LEGISLATIVE AMENDMENTS RELATED TO OFFSHORE COMPANIES AND THEIR POLITICAL IMPLICATIONS

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I.Tax Incentives for Offshore Countries

Corporate Income Tax in Georgia and the so-called "Estonian Model"

Before January 1, 2017, Georgia operated under a standard corporate income tax model, whereby Georgian companies paid income tax on their net profit. Specifically, according to the tax code in effect before 2017, the corporate income tax was levied on "the difference between the taxpayer's total income and the amounts deductible under the code."[1]

Starting from January 1, 2017, the law changed, and a new corporate income tax system, the so-called "Estonian Model," was introduced. The core idea of this model is to defer corporate income tax until the company distributes the net profit to an individual founder or a non-resident entity.[2] With the help of the "Estonian Model" of corporate income tax, a Georgian company can avoid paying corporate income tax if it reinvests the profit it receives back into the business. Therefore, if the company does not distribute the net profit as dividends to the shareholder, it will not pay corporate income tax. However, when the company decides to distribute the accumulated profit, it will have to pay tax at the same rate as under the standard model (15%).

The "Estonian Model" of corporate income tax does not apply to all taxpayers, and in this regard, the tax code establishes several exceptions. Notably, financial institutions (banks, credit unions, microfinance organizations, and loan-issuing entities) and non-resident companies remain under the standard model of corporate income tax. Specifically, financial institutions and non-resident enterprises typically pay corporate income tax on their net profit, which is the difference between the total income received and the amounts deductible in relation to earning that income.

Additionally, the income received by non-resident enterprises may be taxed either under the general rules (for example, income from the supply of goods) or under special rules (for example, dividends, accrued interest, or royalties for the use of intellectual property).

In the case of active income, such as income from the supply of goods, foreign enterprises use the standard model. Specifically, in the case of the sale of property located in Georgia, the object of corporate income tax for the foreign enterprise is the difference between the total income and the amounts deductible as established by the tax code.

[1] Article 97.1 of the Tax Code in effect before 2017.

[2] Article 97.1 of the Tax Code in effect since 2017.

Low-Tax Jurisdictions, or So-Called "Offshore" Countries

Georgian legislation does not use the term "offshore." Instead, what is commonly referred to as "offshore" is designated in the Georgian Tax Code as a "low-tax jurisdiction." The Tax Code outlines the criteria that a state must meet to be classified as a low-tax jurisdiction under Georgian law. Specifically, a country is considered a low-tax jurisdiction if:

- There is no corporate income tax imposed on the profit received by a legal entity;
- A legal entity is exempt from corporate income tax;
- The corporate income tax rate does not exceed one-third (i.e., 5%) of the corporate income tax rate in Georgia.[3]

The list of low-tax jurisdictions, considering the aforementioned criteria, is determined by the Government of Georgia[4] through Resolution No. 615 of December 29, 2016.[5] This list includes territories such as the Virgin Islands, the Cayman Islands, Andorra, Uruguay, Kuwait, Belize, Chile, and others (a total of 64 countries/territories).

In this regard, it is noteworthy that the income received from Georgia by enterprises from low-tax jurisdictions is taxed similarly to the income received by residents of other countries, with minor differences. Specifically, for passive income, interest and royalties paid to a low-tax jurisdiction are taxed at a rate of 15%, instead of the standard 5%. However, dividends in this case are still taxed at 5%. As for income received from the sale of assets, there is no difference in taxation. Specifically, if a resident enterprise of a low-tax jurisdiction purchases shares/stocks of a Georgian company and later sells those shares/stocks at a higher price, its net profit will be the difference between the sale price and the purchase price, and 15% of this profit will be paid to the state budget of Georgia.

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[3] Article 98^2.5 of the Tax Code.

[4] Article 98^2.10 of the Tax Code.

[5] https://www.matsne.gov.ge/ka/document/view/3523434?publication=0#DOCUMENT:1

Legislative Changes in the Tax Code Regarding "Offshore" Companies

Members of the Georgian Parliament, Paata Kvizhinadze, Anton Obolashvili, Irakli Kirtzkhalia, Bezhan Tsakadze, Zaal Mikeladze, Irakli Zarkua, and Gogi Meshveliani, presented a bill concerning "offshore" companies to the Georgian Parliament on April 10, 2024. Furthermore, the Parliament reviewed the bill concerning "offshore" companies under an expedited procedure and passed it on its third reading on the ninth day after its registration, April 19.

On May 2, 2024, the President of Georgia returned the bill to the Parliament with motivated remarks, suggesting the removal of tax benefits from the bill related to companies registered in offshore jurisdictions.[6] The Finance and Budget Committee of the Georgian Parliament (the lead committee) issued a conclusion on May 21, 2024, not supporting the President's motivated remarks.[7] Subsequently, on May 29, 2024, the Parliament overrode the President's veto in a plenary session and supported the original version of the bill.[8]

According to the legislative amendment, Article 309 (Transitional Provisions) of the Georgian Tax Code is supplemented with Paragraph 146, with the following wording:

"Where the ownership rights to all assets (including shares) of a foreign enterprise registered in a low-tax jurisdiction are transferred to a Georgian enterprise by January 1, 2028:

a) The income/benefit received from this transaction by the foreign enterprise and its partner individual, considered as income from a Georgian source for the purposes of this Code, is exempt from profit/income tax;

b) The import of the asset/goods into Georgia is exempt from import duties. The rules and conditions for applying this subparagraph 2 shall be determined by the Minister of Finance of Georgia;

c) The Georgian enterprise is exempt from property tax on the asset received within the framework of this transaction until January 1, 2030.

