PROGRESS REPORT 2018

International Taxation

MINISTRY
OF
FINANCE
OF
GEORGIA

Report on progress 2018

This Progress Report tracks records of achievements in international taxation of the Ministry of Finance of Georgia for 2018 and covers following areas

- International Tax Treaties
- Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI)
- Base Erosion and Profit Shifting (BEPS) minimum standards
- Global Forum on Transparency and Exchange of Information for Tax Purposes
- EU Screening Process
- Capacity Building

Tax Treaties

Currently Georgia has negotiated and concluded agreements on the „Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital“ with **55** partner states. These agreemets include treaties with all EU member states, as well as the OECD countries and Georgia's major trade and economic partners.

In 2018 an agreement with Moldova became effective and a treaty with Saudi Arabia has been ratified by the Parliament of Georgia.

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS

On 7 June 2017, together with 70 Ministers and other high-level representatives **Georgia** signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Instrument" or "MLI").

The MLI offers concrete solutions for governments to close the gaps in existing international tax rules by transposing results from the OECD/G20 BEPS Project into bilateral tax treaties worldwide. It is intended to update more than 2,000 tax treaties worldwide and modify them to include specific BEPS provisions, including minimum standards to counter treaty abuse and improve dispute resolution mechanisms.

In **February 2015** an ad-hoc group on multilateral instrument was established, which was mandated by the G-20 and the OECD countries to develop texts of the Multilateral Instrument and its Explanatory Statement. In **March 2015**, Georgia was officially invited to join the ad-hoc group and became actively engaged in the working process.

As a result of these works, **on November 24, 2016**, the members of the ad-hoc Group on the MLI concluded negotiations and adopted the final texts of the Multilateral Instrument and the Explanatory Statement.

During the 2017 winter plenary meeting the OECD organized a speed matching event. The primary purpose of this event was to enable treaty partners to conduct bilateral talks to discuss in detail the outcomes of changes and effects on their bilateral treaties initiated by the MLI to establish a common approach and arrive at mutual understanding on certain practical aspects.

Multilateral Convention to implement tax treaty related measures (MLI)

Therefore, during the mentioned event, Georgia held consultations with the following 12 treaty partner states: **Liechtenstein, Luxembourg, Netherlands, Switzerland, Slovenia, Slovak Republic, Serbia, Estonia, Israel, Singapore, India, Republic of Korea.**

Apart from this, Georgia conducted intensive communication with the remaining MLI partner states to shape and align their approaches under the instrument.

In addition, during the year Georgia has been closely working with and consulting foreign experts to bring its tax policy in lign with MLI requirements. Several working meetings has been conducted with the GIZ and WB experts, and as a result Georgia has elaborated a separate document which reflects its policy approach towards the MLI, and contains the list of its reservations, options and positions on a number of MLI articles.

Following our international tax policy line, 34 out of 55 active treaties will be modified under the MLI, upon the conclusion of domestic procedures required to bring the instrument into effect. With respect to the remaining jurisdictions, Georgia will be working closely with them on a bilateral basis.

Ministry of Finance has carried out domestic procedures required for the ratification of the multilateral instrument by the Parliament.

On 29th of December, 2018, Parliament of Georgia ratified the multilateral instrument.

Additionally, works related to the preparation of synthesized texts have been initiated. As a result, bilateral working process will be launched in 2019 to coordinate works on synthesized texts with partner countries of the covered tax treaties.

Base Erosion and Profit Shifting (BEPS)

The **Inclusive Framework on BEPS** brings together over 100 countries and jurisdictions to collaborate on the implementation of the OECD/ G20 Base Erosion and Profit Shifting (BEPS) Package.

On June 16 2016, Georgia became an associate member of the inclusive framework for the implementation of the BEPS package (minimum standards). This is a unique opportunity for developing countries, and Georgia in particular, to work closely with OECD and G 20 member states on an equal footing in respect of shaping and implementation of the BEPS outcomes in order to tackle tax avoidance efficiently.

All countries and jurisdictions joining the framework participate in review process, which allows members to review their own tax systems, identify, and remove elements creating BEPS risks.

