

Development Debates - Georgia

Report to the World Bank Office in Georgia

1. Debate on “PARTICIPATORY AND EFFECTIVE MONITORING OF PRSP IMPLEMENTATION”

Time and place

The debate was held in the conference hall of the Hotel “TORI, Tbilisi, on 21st of November 2002. The debates started at 15:00 and lasted 2 hours. In total 22 persons participated in the debates. The list of participants is attached (see Annex).

The package of materials was distributed in advance to all participants, including:

1. Invitation letter
2. Introductory letter about PSI and its involvement in PRSP development process
3. Description and proposed format of the debates
4. The list of invitees
5. The Case Study “Participatory and Effective Monitoring of PRSP Implementation: Selected Discussion Topics” (both English & Georgian versions)
6. Other reading materials

The participants received an additional package of materials at the beginning of the debates consisting of the Document provided by the World Bank Institute (Recommended Practice of PRSP)

Debates

Authors of the case study made brief comments regarding their vision of participatory strategy of PRSP in Georgia. The facilitator briefly reminded about the purpose and the format of the debates.

Initially there were no questions regarding the case study.

The debate started with the discussion of the main question:
Is the suggested Participatory strategy applicable to Georgian context?
Particularly:

1. Does the presented strategy insure public awareness, support of the population to the Program and generation of the sense of ownership;
2. Does the presented strategy insure active participation of society in the management and administration of the program:
 - a. to insure public participation in the process of monitoring and evaluation of the program
 - b. to insure the feedback so, that the results of monitoring and evaluation should be considered in the process of further optimization of the program
3. Does the presented strategy insure active public involvement in the process of implementation of the program
4. Does the presented strategy insure such institutional organization of the program that society would have the direct addresser in the center

All participants of the debates emphasized the importance of participation and noted that participation is the main issue that differs the PRSP from all other existing governmental programs. Therefore the debate concerning participation does not address the question of whether, but how.

The presented strategy of participation was in whole approved by the participants of the debates. It was noted, that the strategy answers all the main requests formulated in the objectives of participation. Mainly, it was stressed the importance of access to the information: only informed and educated society is the guarantee of the accountability of government and success of PRSP. The program will be successful if the global strategy of the program will reach every concrete individual.

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One of the main outcomes of the debate was that participation is considered as **an opportunity of further development of democratic institutions in Georgia.**

The member of editorial board of PRSP Mr. Devi Khechinashvili emphasized, that the process of participation promotes development of both: self-governance and civil society. Today both of them are very weak because of absence of clearly determined and identified functions, capacity, finances etc. Therefore it is considered that participation will enhance their capacity building and stimulate their activity. Self-government and other civil society organizations will try to find the optimal ways of cooperation. In this respect participants of the debates (Mr. Fletcher, Ms. Danelia, Mr. Svani) stressed the role and importance of yearly regional and national conferences. First of all, such conferences play an important role in the sharing of experience. They will bring to light the problems and achievements in the implementation of the program at the regional and national level (best practice). Secondly, the conferences will create an incentive for local organizations to represent themselves at the national level.

Ms. Alkhasishvili noted the importance of representativeness in the process of social dialogue and the problems connected with the involvement of new groups of civil society in this process.

At the same time Mr. Bokuchava and Ms. Gudzaraidze pointed out two aspects that have to be considered during the process of co-operation with self-government:

1. loss of independence by the CSOs
2. duplication of functions between the SCO and local government

Mr. Dzamukashvili stressed a novelty appearing in the strategy - the proposition for setting up a special body to supervise and assess the execution of the strategy by the civil society. This is to be an independent 'Council of Economic Development and Poverty Reduction in Georgia'. Members of the commission would be drawn from organizations representing civil society. The commission would cooperate with the government within the framework of regular meetings and would communicate with the organizations (around 750 NGOs) at annual conferences. These would judge the implementation of the strategy and would shape the direction of propositions for change and further development, setting out definitive strategic priorities.

Mr. Areshidze (PSI) stressed, that securing a position of the "Council" by the President (a proposed legal requirement for the functioning of the commission)

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creates a risk, that changes within the structure of the highest executive level of government may interrupt the functioning of this body.

Mr. George Tarkhan-Mouravi pointed on the main advantages of the strategy: an organization of permanent social dialogue and social participation; social awareness of national problems rises, which is the basis for forming a sense of joint responsibility for the nation's fate; organizations growing bottom-up gain a forum for presenting their problems; organizations gain knowledge, experience, they learn civic attitudes (capacity building).