Note:

1. This part applies if:
a) 100 percent of the shares of the foreign enterprise registered in the low-tax jurisdiction and the Georgian enterprise are owned by the same individual (group of individuals);
b) The transfer involves an asset that was owned by the foreign enterprise registered in the low-tax jurisdiction as of the effective date of this part.

2. In cases covered by this part, the value of the asset for the receiving party is the same as its value for the supplying party at the time of transfer."

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[6] https://parliament.ge/legislation/28600
[7] https://info.parliament.ge/file/1/BillReviewContent/362587
[8] https://shorturl.at/JnWQO

Results of the New Law

Explanatory note of the law

The explanatory note accompanying the bill on amendments to the Tax Code concerning "offshore" companies states that investments in Georgia are often made by foreign enterprises registered in low-tax jurisdictions (offshore), which operate in Georgia through their subsidiary companies. This involves risks of tax evasion and hinders efficient tax administration. Given this, it is important to facilitate the process of transferring assets from companies registered in low-tax jurisdictions to Georgia to prevent tax evasion, ensure business transparency, and simplify tax administration.

The explanatory note also mentions that the process of transferring all assets to Georgia by an "offshore company" may be hindered by the tax obligations that arise during the transfer of these assets. The aim of the legislative change is to encourage the process of transferring assets from a foreign enterprise registered in a low-tax jurisdiction to Georgia by establishing temporary tax benefits for these operations.

Accordingly, the authors of the law state that the main objective of the law is to facilitate the transfer of ownership rights of assets from offshore companies to Georgian companies by establishing tax benefits. To share this logic, we need to determine at least two things:

- Transferring assets from offshore companies to Georgian companies is currently not possible without taxation;
- With the help of the new amendments to the Tax Code, it will become possible to transfer assets without taxation.

We previously noted that in the case of an offshore company selling an asset located in Georgia, the object of corporate income tax is the difference between the selling price of the property and its purchase price (capital gain). According to the legislative amendment, if the ownership rights to all assets (including shares) of a foreign enterprise registered in a low-tax jurisdiction are transferred to a Georgian enterprise by January 1, 2028, the income/profit received by the foreign enterprise from this transaction is exempt from profit/income tax. In other words, within the framework of the new law, if the criteria specified by the law are met, the offshore company will no longer have to pay profit tax on the aforementioned capital gain to the state budget of Georgia.

However, it is noteworthy that even without this legislative amendment, an offshore company can transfer its assets to a Georgian company without taxation, for example, by transferring assets free of charge, contributing these assets to the capital of a Georgian company, or liquidating the offshore company and transferring the assets it owns to the individual founder.

Accordingly, the only novelty of the law is the exemption of an offshore company from corporate income tax in the case of asset transfer through a sale.

Additionally, it should be noted that the legislative amendment does not create any real motivation or incentive for transferring assets from an offshore company to Georgia. Specifically, the benefit is provided only for the operation of transferring the assets. After the assets are transferred, the tax regime remains essentially the same.

In summary, the law does not effectively achieve the goal outlined in the explanatory note. Firstly, it is already possible to transfer assets from offshore jurisdictions to Georgia without taxation even without this amendment. Secondly, the amendment fails to create a genuine incentive for transferring assets to Georgia, as the tax regime remains unchanged and only the transfer operation itself is exempt from tax.

The real outcome of the law - tax-free profit extraction from Georgia

According to the legislative amendment, the tax benefit applies to the transfer of assets by an offshore company to a Georgian company, where the income from the sale of these assets is considered income from a Georgian source for the purposes of the Tax Code.

Income from a Georgian source is defined by Article 104 of the Georgian Tax Code. According to this article, income from a Georgian source includes income from the sale of goods if the supply of goods (transfer of ownership) occurs within the territory of Georgia. Income from a Georgian source also includes income from the sale of shares/stocks of a resident company.

Accordingly, the tax benefit regarding corporate income tax does not apply to the supply of assets located abroad or shares of a foreign company. An offshore company will benefit from these tax exemptions if the asset it transfers to a Georgian company is located in Georgia—such as real or movable property in Georgia or shares of a Georgian resident company. **Therefore, the tax benefit regarding corporate income tax applies not to the transfer of assets from abroad to Georgia, but to the change of direct ownership of assets already in Georgia, provided that the beneficial owner of the assets remains the same individual or group of individuals.**

It is important to note that when a Georgian company purchases an asset from an offshore company, the Georgian company pays the corresponding purchase price to the offshore company. Due to the amendments to the Tax Code, this payment will be transferred from Georgia to the offshore company without incurring any taxes.

In this way, the legislative amendment enables the accumulated profits of a Georgian enterprise, which would have been taxed if distributed to the shareholder, to be transferred out of Georgia tax-free as a purchase price. Specifically, a Georgian enterprise that accumulates profits can, instead of distributing these profits as dividends, purchase property located in Georgia from its own offshore shareholder. Through this mechanism, the accumulated profit of the Georgian company is transferred to the offshore company as a purchase price, which, under the legislative amendment, is exempt from profit tax.

Consequently, the indirect result of the legislative amendment is that profits extracted from businesses in Georgia, which were previously taxed at 19.25%,[9] can now be transferred without any tax liability. This process merely requires a restructuring of the business without changing the ultimate beneficial owner, allowing the accumulated profit to be transferred as a purchase price rather than as a dividend.

[9] The combined net effect of the 15% Corporate Income Tax and the 5% Dividend Tax rates.

Impact of the law on future property

According to the law, the tax benefit applies only if the transfer involves assets that are owned by the foreign enterprise registered in a low-tax jurisdiction as of the effective date of this law. In this way, the legislator seemingly makes the benefit a one-time event and does not extend it to future assets.