The BEPS package consists of 15 Actions, where four of them contain minimum standards. All Inclusive Framework members are committed to implement **BEPS minimum standards.**

The BEPS minimum standards are as follows:

- BEPS Action 5 – Harmful Tax Practices
- BEPS Action 6 – Prevention of treaty abuse
- BEPS Action 13 – Country-by-country reporting
- BEPS Action 14 - Making dispute resolution more effective

As an Inclusive Framework member, **Georgia is actively engaged in the implementation process of the BEPS minimum standards.**

Since 2017 Georgia is a member of the Ad Hoc Advisory Task Force of Working Party 1 and Working Party 6. The advisory task force has been set up with the aim to offer suggestions/ recommendations to the OECD Committee of Fiscal Affairs (CFA), including in its Inclusive Framework on BEPS format, on the strategic direction of the work and priorities of these two working parties beyond 2018.

In 2018 Georgia has been reelected for the second term in Steering Group – the governing body of the Inclusive Framework - which is composed of 22 member jurisdictions and chaired by Germany.

BEPS ACTION 5 – HARMFUL TAX PRACTICES

The Action 5 minimum standard consists of two parts. One part relates to preferential tax regimes, where a peer review is undertaken to identify features of such regimes that can facilitate base erosion and profit shifting, and therefore have the potential to unfairly impact the tax base of other jurisdictions. The other part includes a commitment to transparency through the compulsory spontaneous exchange of relevant information on taxpayer-specific rulings, which, in the absence of such information exchange, could give rise to BEPS concerns.

The Forum on Harmful Tax Practices (FHTP) is the body that has the mandate to monitor and review tax practices of jurisdictions around the world, focusing on the features of preferential tax regimes.

As a member of the inclusive framework, Georgia has been active in the works of the FHTP since 2016 September. In March 2017, Georgia became a member of the Bureau of the FHTP. Currently, the Bureau is co-chaired by France and Japan, and comprises representatives from the following other nine countries: Brazil, Germany, Ireland, Indonesia, Mexico, Singapore, Span, Switzerland and the US.

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In 2017, preferential tax regimes existing in Georgia have been reviewed by the FHTP against the compliance with the Action 5 minimum standards.

These regimes are:

- Free Industrial Zone
- Special Trade Company
- International Financial Company
- Virtual Zone Person

As a result of these reviews, it has been recognized that Georgia's **Free Industrial Zone and Special Trade Company Regimes** are out of scope of the minimum standards. As they are out of scope, no further action is required by Georgia. Two other regimes, the **International financial company and the Virtual zone person** regimes were concluded as 'potentially harmful but not actually harmful.' These two regimes will require no further actions to be taken by Georgia, though they are subject to an ongoing yearly monitoring process on the actual harmfulness.

In 2018 FHTP conducted the reassessment of preferential tax regimes existing in Georgia. As a result these regimes have been granted the same assessments as within the 2017 assessments. The final outcome has been reflected in the **2018 Progress Report on BEPS Action 5: Preferential Regimes** (see below)

CTPA/CFA/FHP/NOE2(2018)14

Jurisdiction	Regime	Status	Comments
Georgia	International financial company	Potentially harmful	Ring-fencing implicated, but no harmful economic effects in practice. Regime is subject to annual monitoring.
Georgia	Free industrial zone	Out of scope	No income from geographically mobile activities.
Georgia	Special trade company	Out of scope	No income from geographically mobile activities.
Georgia	Virtual zone person	Potentially harmful but not actually harmful	Ring-fencing and substantial activities factor implicated, But no harmful economic Effects in practice. Regime is Subject to annual monitoring.

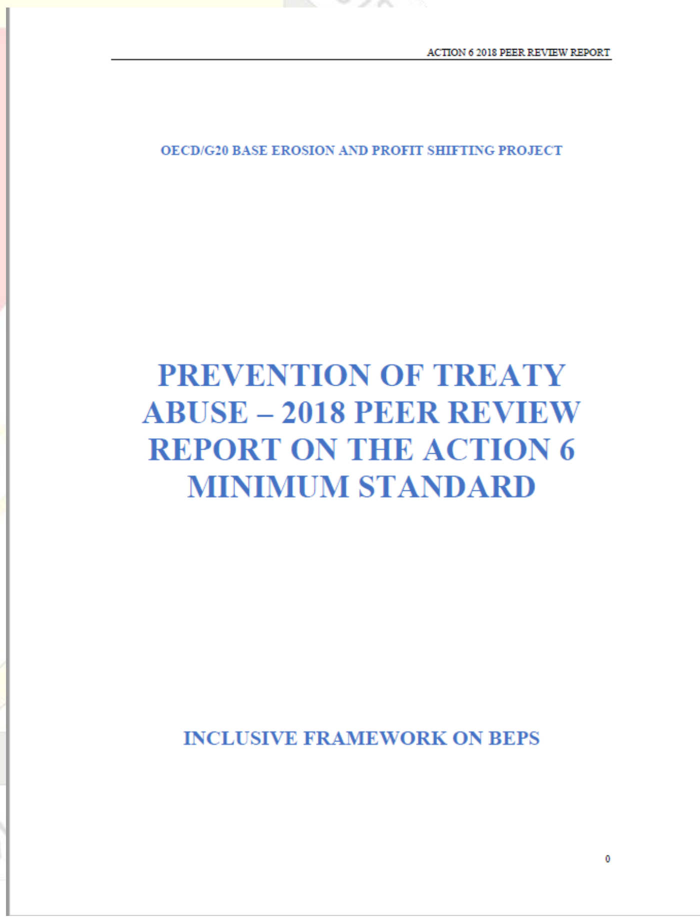
OECD
Organisation for Economic Co-operation and Development

