

**Implementation of the European Neighbourhood Policy
Action Plan for 2012 in Georgia
in Trade and Some Trade Related Areas**

Assessment of Civil Society Representatives

(Report Summary)

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Introduction

Georgia's involvement in the *European Neighbourhood Policy (ENP)* opened up new prospects for the country's deeper integration with the EU. The *ENP EU-Georgia Action Plan (ENP AP)*¹, signed in November 2006, identified trade relations as one of the priority areas of cooperation (Chapter 4.5 *Trade-related issues, market and regulatory reform*). The *ENP AP* outlined a whole set of measures aimed at converging Georgia's regulatory framework with the EU standards in this sphere. The government of Georgia was determined to fulfil the *ENP AP* within three years instead of five. Nevertheless, the process of harmonization with EU legislation and the establishment of corresponding practice in Georgia did not proceed as quickly as planned.

The prospect of signing the Deep and Comprehensive Free Trade Agreement (DCFTA) between Georgia and the EU, which became clear in September 2008, gave a fresh impetus to enact reforms in trade-related spheres.² In March 2009, the European Commission (EC) completed and handed over to the Government of Georgia the official document evaluating country's preparedness to start negotiations on the DCFTA, together with a package of recommendations on priority spheres which were in full conformity with the *ENP AP* requirements.

The fulfilment of the above-mentioned recommendations took almost three years to meet the satisfaction of the EC. During that period, the Georgian side, after heated discussions with the relevant EC services, drew up "comprehensive strategies" for three priority areas (technical barriers to trade (TBT), sanitary and phytosanitary measures (SPS) and competition policy) and started their implementation. Certain measures were undertaken in yet another priority area (the protection of intellectual property rights – IPR).

Even though the EU was critical about a number of steps taken by the Georgian government in the process of achieving the set goals in the stated priority areas, in December 2011 the EU decided to launch negotiations with Georgia on the DCFTA.³ Meanwhile, the *ENP AP* term expired but the EU and Georgia have agreed to extend it until after significant progress has been achieved in negotiations on the EU-Georgia Association Agreement, an integral part of which includes the DCFTA.⁴

Four rounds of DCFTA negotiations were held in 2012 (27-29 March, 26-28 June, 24-28 September and 26-30 November). At these rounds the involved parties set up working groups and started negotiations on a whole set of agreement articles, including articles concerning the trade in goods, rules of origin, TBT, SPS, customs administration and trade facilitation, IPR and others. The Georgian side hopes that the progress achieved in the preparatory stage

¹ European Neighbourhood Policy. *EU-Georgia Action Plan*. <http://eu-integration.gov.ge/uploads/ENPAP.pdf>

² *Presidency Conclusions*. Extraordinary European Council, Brussels, 1 September, 2008

³ European Commission. *Implementation of the European Neighborhood Policy in Georgia, Progress in 2011 and Recommendations for action*, Joint Staff Working Document, Brussels, 15.5.2012, SWD (2012) 114 final, p. 9-12. http://ec.europa.eu/world/enp/docs/2012_enp_pack/progress_report_georgia_en.pdf

⁴ *Ibid*, p.2.

will allow the completion of negotiations by the end of 2013. The European side views this aspiration with cautious optimism.

According to public opinion polls, approximation with Europe, including the format of the *ENP AP*, is a matter of great public interest.⁵ Nevertheless, the preparatory stage reforms implemented by the Government to fulfil EC recommendations in the priority areas were characterized neither by transparency nor the high involvement of civil society. Neither did the situation change after the commencement of DCFTA negotiations: the public, including the expert community, have been granted scarce information regarding the progress of the reforms which deprives them of the possibility to make any meaningful contribution to the EU standards convergence process.

The poor communication which has characterized the relationship between society and the government demands greater civil monitoring of the implementation of *ENP AP*. An impartial expert assessment of the progress of reforms will improve the awareness of society and more actively involve it in the process of policy development. This is the ultimate goal of this report.

The aim of this study is to evaluate the progress in the implementation of *ENP AP* through the requirements outlined in its Chapter 4.5 - *Trade-related issues, market and regulatory reform*.

This report covers the following areas:

- Trade;
- Customs procedures;
- Standards, technical regulations and conformity assessment procedures;
- Investments;
- Competition policy.

The main *ENP AP* priority in these areas is the convergence of relevant legislation and institutional framework. Consequently, this study analyses the changes which took place in the country's legislative, institutional or administrative practice in 2012 from this standpoint.

This report draws on the *ENP AP 2012 Implementation Plan (ENP AP IP)*⁶ and the EC report about the implementation of *ENP AP* in Georgia in 2011.⁷ These documents somewhat complement and specify *ENP AP* provisions. The shortage of information about DCFTA negotiations may be partially compensated through meetings with and interviews of participants in this process.