However, the law stipulates that to take advantage of the benefit, the offshore company must dispose of the assets (including shares/stocks, i.e., subsidiary companies) it owns at the time the law comes into effect. The legislative amendment does not restrict the subsidiary company itself from acquiring new assets.

Therefore, if an offshore company established a subsidiary in Georgia before the law came into effect, the benefit will apply to the sale of shares in this subsidiary until 2028. As a result, from the effective date of the law until January 1, 2028 (the period during which the benefit is in effect), the subsidiary of the offshore company can conduct business in Georgia, accumulate profits, and later, through the scheme described above (selling shares in the subsidiary), transfer these profits out of Georgia tax-free.

Exemption from import duties

According to the legislative amendment, the importation of assets/goods into Georgia by an offshore company for a Georgian company is exempt from import duties. Import duties include the three taxes that may be imposed on the importer: import tax, excise tax, and value-added tax (VAT).

Import tax and excise tax apply only to specific goods, the exhaustive list of which is provided in the Georgian Tax Code (Articles 188, 188[1], and 197). On the other hand, VAT is levied on the import of any goods, unless otherwise specified by law.

It is noteworthy that the current Tax Code, since its effective date (January 1, 2011), has provided for the exemption of the import of securities and civil aircraft from VAT.[10] As a result of amendments made on May 29, 2012, the import of yachts is also exempt from VAT.[11] Additionally, civil aircraft, yachts, and securities are not subject to import tax or excise tax either.

Furthermore, according to Articles 188 and 188[1] of the Tax Code, excise tax primarily applies to alcoholic beverages, tobacco products, petroleum products, and the import of automobiles/motorcycles. The excise rate for automobiles is calculated based on engine capacity rather than its value.[12] Light vehicles, in turn, are not subject to VAT. Consequently, the import of high-value automobiles does not have a significant financial impact under Georgian tax legislation.

Since the amendments to the Tax Code have no effect on the import of airplanes, yachts, cars, and securities, and since the import of real estate is impossible, it is likely that the specific purpose of this exemption is to relieve the import duties **on high-value movable property that would otherwise be taxed under the existing Code**. Such movable property includes, for instance:

[10] Article 173.n and 173.s of the Tax Code.

[11] https://www.matsne.gov.ge/ka/document/view/1661811?publication=0

[12] Article 188.1, graph 4 (of the given table) of the Tax Code.

- Precious metals (gold, silver, platinum) and precious stones (diamonds, pearls, others), whose import is taxed at an 18% VAT rate. Additionally, jewelry made from precious metals is subject to an import tax of 12%.[13]
- Works of art, collectibles, and antiques, whose import is taxed at an 18% VAT rate.

These are types of goods that are likely to be found in offshore countries, whose transportation and storage are relatively inexpensive due to their size, have the greatest tax effect due to their value, and most importantly, are assets that do not participate in the country's economy.

Property tax exemption

According to the legislative amendment, a Georgian company is exempt from property tax on assets received from an offshore company, until January 1, 2030.

Generally, Georgian companies are subject to property tax on their fixed assets (tangible assets used for the production of goods, supply of goods/services, leasing, or administrative purposes) and investment property (land or buildings held for rental income or capital appreciation, or both).

In other words, Georgian companies pay property tax on tangible assets located in Georgia that they use in their business activities, as well as on land they own. Intangible assets (securities, company shares/stocks, intellectual property, etc.) are not subject to property tax.

Therefore, to benefit from this exemption, the offshore company must own tangible property, and this property must be transferred to the Georgian enterprise. The legislative amendment does not impact the transfer of intangible property.

For example, if an offshore company owns shares in a Georgian company and sells those shares to another Georgian enterprise, the property tax exemption would be irrelevant since company shares are not subject to property tax anyway. However, if the offshore company owns real estate in Georgia, and this real estate is transferred to a Georgian enterprise, then the Georgian enterprise would be exempt from paying property tax on that property.

As a result, an individual who owns assets in Georgia through an offshore company can transfer these assets to their subsidiary Georgian enterprise without changing the ultimate business owner. Consequently, for the next six years, the property tax will not be payable on those assets that are already being used in Georgia

Increased risks in money laundering

According to Article 194, Part 1 of the Georgian Criminal Code, money laundering is the legalization of illegal income, meaning giving a legal appearance to illegally or unjustifiably acquired property.

[13] Article 197.1, Point 158 (of the given table) of the Tax Code.

Money laundering involves associated costs—legal income, or money obtained through legitimate means, is subject to taxation. Therefore, there is always an incentive to launder money in countries where the tax burden is low, or where profits are fully exempt from corporate income tax.

As discussed above, the legislative amendment allows a Georgian enterprise to earn profit and subsequently transfer this profit to an offshore country without taxation.

Therefore, although the legislative amendment does not create a new scheme for money laundering, it does allow money to be laundered in Georgia without paying taxes into the state budget. This potential ease of laundering money could create additional motivation for criminal groups to choose Georgia for money laundering instead of other jurisdictions.

Tax benefit or legalized tax evasion scheme?

Article 73.9.b of the Tax Code establishes the so-called principle of substance over form, which allows the Revenue Service to disregard the formal aspect of a transaction if it does not correspond to its actual substance. This means that a business operation can be taxed based on its real economic substance rather than its formal designation.

To enforce this article, the Revenue Service issued Methodological Guidelines on the Requalification of Economic Operations through Order No. 20231 on July 28, 2022. [14]

These guidelines, among other things, provide examples illustrating what the Revenue Service may consider as suspicious transactions and what may be deemed not genuine economic operations or business transactions but rather schemes for tax evasion.

