

Economic reforms in 2022

A glimpse of hope amid geopolitical uncertainty

Without question, 2022 was a year characterized by economic uncertainty and geopolitical chaos in the region. As we head into 2023, much remains uncertain. However, it is evident now more than ever that liberalization and Westernization of the Georgian economy has no alternative. In the spirit of this sentiment, we have summarized the major economic reforms of 2022 and outlined further steps we hope to see taken in the coming year.

Capital Markets

2022 was a very active and productive year for the National Bank of Georgia (NBG) and the economic team of the government. A new covered bonds regulation was initiated in parliament, which will enable commercial banks to issue mortgage-backed securities, a safe and liquid security instrument that will give investors dual recourse towards an issuer, as well as high-quality assets that back the securities in question. At the same time, the Law on Securitization was also submitted to parliament in the last quarter of 2022. While the covered bonds regulation creates a liquidity instrument for commercial banks, the securitization law will enable all businesses to transform their long-term cash-generating assets into financial instruments to raise funding.

The National Bank of Georgia was also given the legislative mandate to regulate virtual assets. The details of this regulation will be set out in the sub-normative regulations (i.e., NBG acts) to be adopted no later than July 1, 2023. The enactment of these legislative changes marks a positive step towards developing digital finance in the country.

Once all these regulations are adopted and implemented, the “first generation reform” of capital markets (i.e., investment funds, derivatives, securitization, covered bonds) in Georgia will

be finalized. A great deal of work remains to enable these reforms, including awareness raising among businesses and improving the tax and auxiliary rules that are fundamental for functional alternative finance and capital market regulation.

Energy Sector

Major changes are anticipated to from March 31, 2023 in Georgia's energy sector. Chief among them is the introduction of an electricity exchange (spot market) where trading electricity through day ahead, intraday, and balancing markets as well as bilateral agreements will be allowed. Trading through capacity and ancillary services will also become possible.

Following the opening of the spot market, the new Governmental Decree on Support Mechanism of Generation and Consumption of Renewable Energy will come into effect, which is currently in the process of being adopted. Based on this decree, any renewable energy source of installed capacity more than 0.5 MW, which has not submitted a full feasibility study to the government, will have the right to participate in a capacity auction generated by the government and obtain CfD (Contract for Difference) support from the government over the successfully obtained capacity.

The CfD support mechanism will allow participants to enjoy the guaranteed tariff for a maximum of 15 years and will create a bankability perspective for power plant projects in Georgia. We hope that these reforms will revive the Georgian energy sector. Development of new generation assets and attraction of investment in the energy sector is essential for the country, particularly because water remains one of the most underused resources and scarcity of energy may soon become a major issue.

Tax

Significant amendments were made to the Georgian tax legislation in 2022 to ensure complete transparency, proper tax administration, and compliance by taxpayers before the tax authority. Here are a few of the biggest developments:

- (a) **Regulation of payment system operators.** Amendments in the Tax Code of Georgia were introduced subsequent to changes in the Law of Georgia on Payment Systems and Payment Services, in accordance with which payment service providers are subject to the same obligations as banking institutions regarding the payment of taxpayer tax liabilities and opening of a bank account.
- (b) **Broadened powers of the tax authority with respect to confidential information.** During a tax audit of a taxpayer, or upon request of another state's authorized body according to an international agreement to which Georgia is a party, the tax authorities are now authorized to request that certain financial instructions provide confidential information protected by the special legislation regulating their activities (i.e., information on user funds, electronic money, transactions executed, information recorded in the register of unit-holders of an investment fund, and information on borrowers existing in a microfinance organization) based on the relevant court decision. Before the amendment, these regulations only applied to banking institutions.
- (c) **Declaring taxes.** As a general rule, if a person fails to file a tax return, he/she is deemed to have filed a tax return, based upon which the amount of the assessed taxes equals zero. However, the general rule is no longer applicable to registered VAT payers; thus, such persons are obliged to submit tax declarations monthly irrespective of whether the payer has taxable operations or not for the reporting month. In other words, if there is no taxable amount, the company must still submit a declaration stating that their taxable amount is zero.

Georgia continues to work on its tax dispute resolution reform, within the framework of which, several steps have already been taken. These include the creation of a new informative platform for taxpayers, the renewal and consolidation of manual guidelines, and analysis and testing of international best practices. The reform aims to contribute to better tax and legal certainty, increased public confidence in the Georgian tax regime, and improved self-compliance by enabling the resolution of tax disputes without litigation, on the basis that is fair and impartial to both the government and the taxpayer. Overall, the Georgian tax system is developing in a way that meets its commitments to implement BEPS minimum standards, create an investor-friendly environment, and become a respected member of the global tax society.

Consumer Protection

The new Law on Consumer Rights Protection was enacted in June 2022. This law regulates the relationship between the providers of goods/services and consumers and introduces several direct obligations. This includes the obligation to provide consumers with information on the trader as well as the goods/services it offers. Traders also have 30 days to deliver goods, and if this is not complied with, the consumer has the right to claim a refund as well as reimbursement of damages. In the case that rules introduced by the law are breached, traders

may be subject to, among others, monetary sanctions not exceeding 2% of their annual turnover. The right to monitor and enforce the law is given to the Competition Agency of Georgia, which is also designated to review consumer administrative complaints. Although this reform was greeted with reluctance by certain businesses, increasing competition and fairness towards consumers is a positive development for Georgia's economy. As 2022 comes to a close, it remains to be seen what specific effect this law will have on how traders and consumers interact.

Environmental Regulations

Georgia continues to work towards the development of environmental regulations. Although these reforms are important, businesses have expressed a desire for closer communication and leniency from the Georgian government. In 2022, the new rules introduced for air pollution filters remained a fundamental issue for several industrial plants as many were penalized for noncompliance. Furthermore, management of solid waste remains an unresolved issue for the country, which is partially due to absence of sufficient waste management plants. Nevertheless, there are significant legislative initiatives in this sector. For example, the new Law on Management of Water Resources was recently initiated in parliament, which will enable the improvement of the ecological status of rivers and allow for more information to be collected on available water resources. It will also introduce permits for the use of water resources, which was previously abolished within the framework of the deregulation of newly constructed energy plants in 2008. Compliance with the relevant undertakings is one of the essential components of the Georgia-EU Association Agreement, and we remain hopeful that the government will succeed in its mandate to create a better environment for all, while, at the same time, acknowledging how costly of a process it can be for businesses to update their operations to comply with the new regulations.

New Year's Wishes

As do all children around the world, we, here at BLC, have our own list of wishes for the New Year. *First and foremost*, we wish peace and victory to the Ukrainian people. They have proven that persistence and belief in any ideal is stronger than any pre-conceived notion of what strength is. *Secondly*, we wish for stability and remembrance of what is important throughout the entire world. As recent events have once again demonstrated, we are all connected, and ensuring the well-being of one another is more important now than it has ever been. *And last but not least*, we wish for the economic prosperity of Georgia and success in the implementation of the aforementioned economic reforms. Increasing the wealth and well-being of every Georgian household will be impossible without this.

On behalf of the entire team of BLC, we wish you happy holidays! Let us all come together and work restlessly for creating a better and more prosperous tomorrow!

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