⁵ Eurasia Partnership Foundation. *Georgia Public Opinion. Attitudes Toward European Integration*, October 2009. http://www.epfound.ge/files/eusurveyreport_georgia_aug09.pdf

⁶ European Neighbourhood Policy Georgia-EU Action Plan 2012 Implementation Plan (*ENP AP IP*). http://eu-integration.gov.ge/uploads/9-plan-2012_04_20-eng.doc

⁷ European Commission. *Implementation of the European Neighbourhood Policy in Georgia. Progress in 2011 and recommendations for action*, Joint Staff Working Document, Brussels, 15.5.2012, SWD(2012) 114 final

This report covers the reforms underway in relevant fields from various angles. It reflects the opinions of representatives of the government sector as well as of business circles and independent experts about these reforms.

The report consists of the introduction and five chapters. Each chapter ends with conclusions and recommendations which, in the authors' opinion, will help improve the efficiency of government policy in trade-related spheres and their further convergence with EU approaches.

The report was prepared with the involvement of the senior fellow at the Georgian Foundation for Strategic and International Studies (GFSIS) Merab Kakulia (Introduction, Chapters I and IV) as well as the independent scholars Bondo Bolkvadze (Chapter II), Nino Chokheli (Chapter III) and Irakli Sokolovski (Chapter V).

I. Trade

1. General Overview

One of key aims of the *European Neighbourhood Policy EU-Georgia Action Plan (ENP AP)* is the further economic integration of Georgia with the European Union “based on the adoption and implementation of economic and trade-related rules and regulations.”⁸ The objectives set forth in the *ENP AP* with respect to trade can be broken down into three groups:

The first group concerns the enhancement of bilateral trade relations between the EU and Georgia, inter alia, through increasing benefits from the Generalised System of Preferences and with it, improving Georgia's export performance;⁹

The second group implies the monitoring of compliance with WTO rules and capacity-building on international trade;¹⁰

The third group envisages exploring possibilities for trade and other trade-related agreements, in particular a bilateral agreement on geographical indications (including in the wine and spirits sector) and carrying on negotiations between the parties on the free trade agreement;¹¹

⁸ European Neighbourhood Policy. *EU-Georgia Action Plan*. Introduction.

⁹ *Ibid*, Paragraph 4.5.1. *Movement of goods. Trade Relations*.

¹⁰ *Ibid*.

¹¹ European Neighbourhood Policy. *EU-Georgia Action Plan*. Paragraph 4.5.1. *Movement of Goods, Trade Relations* and the Priority area 3. *Encourage economic development and enhance poverty reduction efforts and social cohesion, promote sustainable development including the protection of the environment; further convergence of economic legislation and administrative practices*.

The fourth group involves trade-related institutional changes including setting up a mechanism to ensure regular consultation/information passing between the government and the trade community on import and export regulations and procedures.¹²

Out of listed objectives, the last two objectives were reflected in the *ENP AP 2012 Implementation Plan (ENP AP IP)*.¹³

During the accounting period, the Agreement between the European Union and Georgia on the Protection of Geographical Indications of Agricultural Products and Foodstuff entered into force. The recognition by the EU of the increasing number of Georgian geographical indications is an important factor for the enhancement of Georgian agricultural exports; hence, the effective support of this process on the part of the Government requires more effort.

The year 2012 saw the launch of DCFTA negotiations with the EU. A change in key negotiators from Georgia in the process posed some risks but their replacement with Deputy Ministers of Economy and Sustainable Development was justified from an institutional standpoint. At the same time, communication with the civil society about the DCFTA negotiations is minimal and requires substantial improvement.

This section of the report also reviews other *ENP AP*-related issues, namely, the enhancement of the EU-Georgia bilateral trade which, despite its overall positive dynamic, is marked with an upward trend in Georgia's trade deficit with the EU. The report also reflects the inefficient use of the preferential trade regime, the GSP+ scheme, which contributed to the unfavourable dynamic of Georgian exports to EU member states in 2012. Bilateral trade relations are discussed in the report in the context of Georgia's trade policy priorities.

During the accounting period, in accordance with the *ENP AP IP*, a number of measures have been implemented regarding the regular consultation/information of the trade community regarding import and export regulations and procedure.

Export promotion policy in Georgia has been mainly limited to sporadic consultation/information and branding/advertising activities. It did not envisage any state support of exporters in financial or credit terms.

5. Conclusions and Recommendations

In accordance with the *ENP AP*, Georgia's trade policy was implemented within the framework of obligations assumed to the World Trade Organization (WTO) during the accounting period; in particular, the compliance with WTO rules were under constant monitoring.