It is notable that the first example provided in the methodological guidelines almost identically mirrors the scheme proposed by the legislative amendment. Specifically, according to the example in the guidelines, a group of individuals owns shares in two companies - LLC "A" and LLC "B." A sale agreement is then made with the subsidiary company LLC "A," whereby it purchases 100% of the shares in LLC "B" from its shareholders for 300,000 GEL. Similarly to the scheme proposed by the legislative amendment, in this example, the ultimate owners of the sold company remain the same individuals, and only the ownership structure changes, resulting in the shareholders receiving 300,000 GEL as the sale price.

In the assessment of this example, the Revenue Service states: "Generally, a property sale agreement, as a legal instrument, is used to formalize economic operations where the ownership of the property changes hands. Under these conditions, since the selling individuals still indirectly own 100% of the shares in LLC 'B', meaning there is no actual change in the ownership of the property (shares), this operation should be considered a suspicious economic operation for tax purposes. The real purpose (substance) of this economic operation may be the tax-free distribution of dividends to individuals."

[14] https://infohub.rs.ge/ka/workspace/document/45b90f02-cd41-4ae0-9002-13b9d44a3a25?openFromSearch=true

The scheme outlined by the legislative amendment involves the same mechanism as the illustrative example in the guidelines. Specifically, a property sale agreement is executed, resulting in the indirect owner of the sold property remaining the same individual, meaning there is no actual change in ownership. Consequently, this operation allows for the tax-free distribution of dividends to the ultimate beneficial owner of the company. Therefore, the structure proposed by the Georgian Parliament had already been evaluated by the Revenue Service in 2022 as a tax avoidance scheme.

However, the legislative amendment now legalizes this scheme, as it directly requires that the real owner of the asset does not change as a result of the sale and that the transfer of funds remains untaxed. Specifically, according to the legislative amendment, the tax benefit applies only if the same individual (or group of individuals) owns 100% of the shares in both the foreign enterprise registered in a low-tax jurisdiction and the Georgian enterprise.

Instructions for Utilizing Benefits Approved by the Minister of Finance

On October 2, 2024, the Legislative Herald of Georgia published Order No. 329 issued by the Minister of Finance of Georgia on October 1, 2024, regarding the amendment of Order No. 996 of the Minister of Finance of Georgia dated December 31, 2010, “On Administration of Taxes.” As a result of this amendment, Article 111[15], titled "The Procedure and Conditions for Exemption from Taxes/Duties as Provided by Article 309, Part 146 of the Tax Code of Georgia," was added to the “On Administration of Taxes” order. Through this new article, the Minister of Finance establishes the procedures and conditions that offshore companies must follow to benefit from the prescribed incentives.

A significant update in the procedures and conditions established by the Minister of Finance is the requirement for an importer to submit an application, along with the necessary documents, to the tax authority in advance to obtain an exemption from import duties. The Revenue Service will review the application within 10 business days, and if it meets legal requirements, a decision will be made to exempt the imported goods from duties.

Another notable change in the Minister of Finance’s order is the addition of a specific requirement for utilizing the benefit. The order stipulates that, to benefit from the exemption provided by law, the transfer of assets must occur **free of charge**. This requirement substantially limits the use of tax schemes aimed at taking profit out of Georgia without taxation. In this respect, the amendment in the Minister of Finance's order may initially be viewed positively as a mechanism to tackle tax avoidance schemes. However, there are several issues associated with introducing this significant criterion in the order at this time and in this manner;

Conflict Between Law and Ministerial Order

When determining the exemption from taxes for the transfer of assets by a resident company of an offshore country to a Georgian company, the law does not set any restrictions on the form of delivery. On one hand, Article 309, Part 146 of the Tax Code states that a transfer of ownership of assets from a foreign enterprise to a Georgian enterprise is exempt from taxes, without specifying that this transfer must be free of charge. On the other hand, the note in the same provision outlines the criteria for using this exemption, but none of these criteria require the goods to be delivered free of charge.

Additionally, Article 309, Part 146, Subsection (b) — which grants a benefit related to **import duties** — explicitly states that the “Minister of Finance of Georgia shall determine the procedure and conditions for the application of this subsection.” Consequently, the law has granted the Minister of Finance direct authority to establish the necessary procedures and conditions for exemption from import duties. However, in other cases — including exemption from profit tax — the law has not granted such authority to the Minister of Finance.

It should also be noted that Article 127 of the Tax Code regulates the principles for determining the price of international transactions between related parties. According to this article, if a Georgian

enterprise transacts with a related foreign enterprise, both parties must determine their profits in line with arm's length price. In other words, the Tax Code requires that transactions between such parties be conducted at market prices. Therefore, the Minister of Finance's requirement for goods to be provided free of charge contradicts the law's requirement for transactions to be conducted at market prices.

Accordingly, the Minister of Finance established rules and conditions for benefiting from profit tax exemptions without legal authority to do so. Furthermore, the Minister has effectively restricted the scope of the legally defined exemption by imposing a requirement — that goods be provided free of charge — which directly contradicts the law's requirements.

As a result, there is a possibility that a resident from a country with favorable tax treatment could provide all of its assets to a Georgian enterprise for a fee and still benefit from the tax exemption under **the law**. Specifically, according to Article 7, Section 7 of the "Law on Normative Acts of Georgia", legislative acts of Georgia hold higher legal power over subordinate normative acts. Therefore, if a subordinate normative act (in this case, the Minister's order) contradicts the law, the law shall prevail and be applied. Consequently, the law — rather than the Minister's order — does not require a transaction to be free of charge as a prerequisite for obtaining a tax exemption.

