MINISTRY OF FINANCE OF GEORGIA

INTERNATIONAL TAXATION

Report on Progress

2017

Tax Treaties

This report represents achievements of the Ministry of Finance of Georgia in the field of International Taxation for the year 2017 and consists of the following topics:

- Tax Treaties
- Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS
- Base Erosion and Profit Shifting (BEPS)
- Global Forum on Transparency and Exchange of Information for Tax Purposes
- EU Screening Process
- Tax and Crime
- 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 **54** 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 2017agreements with the Republic of Korea and Liechtenstein became effective. While a treaty with Kyrgyz Republic has been ratified by the Parliament of Georgia and a treaty with the Repulic of Moldova has been signed.

Addtionally, in 2017 Georgia has carried out and finalized its domestic procedures required for the signature of tax treaties with the following **5** states:

- the Kingdom of Saudi Arabia,
- the Sultanate of Oman,
- the Lebanese Republic,
- the Kingdom of Morocco, and
- the Republic of Poland

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 worldwide tax treaties and modify them to include specific BEPS provisions, such as the 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 G20 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 its 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 to Prevent BEPS

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 54 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.

At this time, Georgia is running its domestic procedures required for the ratification of the instrument. The final positions, options and reservatioins will be deposited to the OECD Secretariat upon the ratification of the multilateral instrument by the Parliament of Georgia.

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.

Georgia is also an elected member of the 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.

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

Global forum on Transparency and Exchange of Inforamtion for Tax Purposes

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.

Currently Georgia is in the process of implementation of transparency framework for spontaneous exchange of information on certain tax rulings.

BEPS Action 6 – Prevention of Treaty Abuse

The multilateral tax instrument is envisaged with a view to implementing swiftly the treaty output 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.

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

Review of bilateral treaties and protocols will be needed. The peer review process and monitoring of implementation of Action 6 minimum standards is planned to be launched in 2018 with the aim of the first report to be produced in January 2019.

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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.

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.

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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.

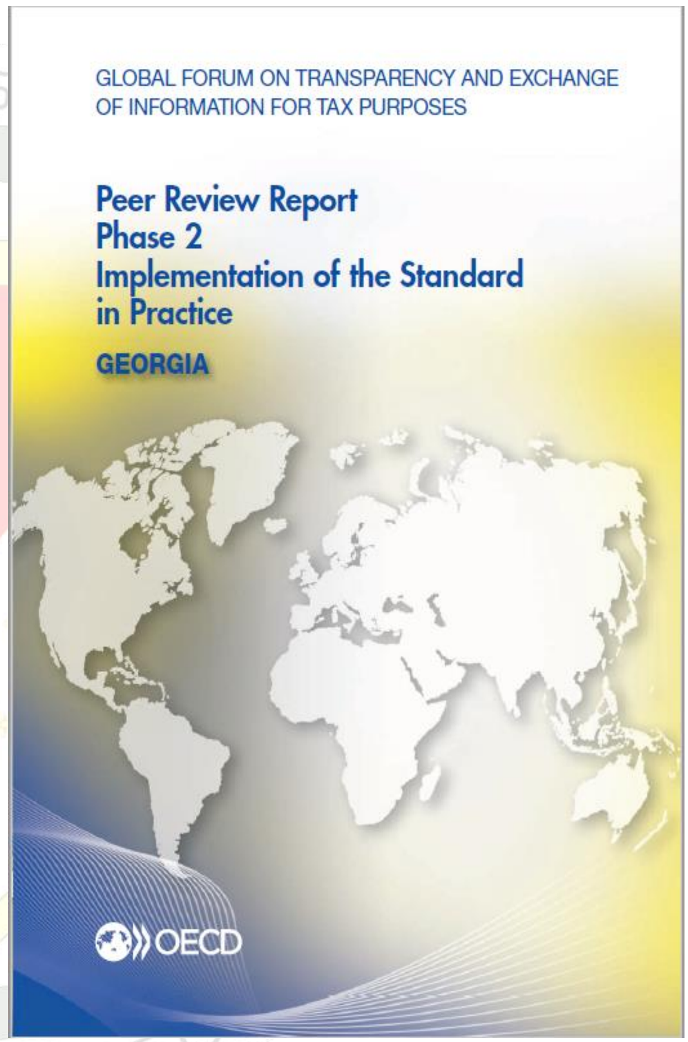
Stage 2 involves the review of the measures taken by the Member to address any shortcomings identified in its stage 1 Peer Review.