¹² European Neighbourhood Policy. *EU-Georgia Action Plan*. Priority area 2. *Improve the business and investment climate, including a transparent privatisation process, and continue the fight against corruption.*

¹³ European Neighbourhood Policy Georgia-EU Action Plan 2012 Implementation Plan (*ENP AP IP*). Paragraphs 13 and 21.

Declared trade policy in 2012 was directed toward the reduction of the trade deficit through the increase of commodity exports. However, due to insufficient export growth, the negative balance of trade has significantly increased. One reason for this is Georgia's inefficient use of existing free trade agreements (including with Turkey) and preferential trade regimes (including GSP+ scheme).

In parallel with the negotiations on Deep and Comprehensive Free Trade Agreement (DCFTA), it would be expedient to conduct a thorough study of factors impeding the efficient application of preferential trade regimes (especially GSP+), to draw up relevant recommendations and consider them in the process of DCFTA negotiations.

In 2012, the export promotion policy was implemented in accordance with the *ENP AP IP*, though it was limited to sporadic consultation/information and branding-advertising activities. Moreover, it was implemented with the view of the policy of attracting foreign investments and developing tourism.

The transfer of the function of developing and implementing the export policy to the Ministry of Economy and Sustainable Development from the National Investment Agency, because of the change in the institutional status of the latter, may intensify the export promotion policy which must be primarily done by a more efficient use of the existing free trade and preferential trade regimes.

Export promotion in the agriculture sector during the accounting period was mainly focused on the promotion of Georgian wines, thus adversely affecting the realization of export possibilities for other agricultural products. The development of logistics centres in rural areas will have a positive impact on the development of agricultural exports if these centres are integrated into the national quality infrastructure.

The enactment of the EU-Georgia Agreement on the Protection of Geographical Indications for Agricultural Products and Foodstuffs is an important prerequisite for the growth of Georgian agricultural exports. Therefore, it is desirable to set up a working group under the Government, which will coordinate activity related to the recognition of Georgian geographical indications.

The accounting period saw the launch of negotiations on the DCFTA. However, the change in the institutional framework and replacement of the chief negotiators on the part of Georgia in the DCFTA negotiations may adversely affect this process. Still, the coordination of these negotiations by the Ministry of Economy and Sustainable Development is reasonable because this is the Ministry that is responsible for the development of priorities and the directions of trade policy; moreover, the concentration of institutional memory related to DCFTA negotiations in this Ministry seems expedient.

The DCFTA negotiations are closed to the public, thereby depriving civil society of the opportunity to evaluate the results of these negotiations and advocate for necessary reforms.

It is therefore desirable to find a mechanism of communication which will ensure the optimal involvement of the non-governmental sector in the negotiation process.

The new government, having come to power after the 1 October parliamentary elections, tries to take effective steps to better meet the conditions set by the EC as precedents for the launch of DCFTA negotiations. Legislative changes initiated by the new government (for example, in the area of competition policy) may necessitate the renewal of negotiations regarding those DCFTA articles which have already been agreed upon. However, these negotiations must proceed swiftly.

II. Customs Procedures

1. General Overview

Obligations outlined in the area of customs procedures of the *European Neighbourhood Policy EU-Georgia Action Plan (ENP AP)* serve the aim of:¹⁴

1. Streamlining customs legislation in line with EU and international standards;
2. Simplifying customs procedures, namely, increasing transparency of customs rules and tariffs;
3. Correctly applying customs valuation rules;
4. Implementing the principles of risk-based customs control and post-clearance control;
5. Improving customs administration structurally and institutionally, including the introduction of advanced IT technologies.¹⁵

In the past few years, the Georgian government has taken significant steps for the fulfilment of *ENP AP* obligations: customs legislation has been substantially improved; measures to synchronize the Georgian customs administration with its EU counterpart in procedural, organizational and administrative terms have been regularly undertaken. At the same time, many changes have been implemented which seem more experimental and less in line with the obligations assumed under the *ENP AP*.

The objectives outlined in the *ENP AP* in the area of customs administration were duly reflected and specified in the *ENP AP 2012 Implementation Plan (ENP AP IP)*. In accordance with this document, risk-based customs control has been improved through the establishment of an automated risk management system; the development of a standard operating procedure manual and guide for customs valuation; the introduction of a customs post-clearance control manual; the opening of new economic zones based on the “one-stop-shop” clearance principle; the conclusion of agreements on customs cooperation and integrated border management with some neighbouring countries; the implementation of

¹⁴ European Neighbourhood Policy. *EU-Georgia Action Plan*. Priority area 2. *Improve the business and investment climate, including a transparent privatisation process, and continue the fight against corruption.*

¹⁵ *Ibid.*

trade facilitation system with the Data Exchange Agency of the Ministry of Justice; cooperation with customs traders deepened through improved education about on-going and expected reforms; and the improvement of customs control in the area of IPR protection.