Effective Dates of the Law and Ministerial Order

Furthermore, there was a four-month gap between the enactment of the exemption provided by law (following the amendment to the Tax Code) and the introduction of the new rule by the Minister's order. Specifically, the amendment to the Tax Code (the exemption) was published in the Legislative Herald of Georgia on June 4, 2024, and took effect immediately upon publication, i.e., on June 4. The Minister of Finance's order, which established the requirement for goods to be provided free of charge, was published in the Legislative Herald on October 2, 2024, and took effect immediately upon publication, i.e., on October 2.

As a result, from June 4, 2024, to October 2, 2024, only the exemption provided by law was in effect, and no obligation for free delivery of goods was established. Consequently, the additional requirements set by the Minister of Finance's order cannot apply to transactions conducted during this four-month period. According to Article 2, Section 2 of the Tax Code of Georgia, the tax legislation of Georgia in effect on the date of the tax obligation's occurrence shall apply to tax assessment. Therefore, if a transaction was conducted during this four-month period, the legislative basis for taxation of that transaction cannot be the rule established by the Minister of Finance at a later date.

Consistency of the Legislative Amendment with OECD Policy

Before the advancement of globalization and the development of international trade and communication systems, a country's tax policy primarily depended on domestic events and had a significant impact mainly on that country itself. However, under globalization, where active trade relations exist between all countries in the world, and multinational companies conduct business in several countries, the effects of each country's tax system extend far beyond its borders and influence the economic and financial situation in other countries.

Multinational companies are inclined towards tax optimization and seek to set up their business or its administrative center in countries with significantly lower tax burdens. In response to this and to attract multinational companies to their countries, some countries have introduced special tax incentive regimes. Such regimes can negatively impact other countries' economies and create unfair competition between nations.

A tax incentive regime may be generally applicable to everyone, established for specific business activities, or introduced for certain individuals, among other variations. Each of these instances represents potentially harmful tax practices that could damage other countries' economies.

Regarding the significance of this harmful tax practice and the need for further research, in 1998, the Organization for Economic Co-operation and Development (hereinafter "OECD") published a document entitled "Harmful Tax Competition, An Emerging Global Issue."[15] In this document, OECD reviews the importance of harmful tax practices and their effects on the global economy, lists various factors qualifying as tax havens and harmful tax practices, and finally provides recommendations for countries on mechanisms to combat harmful tax practices.

In 2013, at the request of the G20, the OECD initiated the Base Erosion and Profit Shifting (BEPS) project, which includes 15 actions. The main goal of the BEPS project is to develop effective domestic and international instruments to prevent aggressive and harmful tax practices.

The OECD also emphasizes the issue of harmful tax practices within the BEPS Project,[16] under which it has introduced Action 5 to combat harmful tax practices. The goal of Action 5 is to eliminate harmful tax practices by reviewing preferential regimes and mandating the exchange of information related to harmful tax practices. In relation to Action 5, the OECD has also created a separate document titled "Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report."[17]

To implement the BEPS project, the Inclusive Framework on BEPS was established in February 2016 by OECD member states and G20 countries. Membership in the Inclusive Framework requires the implementation of the measures outlined in the BEPS project, specifically the obligation to implement

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[15] https://www.oecd-ilibrary.org/taxation/harmful-tax-competition_9789264162945-en

[16] Addressing Base Erosion and Profit Shifting, OECD, 2013 - https://www.oecd.org/tax/beps/addressing-base-erosion-and-profit-shifting-9789264192744-en.htm

[17] https://www.oecd.org/tax/countering-harmful-tax-practices-more-effectively-taking-into-account-transparency-and-substance-action-5-2015-final-report-9789264241190-en.htm

the four minimum standards. Among these minimum standards is the requirement to meet the demands of Action 5.

On June 14, 2016, Georgia joined the Inclusive Framework on BEPS as an associate member. As an associate member of the Inclusive Framework on BEPS, Georgia committed to implementing the four minimum standards outlined in the BEPS project, including the obligation to implement Action 5.

The process of implementing the minimum standard developed under Action 5 is coordinated by the Forum on Harmful Tax Practices (FHTP), which aims to ensure the assessment and monitoring of the standards developed under Action 5.

As part of the monitoring process to determine whether a particular preferential tax practice constitutes a harmful practice that negatively impacts other countries' economies, the FHTP relies on the following two documents published by the OECD:

- Harmful Tax Competition, An Emerging Global Issue, 1998.
- Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report, 2015.

As mentioned above, the main criteria for qualifying harmful tax practices are provided in the first document, adopted in 1998. The 2015 document developed within the framework of the BEPS project mainly relies on the 1998 document but includes some minor additions.

These documents identify two types of harmful tax regimes. The first category includes so-called tax havens, while the second category includes countries that are not tax havens but have special tax regimes or tax incentives that harm the economies of other countries.

Tax havens

To identify a tax haven, the OECD uses four criteria:

1. **Zero Taxes**: In countries that are considered tax havens, income taxes are either zero or so minimal that they have no substantial economic effect on businesses.
2. **Secrecy**: Tax havens are characterized by legislation that allows companies to keep significant information about their operations confidential. This secrecy facilitates not only tax evasion but also money laundering.
3. **Lack of Transparency:** Beyond the concealment of information by companies, tax havens are also marked by the state's own lack of transparency. These countries typically do not share information about the companies registered within their jurisdiction and their incomes with other countries, hindering other states' ability to collect necessary tax data.
4. **Insignificant Business Activity:** If tax legislation requires substantial business operations in the country to benefit from tax incentives, businesses would need to relocate their activities along with their tax base to that country. Tax havens do not impose such requirements, allowing the transfer of tax bases through the establishment of conduit companies, which do not conduct significant operations in the country and are limited to managing funds to reduce taxes.