In order to fulfill the obligations emerged from the second part of the Action 5 of the BEPS Project, Georgia implemented the transparency framework for spontaneous exchange of information on certain tax rulings. Namely, In order to have the necessary legal framework in place for spontaneous exchange of information on rulings covered by the transparency framework and for purposes of fulfilling obligations arising from the joining of Georgia to the Inclusive Platform, the Ministry of Finance of Georgia issued “**the Order on implementation of the obligatory measures under the Base Erosion and Profit Shifting (BEPS) Project**”, as well as **“the form for information exchange”, “Instructions for the form on Exchange of Information” and “Issues Specified by the Base Erosion and Profit Shifting Project Action Plan 5”.** Besides, according to the timeline given to Georgia under BEPS project, **Ministry of Finance exchanged past rulings by 31 December 2018.**

BEPS ACTION 6 – PREVENTION OF TREATY ABUSE

The multilateral tax instrument is envisaged with a view to implementing swiftly the treaty outputs of the OECD work on addressing base erosion and profit shifting (BEPS). As more than 3,000 tax treaties for the avoidance of double taxation (tax treaties) are in force today, a monumental effort would be required to renegotiate each of them in a coordinated and timely manner.

However, the multilateral instrument could avoid such a cumbersome renegotiation process by modifying the tax treaties of all interested states. Signatories to the multilateral instrument will be asked to incorporate into their tax treaty network rules for addressing hybrid mismatch arrangements, abuse of treaties and artificial avoidance of the permanent establishment status, as well as rules for improving dispute resolution mechanisms, including mandatory binding arbitration. Members of the Inclusive Framework on BEPS are therefore encouraged to use the multilateral instrument for that purpose.


ACTION 6 2018 PEER REVIEW REPORT

OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT

PREVENTION OF TREATY ABUSE – 2018 PEER REVIEW REPORT ON THE ACTION 6 MINIMUM STANDARD

INCLUSIVE FRAMEWORK ON BEPS

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These rules for the **prevention of treaty abuse** and **artificial use of permanent establishment status** constitute **minimum standards under the BEPS Action 6**.

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To ensure effective and coordinated implementation of Action 6 minimum standard **in 2018 the OECD launched a Peer Review of existing bilateral tax treaties.**

The 2018 Peer Review covers 116 jurisdictions, amongst them Georgia. As part of the review process, Georgia has filled in an on-line questionnaire and prepared a list of its existing comprehensive income tax agreements in force on 30 June 2018.

The list indicated whether at that time each agreement included the provisions of the minimum standard, i.e. a complying preamble and the necessary anti-abuse provision(s).

Since participation in the multilateral instrument was not mandatory and because jurisdictions could have different preferences about how the minimum standard should be met, **monitoring of the implementation** of the minimum standard would be necessary.

The **Peer Review** revealed, that a large majority of Inclusive Framework members, among them Georgia, have **made substantial progress towards implementing the minimum standard and are currently in the process of modifying their treaty network** by using the MLI, which has proved itself to be a quick and efficient way of allowing jurisdictions to meet the minimum standard.

Additionally, Georgia is in the process of bilateral talks with Poland to conclude bilateral amending protocol intending to bring the agreement with Poland in line with BEPS requirements.

The excerpt of Georgia's review is attached below.

ACTION 6 2018 PEER REVIEW REPORT

Georgia

A. Progress in the implementation of the minimum standard

1. Georgia has 54 tax agreements in force, as reported in its response to the Peer Review questionnaire.

2. Georgia signed the MLI in 2017, listing 34 of its 54 tax agreements.

3. For its agreements listed under the MLI, Georgia is implementing the preamble statement (Article 6 of the MLI) and the PPT (Article 7 of the MLI). The agreements that will be modified by the MLI will come into compliance with the minimum standard once the provisions of the MLI take effect.