The Revenue Service of Georgia, with customs administration as one of its units, is a structure undergoing rapid reform. However, one must note those weaknesses which are still observed in its performance. Bearing in mind that the majority of customs officers have a working experience ranging from two to five years, it's quite a large undertaking for the Revenue Service to create a pool of professional officers who observe high ethical standards. The intensive development of IT technologies is a necessary part of the reform, which must be sustained. Besides, even though customs procedures have been substantially simplified and have become more transparent, some obsolete procedures are still practiced, for example, the so-called "reserve method" of determining customs value, i.e. the practice of applying minimal values. Moreover, there are instances when problems arise if customs traders carry out non-standard transactions, which may impede clearance.

A more detailed overview of the *ENP AP* implementation in 2012 as regards customs administration and an evaluation of key obligations are provided below.

4. Conclusions and Recommendations

The enhancement of a risk management system in every possible direction of customs administration and control still remains a top priority among the obligations assumed by Georgia under the *ENP AP* in the area of customs administration. The efficiency of existing risk management modules needs to be revised and an evaluative mechanism developed.

The Revenue Service must drop the practice of the voluntary pricing of imported goods using the so-called "minimal values" method when determining customs value. To this end, educational work must be continued in order to upgrade the professional qualification of customs officers as well as to better inform private sector representatives about the rules of customs valuation.

In parallel with procedural simplification, the customs audit function must be augmented to counterbalance the weakening of control brought about by these simplified procedures so as to avoid any impediments to the economic activity of custom traders. In this regard, international best practices are crucial and international donor organizations must play a leading role in providing them.

The large-scale introduction of the "one-stop-shop" principle at Georgia's customs checkpoints must be assessed as a positive development, causing satisfaction among private sector representatives.

The agreements achieved during the accounting period with the government of Turkey are very important, as they foster cooperation in the management of customs checkpoints.

Similar agreements with other neighbours of Georgia, especially with Azerbaijan, are highly desirable.

The development of information technologies within the customs administration is an inseparable aspect of the reforms but in a number of instances some deficiencies in information technologies, including in ASYCUDA World software, were revealed. To further increase the efficiency of the customs administration, the development of information technologies and their sustainability must be carried on.

A large segment of Georgia's customs officers still fall short of the desired level of professionalism. The Revenue Service must continue to establish a transparent system of performance evaluation, motivation, incentives, promotion, and demotion. At the same time, the intensity of training programmes should be maintained and further developed.

To improve the protection of IPR at customs checkpoints, the customs administration must raise the awareness of its officers regarding IPR-related issues, create effective mechanisms for cooperation with IPR holders and eliminate risks of impediment in customs clearance because of IPR.

Significant differences remain between Georgia and EU countries in the area of customs legislation and procedures. Among them are: the terms of application of customs regimes, the use of customs guarantee, a standard practice of customs clearance of goods, etcetera. It is desirable to carry out a comparison and detailed convergence of EU and Georgian customs procedures. This must be done within the shortest possible timeframe and, moreover, with the involvement of the private sector. Otherwise, problems caused by unstable legislation and experimental changes will continue to emerge.

III. Standards, Technical Regulations and Conformity Assessment Procedures

1. General Overview

One of *European Neighbourhood Policy EU-Georgia Action Plan (ENP AP)* priorities is the establishment and strengthening of a modern institutional system of technical regulation, standardization, accreditation, metrology, conformity assessment and market surveillance.¹⁶ This priority area aims at establishing sound trade policy and decreasing non-tariff barriers to imports as well as creating opportunities for Georgian products to access international markets through the development of quality infrastructure. The corresponding provisions of the *ENP AP* can be grouped into two main objectives: the strengthening of quality infrastructure institutions (accreditation and standards and metrology bodies) and their integration into international organizations; and the synchronization of relevant legislation, including technical regulations, with international and EU legislation.

¹⁶ European Neighbourhood Policy. *EU-Georgia Action Plan*. Priority area 3. *Encourage economic development and enhance poverty reduction efforts and social cohesion, promote sustainable development including the protection of the environment; further convergence of economic legislation and administrative practices.*

Since 2005, Georgia has actively pursued a trade liberalization policy which implies the unilateral abolition of tariff and non-tariff barriers to trade. As a result of this course, the Georgian legislation and institutional framework is in line with the WTO Agreement on Technical Barriers to Trade (WTO TBT) and EU principle in the areas of quality infrastructure. Georgia introduced a system of voluntary standards and extremely liberal approach to technical regulation. In addition, conformity assessment functions have been distributed between the private and public sectors. The adoption of the Code on Security and Free Movement of Products in 2012 has further strengthened these approaches.