At the same time Ms Paichdse put a question whether the transaction costs of conducting a permanent social dialogue is considered in the strategy.

To summarize, the main concern of participants were as follows:

1. To what extent the results of monitoring will be considered in further evaluation of the program
2. How can be achieved the sustainable participation of SCO (NGO, CBO, business communities and other groups of civil society)
3. Will the SCO 's independence be guaranteed
4. How will be achieved that there will be no limitations for involving new groups (SCO)
5. Does the strategy guarantee the avoidance of duplication of functions between the SCO and local government.

Conclusions

The main conclusions of the debate were as follows:

1. The suggested strategy (if it will be followed) will ensure access to the information for all the interested members of society.
2. The proposed institutions of participation will guarantee the intermediate role between the governmental structures and the civil society (instrument for social dialogue)

We have summarized the main advantages, problems and risks of the proposed strategy in the Table1. (See bellow)

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Table 1.

ADVANTAGES	PROBLEMS	RISKS
Supports social dialogue (instrument)	Representativeness	Conflict with parliament
Supports the bottom up process	Co-operation with self-government	Structural changes within the senior executive level (with regard to the location of the PRSP Council of Georgia)
Promotes horizontal accountability	Transaction costs	Loss of independence by the SCO
Increases access to information		Duplication and overlapping of functions
Promotes capacity building		
Promotes civic control		

2. Debate on “Business Environment”

Time and Place

The debate was held in the conference hall of the Hotel “TORI, Tbilisi, on 22nd of November 2002.

The debates started at 15:00 and lasted 2 hours.

In total 25 persons participated in the debates. The list of participants is attached (see Annex).

The package of materials was distributed in advance to all participants, including:

7. Invitation letter
8. Introductory letter about PSI and its involvement in PRSP development process
9. Description and proposed format of the debates
10. The list of invitees
11. The Case Study “Business Environment in Georgia: Selected Discussion Topics” (both English & Georgian versions)
12. Other reading materials

The participants received an additional package of materials at the beginning of the debates consisting of the Document provided by the World Bank Institute (Recommended Practice of PRSP)

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Debates

Mr. Devi Khechinashvili, PSI Chairman of The Board, who briefly reminded the audience about the purpose and the format of the debates, opened the debates.

The case study distributed to the participants in advance was centered on, and the debates were supposed to focus on the tax barriers to business development in Georgia, as well as related problem of economic corruption. Initially there were no questions regarding the case study.

The discussion was opened by Mr. Archil Melikadze, Director of the Center for Enterprise Restructuring and Management Accounting (CERMA). He summarized the experience of CERMA regarding the issues raised in the case study. The two basic themes were voiced:

- 1) While most of the criticism towards Georgian Tax code customarily centers on the *height* of the taxes, the real problem is the inequality of entrepreneurs against the Tax Administration in Georgia. Whatever the taxes are, some businesses are practically exempt from them while some are (or at any moment may be) requested to pay them in full. Not the taxes themselves are ruinous to businesses but the gap, which differential treatment creates between the fortunate who have a protector and those who lack one.
- 2) Whatever the formal tax calculation mechanisms are, (e.g. 20% of company profit), the actual procedure employed in most cases by tax collectors is the visual inspection of a business (premises, number of workers, type of the car the businessman has, etc.) and setting the corresponding tax target. That is, the actual mechanism is much simpler (and much more subjective) than formally required. Why not simplify the formal mechanism while retaining its objective basis?

Other participants then further developed the two above themes. Mr. Chkheidze noted that, particularly, VAT poses significant problems for the administration and is the main source of subjectivity (hence *inequality*) in taxation. Participants cited the examples of different countries where either the introduction of VAT failed or the tax was abolished, or where the tax was not introduced at all due to expected problems with its administration. It was generally agreed that for a country with

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as short current history of market relationships, and nascent taxpaying culture, as Georgia has, VAT is far not appropriate tax instrument.

Mr. Gia Jandieri from the Open Society – Georgia Foundation, presented the new model of the tax code elaborated by independent economic experts within the project funded by OSGF, the model is sometimes referred as “Orvelashvili” model, by the name of its principal author, or as “Industrialists” model, by the name of the political party with which it is often incorrectly associated. The model is radically different from the present tax code in that it:

- 1) Eliminates social taxes – it is assumed that there is no reason why social protection should not be largely delegated to individuals themselves and private pension funds. Or, from another perspective, if social tax is still something to be collected by the state, then why not also collect defense tax, police tax, education tax, etc.
- 2) Sets enterprise profit tax rate at 15%;
- 3) Proposes two optional regimes for personal income taxation: family (15%) or individual (10%) scheme;
- 4) As regards VAT, the speaker noted, while to eliminate it completely would be the best solution, the strategic objective of harmonizing Georgian legislation with that of EU would prevent this. Though, the easy way round would be just to set the VAT rate at 0%, while leaving the tax in the code;
- 5) Eliminates most of the “nuisance” taxes;
- 6) Proposes much simplified tax administration model.