4. Georgia indicated in the response to the Peer Review questionnaire that bilateral negotiations would be used for its agreement with Poland.

B. Implementation issues

5. No jurisdiction has raised any concerns about their agreements with Georgia.

The 2018 Peer Review report on the Action 6 minimum standard is subject to approval by the CFA and will go public in 2019.

BEPS ACTION 13 – COUNTRY-BY-COUNTRY REPORTING

The BEPS Action 13 report (Transfer Pricing Documentation and Country-by-Country Reporting) provides a template for multinational enterprises (MNEs) to report annually and for each tax jurisdiction in which they do business the information set out therein. This report is called the Country-by-Country (CbC) Report.

As one of the four BEPS minimum standards the Action 13 is subject to peer review in order to ensure timely and accurate implementation and thus safeguard the level playing field. All members of the inclusive Framework on BEPS commit to implementing the action 13 minimum standard and to participating in the peer review on an equal footing.

Since the Action 13 Report was released, jurisdictions have made great efforts to establish the necessary domestic and international legal and administrative frameworks for the filing and exchange of CbC Reports in accordance with the Action 13 minimum standard and the global landscape for CbC Reporting by MNE groups is still evolving.

On 30 June 2016 in the framework of the first meeting of the Inclusive Framework on BEPS Georgia signed the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country (CbC) Reports. Currently Georgia is in the process of implementation of the CbC Reporting. At the same time, we actively cooperate with the OECD, which performs monitoring of the implementation of the CbC Reporting.

In November 2018, the Ministry of Finance of Georgia prepared the draft package for the implementation of the Country-by-Country reporting, consisting of the amendments to the primary legislation along with the secondary legislation.

BEPS ACTION 14 - MAKING DISPUTE RESOLUTION MORE EFFECTIVE

The minimum standard of Action 14 requires Inclusive Framework countries to ensure the consistent and proper implementation of tax treaties, including the effective and timely resolution of disputes regarding their interpretation or application through the mutual agreement procedure. The commitment by members to implement the Action 14 minimum standard includes a commitment to provide timely and complete reporting of MAP statistics pursuant to an agreed reporting framework.

The MAP peer review and monitoring process is conducted by the Forum on Tax Administration (MAP Forum) in accordance with the Terms of Reference and Assessment Methodology, with all members participating on an equal footing. The Assessment Methodology establishes detailed guidelines for a two-stage approach to the peer review and monitoring process.

Stage 1 involves the review of a Member's implementation of the minimum standard based on its legal framework for MAP and the application of this framework in practice.

Stage 2 involves the review of the measures taken by the Member to address any shortcomings identified in its stage 1 Peer Review.

Since 2017, Georgia is actively involved in the peer reviews of the Batch I, Batch II and Batch III jurisdictions.

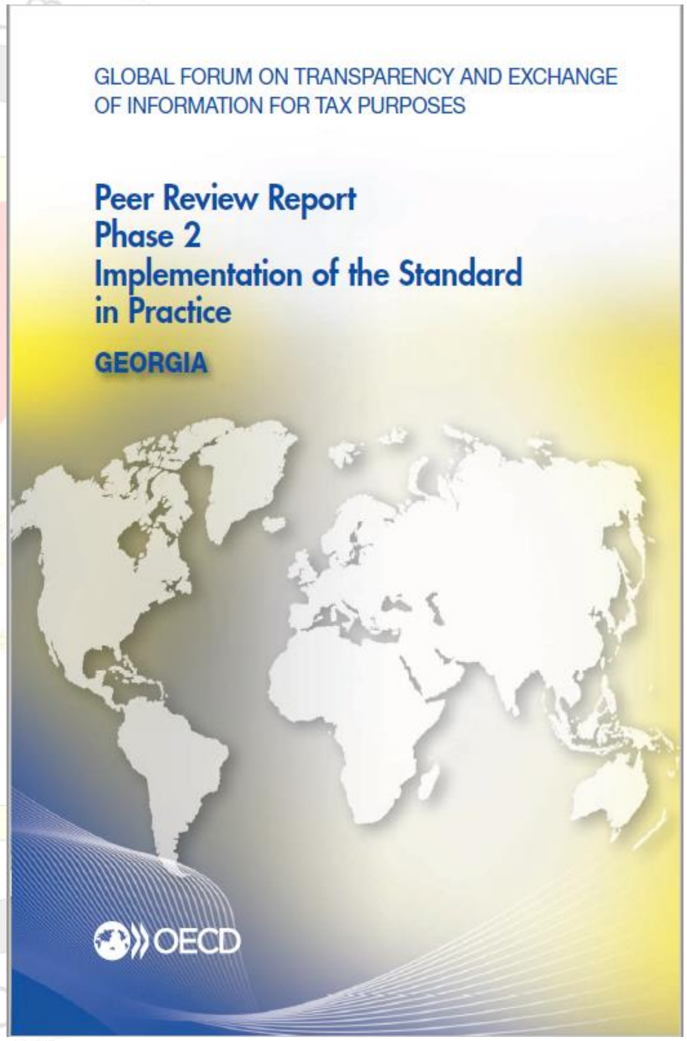
In May 2017, Georgia was elected as a member of the FTA MAP Forum Steering Group.