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.

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 147 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.

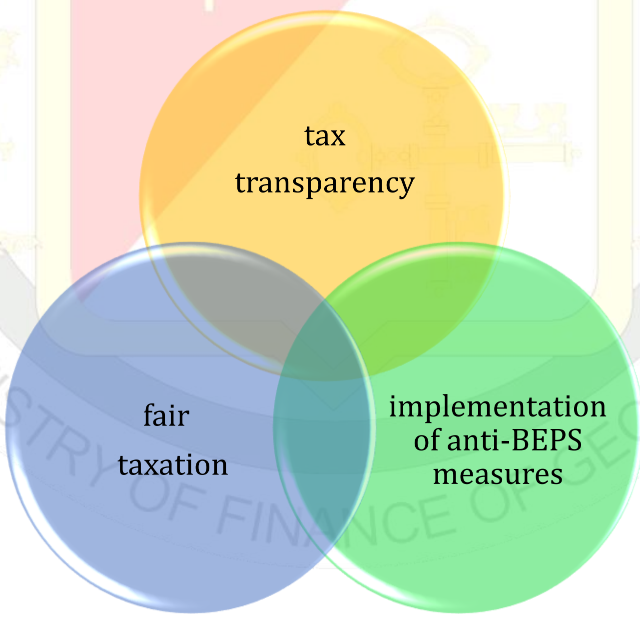
Georgia's assessment under the new second round of reviews is scheduled for 2020.

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



EU Screening Process

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.

The Ministry of Finance of Georgia was actively engaged in the clarification process providing explanations in writing, conducting bilateral discussions and suggesting solutions to facilitate the understanding that our taxation system (tax-related arrangements) is compliant with the above mentioned good governance criteria.

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. The Commission and Member States (in the Code of Conduct Group) will continue to monitor all jurisdictions closely. The EU list will be updated at least once a year.

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. The Commission also expects Member States to continue towards strong and dissuasive countermeasures for listed jurisdictions, which can complement the existing EU-level defensive measures related to funding.

EU LIST Of non-cooperative Tax Jurisdictions		
American Samoa Bahrain Barbados	Macao SAR Marchall Islands Molgolia	Saint Lucia Samoa Trinidad and Tobago
Grenada Guam	Namibia Palau	Tunisia United Arab Emirates
Korea (Rep. Of)	Panama	

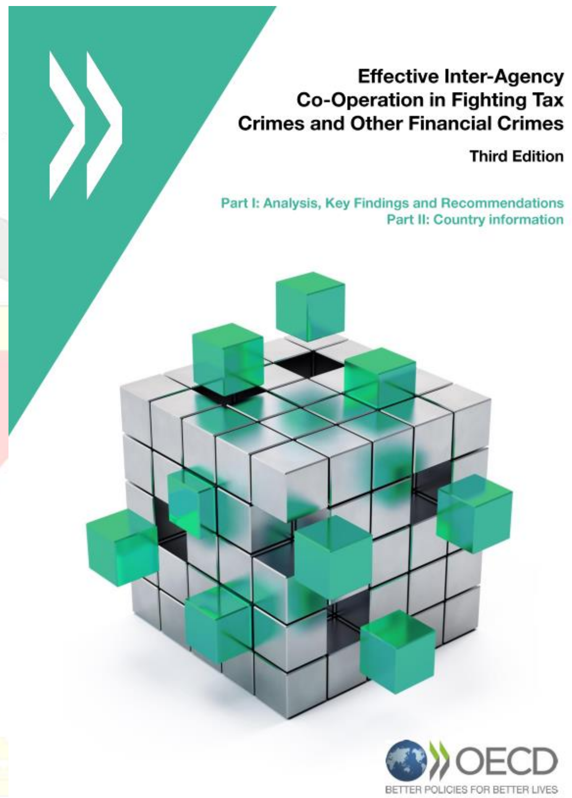
List of jurisdictions committed to address deficiencies in their tax systems