To support the export of Georgian products, quality infrastructure institutions need to be strengthened and further developed in order to gain international recognition. To this end, over the past few years the key objective of the Georgian National Agency for Standards, Technical Regulation and Metrology (GEOSTM) and the Georgian Accreditation Centre (GAC) has been integration into relevant international organizations and the consequent achievement of a multilateral recognition regime. This objective was adequately reflected in the *ENP AP 2012 Implementation Plan (ENP AP IP)*. Consequently, during the assessment period, the GEOSTM and the GAC were largely oriented toward the achievement of this objective. The establishment of a quality management system and the related capacity building of personnel – these being among the prerequisites for membership into and recognition by international institutions – were actively carried out both in the GEOSTM and the GAC. Even though the state declared this goal as a priority, institutional development, staff trainings and technical equipment upgrades were carried out mainly with the assistance of donor organizations. The rapid development of this sphere requires adequate support from the state as well. It is also desirable to step up the process of the adoption of international and European standards as national standards and to ensure their translation in priority sectors. The GEOSTM must continue its work with the private sector to promote international standards.

The *ENP AP 2012 Implementation Plan* is bereft of measures to be implemented in the spheres of technical regulation and market surveillance. Significant progress was observed in the convergence of Georgia's technical regulation legislation with relevant EU laws at the preparatory stage of DCFTA negotiations. The Strategy in Standardisation, Accreditation, Conformity Assessment, Technical Regulation and Metrology and Programme on Legislative Reform and Adoption of Technical Regulations of the Government of Georgia, which was adopted in 2010, set out a schedule for the incorporation of the EU New Approach and the Global Approach Directives into the national legislation. In 2011, the first group of directives was introduced, and in 2012 work on the translation of the three remaining directives and their adoption as technical regulations was continued. At the same time, the mechanism for applying the technical regulations of other countries in Georgia remains a problem, which questions the effectiveness of the existing system of conformity assessment and market surveillance. Bearing this in mind, an intensive stage-by-stage renewal of national technical regulations must be carried out, including the introduction of the EU New Approach and the Global Approach Directives. At the same time, surveillance bodies must be strengthened,

particularly through the training of personnel, in order to be able to conduct effective control in accordance with the new technical regulations.

Among the notable reforms implemented during the period covered by this assessment is the market surveillance model which was defined in the Code on Security and Free Movement of Products and, according to which, market surveillance functions were redistributed asymmetrically between the private and public sectors. The Technical and Construction Inspection Agency, established in July 2012, was tasked only with the control of documents of regulated objects/entities while private inspection bodies were solely empowered to carry out on site technical inspections. Nevertheless, no private inspection body has yet been established and the Agency continues to perform the function of technical inspection until such bodies are created. Consequently, the material and technical as well as the human resources of the Agency, which are designed mainly for performing the control of documents, are inadequate for the *de facto* functions of the Agency.

2. Conclusions and Recommendations

The reforms implemented in the removal of technical barriers to trade during the reporting period must generally be assessed as positive. In terms of compliance with international obligations (WTO TBT), Georgia is marked by outstanding liberalism. There are, in fact, no technical barriers to imports; however, shortcomings in the national quality infrastructure create barriers to the export of Georgian products to the European market.

At the same time, the citizens' legal right to safe, harmless and quality products, as well as a safe working environment, is not protected. Such unilateral liberalization puts local producers in a disadvantaged condition vis-a-vis low-quality and often hazardous imported products.

The existing market surveillance model clearly lacks balance with regard to the distribution of functions between the private and public sectors. Facility site inspection is entirely privatized. Since this model has not been put into practice yet, it is difficult to assess its effectiveness. However, it is already apparent that it raises many questions: how competent will a private inspection body be? Is accreditation a sufficient mechanism for entirely turning over the inspection of high-risk enterprises to private bodies? While, for fear of corruption, the government restricts control over business by state bodies, what mechanism exists to avoid corruption in the private sector?

No matter whether or not this model will exist, the market surveillance body – the Technical and Construction Inspection Agency – needs to be enhanced and equipped with corresponding material and technical means and the qualification of its personnel must be upgraded in order to effectively handle even those minimal functions with which it has been legally ascribed.

There is no body which will control the compliance of products belonging to non-regulated spheres with the general product safety requirements.