One of the salient features of the new model is the introduction of private arbitrage for resolving disagreements between businessmen and tax service. It was noted that both businessmen and tax officials commend this novelty. Unfortunately, this is prohibited by the Georgian Administrative Code. A number of civil society organizations (PSI, ABED) are actively advocating respective legal changes.

It was also stressed that the issues of *high* taxes in Georgia should not be disregarded at all. This is still relevant point and may easily be connected with the *inequality* issue. First, the taxes are indeed *high* in Georgia, for the given local level of public good and services, risk of doing business, and cost of capital. Any mechanical comparison of tax rates between Georgia and other countries is

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meaningless without the simultaneous comparison of the named factors. Second, the higher taxes, the higher protecting barrier around those who do not pay these, e.g. higher the *inequality*.

The general agreement on the above issues was challenged by the question of: If we all know so well that Georgian Tax System is so bad, why we do not change it?

Two main obstacles were named by meeting participants:

- 1) Resistance of those who benefits from the existing state of affairs – corrupt officials and associated businesses;
- 2) Resistance of the IMF to accept legal changes without comprehensive impact analysis

George Loladze, Georgian Stock Exchange Chairman of the Board proposed a possible way to overcome the problem, elaboration of detailed and realistic business-plans for enterprises, different industries, regions, and, as a result, for the country as a whole, was suggested. Such modeling exercise, which should actively involve business associations, governmental bodies, as well as development institutions, would make it possible to pretest tax systems (scenarios) in their fiscal, economic, and social impact and determine the optimum which should be implemented. The models will also be productively used to forecast economic performance of regions and accordingly plan state budgets. Some skepticism was, however, voiced at the same time regarding the reliability of the initial data (basic economic indicators) that are to be fed into the models.

Another important issue raised by Mr. Gia Areshidze of PSI was the supremacy of property rights, which are hardly adequately protected at present. According to a survey by PSI, a lawyer is only in the 10% of cases may reasonably predict the outcome of court hearing on property right issues. As an example, the present legal provision was cited that allows for expropriating excisable goods sold without the excise stamp. Common agreement was that the adoption of the new organic property law should enter the current policy agenda.

It was agreed that private property and rule of law are the cornerstones for economic freedom and development. The lack of the latter was cited as the main

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reason for the establishment of private centralized economic controls in Georgia that replaced Government centralized controls. At this point, the link between the Rule of Law and Corruption, or better, as had been emphasized in the case study distributed to discussion participants, the exact opposition of Corruption and the Rule of Law was pointed out. Therefore, the measures to strengthen the rule of law should be the principal way to counter corruption. However, such measures should concentrate on reducing the gap between the current legal system and socially approved systems of behavior and dealing, rather than on the enforcement of the existing laws, which are partly viewed as culturally illegitimate.

At the end of the discussion of the problems that the inadequate legal system poses to businesses the note of Mr. Lancelot Fletcher of AmCham/GBC was met with common approval. He suggested that currently in Georgia most of the discussions on economic themes, formal or informal, center on the *problems and barriers* that face entrepreneurs. Some positive shift of the perspective is obviously required so that strategic goals of human development, prosperity, high quality of life, as well as the abundant positive factors that should ensure these (rich human resources, developed social capital etc), are not completely overshadowed by destructive actions and attitudes.

The discussion, then, moved to another theme raised in the case study – business registration system, which, though admittedly does not pose any significant difficulties to businesses themselves, often does so for third parties in that it leaves much room for fraud and corruption.

The speech of Mr. David Tarkhan-Mouravi, Head of the State Department for Informatics, was met with significant interest and opened new avenues for the discussion. Mr. Tarkhan-Mouravi spoke about the new governmental plan to introduce electronic business (as well as personal) identity cards (passports) that would register all the transactions in which the business engages itself. All the information will also be stored in the centralized database. Interconnection of such national systems through satellite links is also conceived. In case the bilateral agreements are signed with other countries, the cards may be used (read by third parties) internationally.