Curacao, Hong Kong, New Caledonia, Oman, Qatar, Taiwan, Bosnia and Herzegovina, Cabo Verde, Fiji, Jordan, Montenegro, Serbia, Swaziland, Turkey, Viet Nam, Armenia, Botswana, F.Y.R of Macedonia, Jamaica, Maldives, Morocco, Peru, Thailand,

Andora, Aruba, Belize, Cook Islands, Liechtenstein, Mauritius, Saint Vinsent and the Grenadines, San Marino, Seychelles, Switzeland, Uruguay, Malaysia, Labuan Islands, Bermuda, Cayman Islands, Guernsey, Isle of Man, Jersey,

Vanuatu, Faroe Islands, Greenlad, Albania, Nauru, Niue

Tax And Crime



On May 10 2017, Georgia was invited by the OECD Center for Tax Policy and Administration (CTPA) to participate in two important projects to support countries in the fight against financial crime and illicit flows:

- **Third edition of the OECD report *Effective Inter-Agency Co-operation in Fighting Tax Crime and Other Crimes*** (The Rome Report) contains an in-depth analysis of models for sharing information between the tax administration, customs, police and law enforcement, the FIU and financial regulators in different countries. Is also explores models for enhanced cooperation, including joint investigations and inter-agency intelligence centers. The Rome Report identifies successful practices for inter-agency co-operation and makes recommendations for how co-operation may be improved.

- **Global Reference Guide on Key Principles and Best Practices in Fighting Tax Crime –** helps all countries in improving their domestic practices in the fight against tax crime. This will allow countries to benchmark their legal institutional, administrative and operational frameworks and identify successful practices based on the experience of other countries.

The Ministry of Finance of Georgia accepted the invitation and successfully lead the process acting as a coordinating and managing body for the preparation of requested information and the central contact point.

As a result, **the third edition of the Rome Report** and **the first edition of the Global Reference Guide** were released and presented at the fifth OECD Forum on Tax and Crime, held on 7-8 November 2017 in London.

Capacity Building

In addition to the abovementioned acitivities, a number of capacity bulding projects were carried out in 2017, 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. The twinning programme seeks to strengthen the capacity of new members of the Inclusive Framework on BEPS to participate effectively in its work. The following topics were outlined as working areas within this project:
    - Transfer Pricing and Country-by-country reporting;
    - Application of Double Tax Conventions;
    - BEPS policy issues;
    - Inclusive Framework on BEPS reviews.

- As part of this programme, the first assistance project was carried out on December 18-20, where tax experts from the Ministry of Finance of the Netherlands held seminar on Transfer Pricing.

- 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 Induction Programme, seminar on the BEPS implementation was carried out in October.

- On 19-24 June, within the assitance project between the Ministry of Finance and the GIZ, an IBFD expert was invited to run a course on Permanent Establishment. This study course was designated for representatives of the Revenue Service of the Ministry of Finance. The primary purpose of the course was to share foreign best practices and communicate new developments of interntational taxation regrading the taxation of permanent establishments.

- As part of the GIZ assistance on November 28-30 a working meeting with the German expert was organized. The target audience was employees of the Audit and Service Departments of the MoF Revenues Service, as well as employees of International taxation of the Ministry of Finance. Some further actions have been scheduled for

2018 within this expert assistance project in light of further elaboration of aspects of international taxation.

- In the framework of cooperation with the World Bank, a working meeting was organized with the WB expert in February this year. The primary purpose of this meeting was to advise georgian policymaker team on approaches to be taken with regards to the Multilateral Instrument.

- The second mission of the WB took place in November 2017, which covered BEPS implementaion and Transfer Pricing issues.