While the recognition of the technical regulations of developed countries as equivalent, and of documents issued by the accredited conformity assessment bodies of these countries according to the Code on Security and Free Movement of Products is a very progressive approach, the mechanism of application of technical regulations of other countries on the territory of Georgia by local producers requires revision. Instead of the aforementioned approach, national technical regulations must be gradually updated. The New Approach and the Global Approach EU Directives must be introduced and the requirements of such technical regulations must be applied to local producers. Otherwise, there is a danger that the state control and technical inspections in regulated spheres will be ineffective. Moreover, an approach for the control of products belonging to regulated spheres, which are imported from developing countries, must be deployed.

For a full enactment of the Code on Security and Free Movement of Products, the government, in 2013, must continue active work on the drafting and adoption of a whole set of bylaws as defined by transitional provisions of the Code.

Work must be carried on to ensure the strengthening of the quality infrastructure institutions of Georgia and their compliance with international best practice. The enhancement of the Agency for Standards, Technical Regulation and Metrology and the Accreditation Centre and their membership in international organizations will be a significant prerequisite for the promotion of Georgian exports to western markets. Work with the private sector for the promotion of international standards must also continue.

Currently, quality infrastructure institutions have been developed thanks to donor assistance. The state must realize the importance of this system for the business sector and must also invest in the advancement of this sphere.

IV. Investments

1. General Overview

One of the key priorities of the *European Neighbourhood Policy EU-Georgia Action Plan (ENP AP)* is the improvement of the business and investment climate¹⁷ which is aimed at creating conditions which better encourage investment and economic activity. Within the *ENP AP* format, the creation of such conditions is related to two groups of objectives with the first group involving the establishment and operation of companies¹⁸ while another group is specifically related to foreign investments.¹⁹

¹⁷ European Neighbourhood Policy. *EU-Georgia Action Plan*. Priority area 2. *Improve the business and investment climate, including a transparent privatisation process, and continue the fight against corruption.*

¹⁸ European Neighbourhood Policy. *EU-Georgia Action Plan*. Priority area 2, paragraph 4.5.2. *Right of establishment, Company Law and Services.*

¹⁹ *Ibid.* paragraph 4.5.3. *Movement of capital and current payments.*

As regards the objectives of the first group, the past few years have seen notable progress in the area of establishment of companies (including those created with foreign capital), namely in terms of registration and licensing. This progress is clearly reflected in international business rankings.²⁰ At the same time, recent rankings also clearly show the violation of investors' property rights, low levels of judicial independence, state favouritism toward specific companies, an imperfect mechanism of dispute resolution,²¹ the weak execution of contracts and an inefficient bankruptcy process.²² In 2012, the situation had not essentially changed: the investment climate has remained inconsistent, creating huge difficulties primarily for local investors.

The second group of objectives in the *ENP AP* involves ensuring the free movement of capital invested in companies in the form of direct and other investments; the protection of such foreign investments and the liquidation and repatriation of profits and capital as well as an exchange of information about the present legal and regulatory regime as concerns capital movement. Georgia has not experienced significant problems in these areas for quite a long time. In the accounting period, the Georgian government tried to create additional incentives for foreign investors while still remaining less tolerant toward local investors.

Measures in the *ENP AP 2012 Implementation Plan (ENP IP)* designed to support investments are mainly focused on foreign investments and include the following directions:

- Organisation of business, including investment forums with the outlook to deepen the cooperation between Georgian and foreign manufacturers;
- Preparation of investment proposals for foreign investors;
- Introduction of an investor post-service system (Aftercare) for re-investment purposes;
- Global advertising of Georgian investment potential.²³

The *ENP AP IP* only partially reflects the objectives set out the *ENP AP* in terms of the investment sphere. Therefore, in addition to analysing the implementation of the measures envisaged in the *ENP AP IP*, this section of the report also reviews the priorities and investment policy instruments in 2012, institutional changes, as well as EU investments in Georgia.

4. Conclusions and Recommendations

Georgia's declared investment policy in 2012 was in line with the *ENP AP*. Although the state has been especially tolerant toward foreign investors, the National Treatment Regime

²⁰ IFC, World Bank. *Doing Business 2013 data for Georgia*,
<http://www.doingbusiness.org/data/exploreeconomies/georgia>

²¹ World Economic Forum. *The Global Competitiveness Index, 2012-2013*, Insight Report, p.175.
http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

²² IFC, World Bank. *Doing Business 2013 data for Georgia*,
<http://www.doingbusiness.org/data/exploreeconomies/georgia>

²³ European Neighbourhood Policy Georgia-EU Action Plan 2012 Implementation Plan. Paragraph 13.

was actually inoperative which, was expressed by the infringement of the interests of local investors, particularly with regard to property rights.