Harmful tax practices

As mentioned earlier, besides tax havens, there are countries that do not qualify as such but create harmful preferential tax practices due to their tax systems and policies. Many countries strive to become more attractive for companies, offering a cheaper place to store assets and conduct financial operations.

Several key factors are identified to determine a harmful tax regime, which largely resemble the criteria used to identify tax havens:

1. **No or Nominal Taxes**: The presence of low or zero taxes is a crucial element of a preferential tax regime and is interpreted similarly to the criteria for tax havens.
2. **Ring-fencing**: This involves the separation of a special tax incentive regime from the rest of the country's economy. To prevent the special tax regime from negatively affecting the economy, the country may (a) restrict its resident individuals and entities from using this regime or (b) limit the free integration of entities benefiting from this regime into the rest of the economy. For example, in Georgia, a person registered in a Free Industrial Zone[18] is prohibited from receiving services from other Georgian companies that are not registered in the industrial zone.
3. **Lack of Transparency:** Countries with harmful tax regimes may hide information about the special regime. Additionally, the harmful nature of a tax incentive may not be explicitly highlighted in legislative regulations, but in practice, the tax authority may provide opportunities to taxpayers that can be considered harmful practices. Therefore, the requirement for transparency also encompasses the transparency of tax practices and administration.
4. **Lack of Information Exchange**: A country with a harmful tax regime may not exchange tax-related information about specific companies with other countries, even though it might have such obligations under international agreements.
5. **Insignificant Business Activity**: The tax incentive applies to companies that do not conduct substantial business activities in the country providing the incentive.

To determine harmful tax practices, other relevant risk factors may also be used, indicating that the tax regime could be detrimental to other countries.

In the presence of such risk factors, the FHTP conducts further investigations to assess whether the special tax regime has a real harmful impact on the economies of other states and whether it hinders fair competition between countries.

Analysis of the impact of the legilative amendment

The analysis provided in the first part of this document makes it clear that the tax benefit under the legislative amendment is intended for a specific operation and is limited to a specific time frame. Within the scope of this tax benefit, it is primarily Georgia that loses tax revenues, and there is no

[18] Special tax regime.

indication that the benefit could have a harmful impact on the economies of other, non-offshore countries.

The tax benefit provided by the legislative amendment could only affect the economies of other countries if, for example, an offshore company owns machinery (or other assets) that it uses to conduct business activities in another country and relocates these assets to Georgia due to the property tax exemption. In this case, the country where the machinery was previously based would lose the economic benefits generated by this business (such as taxes or jobs).

It is important to note that such an impact is not considered a harmful effect on the economies of other countries, but rather represents fair competition between states. One of the criteria for identifying harmful tax practices is a tax benefit that applies to a company without substantial business activity in Georgia. Under the conditions of the specified model, to be exempt from property tax, the taxpayer must bring the asset to Georgia.

Furthermore, it should be noted that the BEPS project addresses income-related taxes (income tax, corporate tax), and consequently, the FHTP examines harmful tax practices in relation to these taxes and not property taxes.

Therefore, the tax benefit provided by the legislative amendment will have a harmful impact only on the Georgian economy in terms of corporate income tax, while the benefits related to property and import taxes do not fall within the OECD's oversight scope.

Regarding transparency and information exchange requirements, the OECD's annual reports on Georgia do not indicate any deficiencies or issue additional recommendations, suggesting that the organization does not consider Georgia a risk factor in this area.[19]

Consequently, at this stage, it does not appear that the introduced tax benefit conflicts with OECD policy. However, it will be important for the FHTP to conduct further examinations, which will more thoroughly investigate the practical implementation of the benefit.

[19] Please see the OECD reports for the years 2020, 2021, and 2022:
2020 - https://www.oecd.org/tax/beps/harmful-tax-practices-2020-peer-review-reports-on-the-exchange-of-information-on-tax-rulings-f376127b-en.htm
2021 - https://www.oecd.org/tax/beps/harmful-tax-practices-2021-peer-review-reports-on-the-exchange-of-information-on-tax-rulings-4034ce42-en.htm
2022 - https://www.oecd.org/tax/beps/harmful-tax-practices-2022-peer-review-reports-on-the-exchange-of-information-on-tax-rulings-22bbeacc-en.htm

Summary

This part provides a brief overview of the tax incentive introduced by the Parliament of Georgia on June 4, 2024, regarding companies registered in offshore jurisdictions.

According to the introduced tax benefit, if a company registered in an offshore country and a company registered in Georgia have the same shareholder(s), the following transactions are exempt from tax:

- **Corporate Income/Income Tax Exemption**: Income/profit generated by an offshore company from supplying all assets to a Georgian company, considered to be Georgian source, is exempt from corporate income/income tax if the supply is made by January 1, 2028.
- **Import Duty Exemption**: Importation of assets into Georgia under this transaction is exempt from import duty.
- **Property Tax Exemption**: Property received by a Georgian company under this transaction is exempt from property tax until January 1, 2030.

According to the explanatory note of the law, the objective of this law is to encourage companies registered in offshore jurisdictions to transfer assets to Georgia tax-free. However, this argument does not reflect the current reality, as companies registered in offshore jurisdictions could have transferred ownership of assets tax-free even without the presented tax incentive. Therefore, the real objective of the introduced incentive could not be as stated by the authors of the law in the explanatory note.