Throughout the year 2018 Georgia was closely involved in activities of the FTA MAP Forum and participated in the reviews of other jurisdictions. On April 17 2018 The Ministry of Finance provided the reporting of its MAP statistics pursuant to the agreed reporting framework.

The Peer Review of Georgia on Action 14 - Mutual Agreement Procedures (MAP) is scheduled for 2020.

Global Forum on Tranparency and Exchange of Information for Tax Purposes

The Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum) is the world's leading multilateral body within which work in the area of transparency and exchange of information for tax purposes is carried out. The mandate of the Global Forum is to ensure a rapid and effective implementation of the standards on transparency and exchange of information for tax purposes. Its work focuses on two internationally recognised standards: exchange of information on request (EOIR) and automatic exchange of financial account information (AEOI). The Global Forum now has 154 members on equal footing.



One of the main instruments used by the Global Forum to ensure that its members effectively implement the internationally agreed standards is a peer review process. The process is robust and transparent and is designed to identify any areas of the legal or practical implementation of the standards that require improvement, and thus ensures the level playing field.

Since 2009, EOIR peer reviews have generally been conducted in two phases: and examination of the legal framework, followed by an examination of the practical implementation which then assigns overall compliance rating. Since mid-2016, a second round of reviews has commenced, which is a combined examination of both the legal and regulatory framework and the practical implementation of the standard. Peer reviews are undertaken on the basis of agreed terms of reference, using the methodology and assessment criteria.

The work on EOIR is undertaken by the Peer Review Group (PRG) comprising 30 members, among them Georgia. The PRG meets during the year and reports to the Global Forum, which is the sole decision making body.

On 11 April, 2011, Georgia became a member of the Global Forum on Transparency and Exchange of Information for Tax Purposes. Georgia's Phase 1 and Phase 2 reviews have been conducted in 2013-2016. As a result of the assesment it was established in 2016 that Georgia's legislation and practice in the field of tax transparency and exchange of information comply with the international standard and Georgia rates as overall **largely compliant** with the international standard.

In 2017 as a member of the Peer Review Group, Georgia was actively participating in and contributing to the monitoring and peer review process for EOIR. In addition, to these activities, in the second round of Reviews of the Global Forum, Georgia was the assessor for Denmark, together with the other 2 team members from the UK and the OECD secretariat.

Georgia's assessment under the new second round of reviews is scheduled for 2020.

On February 2018 the Ministry of Finance received a questionnaire for the second round of Review of Georgia, which was intended to identify (what laws and practices may already be in place to ensure the availability of, access to, and exchange of all information foreseeably relevant for tax purposes.) potential gaps to be addressed.

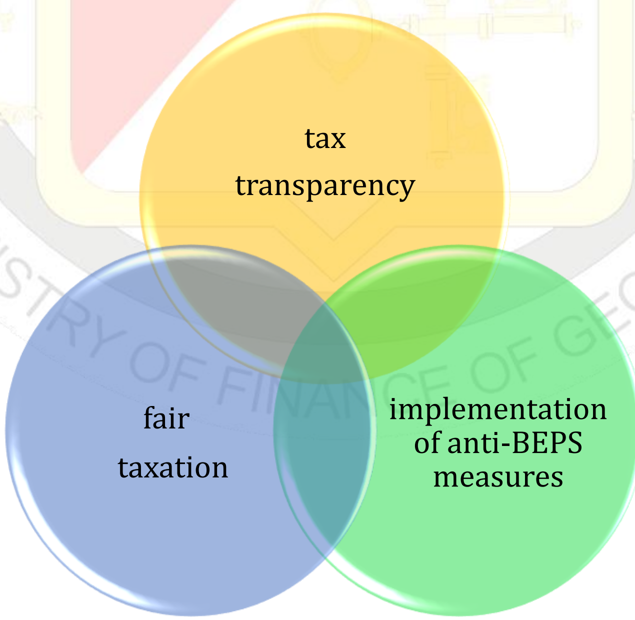
During the year 2018 the work on the questionnaire was carried out in close communication with the OECD experts and the relevant ministries/authorities. The completed questionnaire has been sent to the Secretariat.