The new government's efforts to create solid legal guarantees for the protection of ownership rights deserve support. At the same time, to ensure the effective support of investors it is desirable that the National Investment Agency enacts the means envisaged by the law, such as subvention, guarantee and subsidy.

A cornerstone of the policy of attracting investments in the accounting period was the idea of creating regional business platform in Georgia. To that end, the government offered new incentives to investors but these did not bring any tangible results. Additional benefits established in free industrial and tourism zones for investors have also proved inefficient thus far. Nonetheless, we believe that the existing benefits should be maintained and further elaborated so that, in the climate of a fair and predictable economic and geopolitical environment, they will definitely produce significant results.

In 2012, as a result of institutional changes implemented in the sphere of investment policy, the development of policy has been separated from its implementation with the Ministry of Economy and Sustainable Development being in charge of policy development and the JSC Partnership Fund and the Strategic Development Agency being tasked with policy implementation. A new institutional framework is, in general, acceptable but is not insured from an overlapping of functions. Therefore, we think that functions between the mentioned units need to be separated more explicitly.

Given the aims and the size of the Partnership Fund's assets, it is necessary to ensure the maximum transparency of this institution. It would also be advantageous to abolish the Strategic Development Agency and to transfer its on-going projects (if any) to the Partnership Fund.

In accordance with the *ENP AP IP*, several sectorial studies have been conducted for the aim of developing investment proposals. The National Investment Agency introduced the investor post-service (aftercare) system with the aim of promoting reinvestment; several investment forums were organized and a global advertising campaign to promote the country's investment potential was conducted.

ENP AP IP envisaged the execution of bilateral agreements on avoiding double taxation with three more EU member states during the accounting period. Such agreements were signed with two EU member states (Hungary and Portugal). Taking into account that similar agreements have been initialled with three EU member states (Slovenia, Cyprus and Sweden), it seems absolutely feasible that in near future the government will sign agreements on the avoidance of double taxation with all 27 EU member states.

V. Competition Policy

1. General Overview

The *European Neighbourhood Policy EU-Georgia Action Plan (ENP AP)* identifies the competition and state aids policy as a priority direction in bilateral relations. According to the *ENP AP*, Georgia must ensure the convergence of its legislation with EU principles on competition, including through the enhancement of the independence of the Free Trade and Competition Agency and the optimization of administrative capacity.²⁴

The convergence of the competition legislation with the *acquis* was defined as an indispensable prerequisite to the launch of negotiations on the DCFTA. On 3 December 2010, the Government of Georgia adopted the Comprehensive Strategy in Competition Policy²⁵ (hereinafter Strategy) aimed at bringing competition legislation in line with the best international standards. The document reflects the stance of Government of Georgia (GoG) with regard to competition policy and outlines the list and timetable of the measures for the implementation of the Strategy. The actions set out under the Strategy concern institutional and legislative reforms, enhancement of administrative capacity and involvement of interested stakeholders.

A special group set up in the Government of Georgia in accordance with the Strategy, prepared, together with EU experts, the draft Law on Free Trade and Competition, which was adopted by the Parliament of Georgia on 8 May 2012. The Law on Free Trade and Competition (hereinafter the Law) sets out the principles for the protection of free and fair competition from undue restrictions and defines the legal means and grounds for preventing breaches of competition rules and enforcement of the competition policy. The main provisions of the Law are reviewed in a corresponding section of this report.

The measures outlined in the Strategy have been partially reflected in *ENP AP 2012 Implementation Plan (ENP AP IP)*. In particular, this document defines the actions to be implemented by the Government of Georgia in the area of competition, which can be divided into the following groups:

The first group includes the drafting of normative acts in accordance with the Law on Free Trade and Competition.²⁶

The second group envisages the training of the personnel of the Competition and State Procurement Agency and other relevant public officials, including judges, on competition issues as well as the organization of a seminar on state aid for the same target group.²⁷

²⁴ European Neighbourhood Policy. *EU-Georgia Action Plan*. Paragraph 4.5.5. Other key areas; Competition policy.

²⁵ Decree #1551 of the Government of Georgia, dated 3 December 2010, *On the Approval of the Comprehensive Strategy in Competition Policy*.

²⁶ European Neighbourhood Policy Georgia-EU Action Plan 2012 Implementation Plan. Paragraph 17, subparagraph 1.

The third group of actions envisages the organization of a conference in order to inform the private sector on competition legislation.²⁸

The fourth group refers to the elaboration of the normative act on the general rule for the provision of state aid.²⁹

Out of the listed measures, the most urgent is drafting of normative acts in the area of competition and state aid because these normative acts represent a prerequisite for the effective implementation of the Law. However, this objective has been partially achieved.