Real Impact of the Introduced Tax Benefit:

- **Corporate Income/Income Tax:** The legislative amendment allows profits accumulated by a Georgian enterprise, which would be taxed if distributed to the shareholder, to be transferred out of Georgia tax-free as a sale price. For example, instead of distributing the accumulated profit as dividends, a Georgian enterprise can purchase property in Georgia from its shareholder. In this way, the accumulated profit is transferred to the offshore country as the sale price, which is not subject to corporate income tax under the legislative amendment. Consequently, the indirect result of the legislative amendment is that profits extracted from businesses in Georgia, which were previously taxed at an effective rate of 19.25%, can now be transferred to offshore without taxation.
- **Import Duty:** Given that the introduced benefit provides an exemption from import duties for imported assets, it is expected that high-value movable assets will be brought into Georgia. Examples of such assets that will be affected by the tax benefit include precious metals (gold, silver, platinum), precious stones (diamond, pearl, etc.), jewelry made from precious metals, works of art, collectibles, and antiques. These items were previously subject to import taxes ranging from 12-18%, which will no longer apply after the benefit is enacted.

- **Property Tax:** Significant benefits can be obtained by individuals who previously owned high-value real estate in Georgia through offshore companies and paid property taxes on these properties annually. Following the introduction of this tax relief, if offshore companies transfer such assets to a company registered in Georgia (with the same beneficial owner), the Georgian company will be exempt from paying property tax on these assets until January 1, 2030. Furthermore, the transfer of these assets to the Georgian company is also exempt from profit/income tax (as previously discussed).

Additionally, the Revenue Service, through Order No. 20231 dated July 28, 2022, has approved methodological guidelines for the reclassification of economic operations. In these guidelines, the Revenue Service has outlined a scheme similar to the proposed tax benefit and has evaluated it as a suspicious operation potentially aimed at tax avoidance.

On October 2, 2024, the Minister of Finance of Georgia amended his own Order №996 of December 31, 2010, by adding Article 111[15]. In this article, the Minister regulated the procedures for applying the tax incentive introduced by the Tax Code. Although the tax incentive in the Tax Code gave the Minister of Finance the authority to regulate **only** procedures related to the importation of goods, the Minister still introduced a new, special rule differing from the law for the application of the incentive. Specifically, according to the Minister's order, the tax incentive applies only if the assets are transferred by the offshore company to the Georgian company free of charge. **As a result, the Minister excluded the implementation of tax schemes that could transfer profits from Georgia to an offshore company.** Despite this, there was a 4-month window between the enactment of the tax incentive in the Tax Code and the amendment to the Minister's order, which allowed transactions to be carried out for a consideration during that period. **Furthermore, such transactions can still be carried out today because the Minister's order is a subordinate regulatory act and does not have higher legal authority than the Tax Code.** When there is a conflict between the provisions of the Tax Code and the Minister's order, the rule established by the Tax Code applies. Therefore, since the Minister's order contradicts the tax incentive provided by the Tax Code (by essentially narrowing the conditions for using the incentive), there still remain risks of tax-free profit transfers from Georgia to offshore countries.

Additionally, since the discussed incentive will have a detrimental impact only on the Georgian economy (and not on the economies of non-offshore countries), it has not yet been established that the introduced tax incentive contradicts OECD policies. However, it will be important to observe the further review by the FHTP, which will examine the practical implementation of the incentive in more detail.

In light of all the above, it is not expected that the tax incentive will have any positive impact on the Georgian economy, and on the contrary, it may prove to be detrimental to the state budget.

II.Who Benefits from the So-Called Offshore Law?

The legislative amendments introduced in the Tax Code offer several benefits to companies registered in offshore zones, including an exemption from profit tax.

Squander Detector pexamined large enterprises registered in Georgia whose shares are owned by foreign enterprises registered in offshore zones.

The research revealed that the legislative amendment, introduced by the ruling party, mainly benefits large offshore companies with substantial retained earnings accumulated in Georgia.

During the study, we examined 20 large Georgian companies whose shares are fully or partially owned by companies registered offshore and which were affected by the tax amendments under review. Under the new legislative changes, these companies had the opportunity to dispose of their accumulated profits from previous years without being taxed (19.25%)[20] and thus legally avoid profit distribution.

Upon reviewing the financial statements of these companies, we found that 10 companies have accumulated up to 500 million GEL in undistributed profits.

Notably, the amendments to the Tax Code provided companies with a four-month window to use this tax avoidance mechanism.

On October 2, 2024, the Minister of Finance published Order No. 329, dated October 1, 2024, regarding amendments to Order No. 996, "On Administration of Taxes," issued on December 31, 2010. In accordance with this order, the Minister of Finance defined the rules and conditions that offshore companies must comply with to benefit from the specified incentives.

The additional requirements for using the benefit set out in the Minister's order have created a conflict between the law and the order. Specifically, the law did not grant the Minister of Finance the authority to establish rules and conditions for the profit tax exemption. The Minister of Finance set parameters for the application of the tax exemption that, in effect, directly contradict the requirements of the law.

Therefore, there remains a possibility for companies registered in offshore zones to use the benefit based on the law. According to the "Law on Normative Acts of Georgia", legislative acts of Georgia hold superior legal authority over subordinate normative acts. Consequently, if a ministerial order (a subordinate normative act) conflicts with the law, the law is applied, and it takes precedence.

[20] The combined net effect of the 15% Corporate Income Tax and the 5% Dividend Tax rates.

The purpose of the legislative amendment, its timing, and the political context raise suspicions that it is tailored to the interests of specific individuals and businesses, with the aim of securing the political loyalty and co-optation of the major business elite.

However, it is difficult to determine at the time of the study whether large companies took advantage of the aforementioned five-month benefit period, as confirming data would only appear in their financial reports, which they will not submit until the following year. Nonetheless, the conflict between the law and the ministerial order does not preclude the possibility for companies to continue benefiting from the exemptions even after the order's publication.