EU SCREENING PROCESS

The Council of the European Union, taking account of developments at international level, has committed as a priority to coordinated policy efforts in the fight against tax fraud, evasion and avoidance and against money laundering at EU and global level.

On 8 November 2016, the Council adopted the “Conclusions on criteria and process leading to the establishment of the EU list of non-cooperative jurisdictions for tax purposes”. These Conclusions contain a set of objective criteria that should be promoted internationally in relation to taxation systems of jurisdictions that are not EU Member States.

Criteria for screening jurisdictions with a view to establishing an EU list of non-cooperative jurisdictions



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On 8 November 2016, the Code of Conduct Group (Business Taxation), set up by the Council and the Governments of the EU Member States in 1998 to assess the tax measures of the EU Member States, has been instructed by the Council to select jurisdictions to be invited to engage in a process, which will be arranged in an objective and cooperative manner, based on a common analysis against the criteria referred above.

It should be emphasized that the selection of jurisdictions for the 2017 screening process was based on a set of objective indicators (such as strength of economic ties with the EU, financial activity and stability factors) and that this selection does not prejudge the outcome of this process.

In order to ensure a smooth functioning of the screening process and engage in the dialogue on clarification of specific aspects and relevant commitments, the relevant authorities have been approached to clarify any aspects in respect of which the EU authorities had further queries.

In 2017 The Ministry of Finance of Georgia was actively engaged in the assessment process. As a result, on December 22, Georgian Ministry of Finance was officially notified that Georgia has not been included in the first ever EU list of the non-cooperative Jurisdictions agreed on December 5, 2017 by the Finance Ministers of the EU.

In total, ministers have listed 17 countries for failing to meet agreed tax good governance standards. In addition, 47 countries committed to addressing deficiencies in their tax systems and to meet the required criteria by the end of 2018, or 2019, following contacts with the EU.

As a result of these measures, by December 2018 the number of the black-listed jurisdictions decreased to 5 and the number of Grey-listed jurisdictions increased to 63.

https://ec.europa.eu/taxation_customs/sites/taxation/files/eu_list_update_04_12_2018_en.pdf

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The Commission and Member States (in the Code of Conduct Group) continue to monitor all jurisdictions closely. The EU list is updated at least once a year. **Thus, in 2018, Georgia worked actively to maintain the status achieved, as well as on the implementation of the other criteria to be complied with in the upcoming years.**

With the letter from December 18 2018, the Ministry of Finance was informed by the General Secretariat of the Council that for the year 2019 Georgia retains its status and will not be included in the lists of non-cooperative jurisdictions. In addition we were notified about the endorsement of the new criterion 3.2 (implementation of the Country-by-Country Reporting (CbCR) anti-BEPS minimum standard) in the context of the EU listing exercise.

Georgia should have effectively implemented the CbCR minimum standard by the end of 2019.

Capacity Building

In addition to the abovementioned acitivities, a number of capacity bulding projects were carried out in 2018, in particular:

- On June 20, 2017, the Ministry of Finance of Georgia and the Ministry of Finance of the Netherlands signed a bilateral **twinning programme** within the Inclusive Framework on BEPS.

  - As part of this programme, in September 2018, the Dutch experts provided a 2-day workshop on BEPS minimum standards, designated for tax esperts of the Ministry of Finance ans well as Revenue Service.

- In 2017 Georgian Government and the OECD agreed to launch an **induction programme** to support Georgia to review its domestic legislation and implement BEPS minimum standards and tools developed by the OECD to facilitate the implementation process of the BEPS minimum standards.

  As part of the OECD Industion Programme, a roadmap for Georgia has been finalized in 2018. The reoadmap is a working document that outlines particular areas where technical assistance is required and sets relevant timelines thererof.

- As part of the GIZ assistance, on November 6-8 an expert from the German Ministry of Finance delivered a workshop on capacity-building on treaty application and BEPS practical issues.