During the assessment period certain steps have been taken toward the enhancement of administrative capacity, mainly in the form of organizing seminars and study tours for relevant personnel. Especially noteworthy is the training on competition conducted for Georgian judges. At the same time, against the backdrop of efforts to enhance administrative capacity, almost no steps have been undertaken to inform the private sector on reforms to the competition legislation. The involvement of the private sector in drafting and evaluating the Law was minimal. A more detailed analysis of the implementation of measures planned by the government is provided in a corresponding section of this report

This report is not limited to the analysis the implementation of *ENP AP IP* but reviews all problematic aspects of the competition legislation. The document focuses on the competencies of the Competition and State Procurement Agency (hereinafter the Agency) and on those exceptions which (may) prevent or restrict the application of the Law.

4. Conclusions and Recommendations

In accordance with the *ENP AP IP* and the Strategy, essential steps were taken in the accounting period for harmonizing Georgian competition legislation with international and EU standards. Among these measures, especially important is the adoption of the Law on Free Trade and Competition. However, the full implementation of the Law did not take place during the accounting period.

Pursuant to paragraph 8, Article 34 of the Law, a precondition for the exercise of powers by the Agency, as defined by the Law, is the preparation and adoption of normative acts which did not take place in the accounting period. Apart from the fact that this does not comply with the *ENP AP IP*, the absence of normative acts entails significant legal results: namely, until these documents are adopted, the Agency cannot implement its functions, including the competences of receiving complaints and applications from economic agents as well as the ability to launch inquiries into the facts of alleged breach of competition rules. In the absence of such normative acts, the new initiative of the Ministry of Economy and

²⁷ European Neighbourhood Policy Georgia-EU Action Plan 2012 Implementation Plan. Paragraph 17, subparagraphs 2 and 4; paragraph 18, subparagraph 2.

²⁸ *Ibid.*, paragraph 17, subparagraph 3.

²⁹ *Ibid.*, paragraph 18, subparagraph 1.

Sustainable Development of Georgia to open an anti-monopoly hotline may prove inefficient. Without defining the corresponding procedures in normative acts, the application of those mechanisms, which are envisaged in the Law, against violations of competition detected by means of the hotline will be impeded. Consequently, an immediate objective is to adopt the normative acts envisaged by the Law as soon as possible.

According to the Law, the Government of Georgia approves the priority directions of the Agency's activity. The Agency may probe only those cases, which fall within scope of the adopted priorities. Thus, when identifying priorities, the GoG should take into account urgent needs of the society and prioritize those spheres which attract high public interest and have a significant influence on the daily life of society. At the same time, priority directions must not be identified narrowly so as to limit the possibilities of economic agents to apply to the Agency and thus render the application of the Law ineffective.

The Law has broadened the list of competences of the Agency as the main regulator of the competition sphere, to include, *inter alia*, inquiries into breaches of requirements of the Law and, in certain cases, the imposition of a penalty on an economic agent. It also grants broad powers to the Agency to conduct investigations into violations of the Law. On the other hand, however, the Agency is not equipped with *ex officio* powers and can launch investigation only on the basis of complaint/application submitted by legal or physical persons. It is desirable to assign the Agency with the power to open investigation proceedings on its own initiative within, at least, the priorities defined by the Government of Georgia and in cases of gross violations of competition rules.

The merger of the competition and state procurement agencies can be viewed as an administrative enhancement of the Agency. As a result of this merger, the Agency has the opportunity to use the legal and analytical departments of the State Procurement Agency to inquire into facts of competition violation or to carry out thorough analyses of various market segments. Given the complexity and difficulty of competition cases, it is desirable to allocate additional resources which would be used to invite and involve independent experts in investigation of competition cases.

In 2012, the training of the Agency personnel and other public officials, including judges, was conducted in accordance with the *ENP AP IP*, though it was not enough for the enhancement of administrative capacity. Consequently, an active retraining process must continue. In addition to the public servants, it would be desirable to engage representatives of civil society and the private sector in this process.

Throughout 2012, the involvement of civil society and private sectors in the consideration of the Law on Free Trade and Competition was minimal, which limited the possibility of making a critical assessment and of introducing certain changes. At the same time, the DCFTA negotiations are closed and the civil society is deprived of any possibility to evaluate negotiation results in the area of competition.

Information channels through which primary consumers of the Law (entrepreneurial and non-entrepreneurial entities) would be able to receive information about the content and proper application of the Law are rather limited. It will be advantageous to draw up manuals and guides which, along with interpretation of the Law, would also provide examples of situations and instances for illustration purposes. Such a strategy will help to ensure clarity in the application of the law and assist relevant economic agents to better evaluate the compliance of their actions within the requirements of the Law.