Purposes



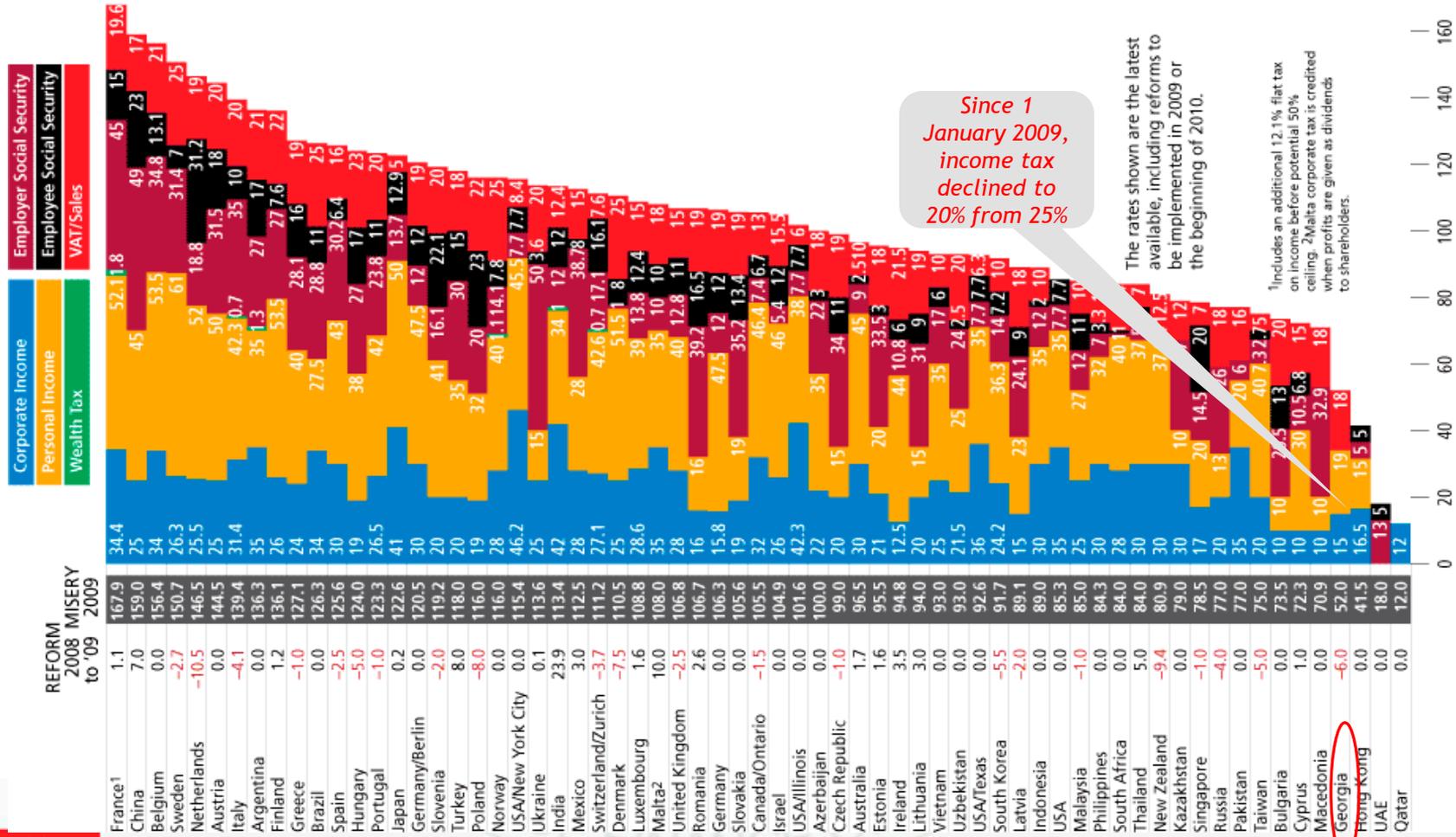
- In the first half of 2011 Georgia will become a member of Global Forum on Transparency and Exchange of Information for Tax Purposes. 98 States are the Members of Global Forum, including all OECD countries and all G20 countries.
- **The main objectives of the Global Forum are:**
 - 1) to ensure that all its members are on an equal footing; and
 - 2) will fully implement the standards of exchange of information they have committed to implement.



One of the Best Performer by Forbes Tax Misery & Reform Index



- According to 2009 Tax Misery & Reform Index, release by Forbes Business & Financial News, Georgia is the fourth least tax burden country after Qatar, UAE and Hong Kong



Contacts



Rusudan Kemularia
Deputy Minister of Finance of Georgia
+995 32 262406
R.kemularia@mof.ge