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At present, the main purpose of introducing the cards is to counter the smuggling of goods into Georgia. Decentralized inland customs system that currently operates in Georgia allows, by different estimates, for up to 90% of goods entering the country to avoid customs clearance. The proposal is to provide all the imported goods shipments with the temporary electronic IDs where the shipment parameters (volume, value, goods nomenclature, etc.) and destination customs point are recorded, either on border or during the pre-shipment inspection. The information stored on the card may not be changed, thus it will be easy for any inspector to determine whether the shipment was tempered with or misdirected.

Although not at this stage explicitly meant to improve business registration system, the implications therein of the novelty are clear. Besides, the system is viewed as an important drive for legalizing business that is largely in shadow at present, and its subsequent capitalization.

Conclusions

It was agreed that *inequality* – differential treatment of entrepreneurs by authorities (not necessarily tax authorities) is the principal problem regarding the business environment in Georgia. The main causes of, or closely linked phenomena to, inequality are the deficiency of the legal system, lack of the rule of law, and corruption.

Most of the participants agreed that the Tax System currently operational in Georgia is inadequate to the economic needs and realities of the country, and must be fundamentally reviewed within the framework of the participatory public/private dialogue.

Implementation of large-scale micro- and macro-economic modeling (including social impact assessment) project is viewed as a necessary exercise to improve the government finance management and bring the dialogue with stakeholder organizations and development institutions on a higher level of quality. The capacity building assistance from the donor organizations should be very important.

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Protection of property rights is of crucial importance to the economic development in Georgia and needs adequate institutional building.

Active use of the informational technologies was agreed to hold a large potential for improving business environment in Georgia.

Fight with Corruption by general agreement should happen mostly through the harmonization of current body of legislation with the approved social norms rather than blind enforcement of laws which are often copied from largely different environments.

Annexes

List of Participants in the Development Debates on “PARTICIPATORY AND EFFECTIVE MONITORING OF PRSP IMPLEMENTATION”

1. Tinatin Danelia – ABED
2. Devi khechinashvili – PSI (Member of PRSP editorial board)
3. Nino Lezava – PSI
4. Nato Alkhasishvili – UNDP
5. Inga Paichadse – WB
6. Gia Areshidze – ABED
7. Charita Djashi – Gender Development Assosiation (Member of Editorial Board)
8. Nino Gudzaraidse – CEE Bankwatch Network
9. Gia Jandieri – OSGF
10. Merab Svani – Civil Society Development Institute
11. Zviad Bokuchava – Movement “Future with Dignity”
12. Lancelott Fletcher – AmCham
13. Nick Loladse – Anchor Consulting
14. Nana Adeishvili – CERMA
15. Nino Sul Khanishvili – ACTA Consultants LTD
16. George Kukulava – GYLA
17. Marika Darchia – Institute of Public Relations
18. David Gzirishvili – National expert on Public Participation (Member of editorial Board)
19. George Tarkhan-Mouravi – Institute for Policy Studies (Member of PRSP editorial board)
20. Giorgi Dzamukashvili – Genius Loci
21. Tamaz Asatiani - Foundation CASE Transcaucasus
22. George Chkheidze – Gori Businessmen Association

List of Participants in the Development Debates on “Business Environment”

1. Nino Sulkhaniashvili – ACTA Consultants LTD
2. Tinatin Danelia – ABED
3. Devi Khechinashvili – PSI (Member of Editorial Board)
4. George Loladse – GSE (Member of Editorial Board)
5. Sergo Vashakmadse – WB
6. Mariam Khutsishvili – Georgian Real Estate Association
7. Tata Kandelaki – WB
8. Nick Loladse – Anchor Consulting
9. Gia Jandieri – OSGF
10. Temur Tsagareishvili – Association of Independent Tv&Radio Companies
11. Lancelott Fletcher – AmCham
12. Archil Melikadse – CERMA
13. Nana Adeishvili – CERMA
14. David Tarkhan-Mouravi – State Department of Informatics
15. Nino Lezava – PSI
16. Zurab Gvasalia – Association of Banks of Georgia
17. Gia Areshidze – ABED
18. Nato Alkhasishvili – UNDP
19. Charita Djashi – Gender Development Association (Member of Editorial Board)
20. George Chkheidze – Gori Businessmen Association
21. Zurab Shengelia – Association of Freight Forwarders
22. Nino Gudzaraidse – CEE Bankwatch Network
23. George Gotsadze – CURATIO International Foundation
24. Merab Svani – Civil Society Development Institute
25. Zviad Bokuchava – Movement “Future with Dignity”