Below is a list of the 10 companies with the largest undistributed profits and offshore companies linked to Bidzina Ivanishvili. However, the number of enterprises that could benefit from the so-called offshore law is much larger, and the associated loss that the budget of Georgia may incur due to these offshore companies is substantial.

1. **Tbilisi Energy**

Tbilisi Energy is engaged in the distribution of natural gas and operates as a monopoly under a license granted by the Georgian National Energy and Water Supply Regulatory Commission.

According to the company's latest financial statement, dated 2023, Tbilisi Energy has accumulated profits of **97,611,000 GEL**. Tbilisi Energy is 100% owned by Voltbay LLC, registered in the Marshall Islands. The ultimate beneficiaries are Khvicha Makatsaria and Nasib Hasanov.

2. **Geosteel LLC**

Established in 2006, Geosteel LLC manufactures construction rebar through hot-rolling and by using structural steel billets.

According to its latest financial statement, dated 2024, Geosteel LLC has accumulated profits of **152,585,000 GEL**. Georgian Steel Group Holdings Limited ("GSGHL"), registered in the Virgin Islands, owns 90% of Geosteel LLC, while JSW Steel B.V. ("JSW BV"), registered in the Netherlands, owns the remaining 10%.

3. **Chiaturmanganum Georgia LLC**

Chiaturmanganum Georgia LLC is engaged in the production and sale of various types of manganese ferroalloys.

As of its latest financial statement, dated 2023, the company has accumulated profits of **57,792,732 GEL**. Greenfield Financial Corp, registered in the Republic of Seychelles, owns 100% of Chiaturmanganum Georgia LLC, with Shmagi Kemertelidze listed as the ultimate owner.

4. **Alma LLC**

Alma LLC operates in the outdoor advertising market. It holds exclusive rights to place advertisements on infrastructure owned by the Tbilisi Transport Company, as well as on movable and immovable property. Additionally, Alma LLC has exclusive rights to place internal advertising in Tbilisi and Batumi international airports.

According to the latest financial statement dated 2023, Alma LLC has accumulated profits of **109,264,635 GEL**. The company is owned by Meridian Malta LLC, registered in Malta, with Soso (Samson) Phkhakadze and Levan Phkhakadze as the ultimate controlling individuals.

5. **Mars LLC**

Mars LLC offers clients online sports betting, online casinos, online peer-to-peer, and other online games through the website www.crystalbet.com. The company also operates a land-based casino, betting facilities, and 21 cash registers.

According to the 2023 financial statement, Mars LLC has accumulated profits of **29,124,000 GEL**. Entain Georgia LLC, registered in Georgia, owns 100% of the company, which is, in turn, 100% owned by bwin Holdings (Malta) Limited, registered in Malta.

6. **Clean House LLC**

Clean House LLC is a retail network that provides consumers with hygiene products, household chemicals, cosmetics, perfumes, and sanitary-hygienic supplies.

According to the 2023 financial statement, Clean House LLC has accumulated profits of **29,731,000 GEL**. GRG Trading Ltd, registered in the Virgin Islands, owns 96% of the company, with Archil Macharashvili as its representative, and Tamar Gvinashvili owns the remaining 4%.

7. **Georgian Petroleum LLC**

Georgian Petroleum LLC supplies aviation fuel at airports and operates at Tbilisi, Kutaisi, and Batumi International Airports.

According to the latest financial statement, the company has accumulated profits of **8,435,000 GEL**. Georgian Petroleum LLC is owned by three offshore companies: Akert Group S.A., registered in the Seychelles, owns 50%, Gateline Projects Limited, registered in the Virgin Islands, owns 25%, and Greenfield Georgia LLC, registered in Georgia, owns the remaining 25%, with its ultimate owner being Greenfield Holdings, registered in the Virgin Islands.

8. **GTG LLC**

GTG LLC's primary business is the sale of alcoholic beverages.

According to the latest financial statement, GTG LLC has accumulated profits of **6,122,400 GEL**. Vioneo Holdings Limited, registered in Cyprus, owns 85% of the company, with Tsiala Darchiashvili owning 10% and Maia Bitskinashvili owning 5%.

9. Service Net Group LLC

The primary activity of Service Net Group LLC involves the construction of various types of linear buildings, including aerial and underground infrastructure and internal network development.

Notably, according to the 2023 financial statement, 99% of the company's revenue came from a single client, and it has accumulated profits of **5,745,666 GEL**. The company is 100% owned by Jupiter Finance (Malta) Limited, registered in Malta.

10. Batumi International Container Terminal LLC

Batumi International Container Terminal LLC owns a container terminal and ferry bridge in Batumi, Georgia. According to the latest financial statement, the company has accumulated profits of **3,220,973 GEL**. The company is 100% owned by ICTSI Georgia Corporation, registered in the Cayman Islands.

The ruling party adopted the bill amending the Tax Code in an expedited manner, with three readings on April 19. Within days, Georgian Dream got support from the business community. Accordingly, the new tax incentives introduced by the ruling party give the impression that these amendments were tailored to benefit specific business sectors to secure their loyalty and support.

Offshore Companies Linked to Bidzina Ivanishvili

In the research process, it was essential to examine the impact that the new amendments to the Tax Code would have on companies associated with Bidzina Ivanishvili.

Currently, 14 offshore companies linked to Bidzina Ivanishvili have been identified (though this number may be significantly higher):

- Limestone Finance International
- Finsec Limited
- Ringold Finance Limited
- Vanity Overseas Limited
- Gilmar Holding Limited
- Christa Investment Limited
- Sargans Limited
- Tarpan Management Limited
- Fresno Management Limited
- Frankston International
- Brystone Finance Limited
- Ecliton Commerce Corp.
- Vizelia Enterprises Limited
- GCF Luxembourg

These offshore-registered companies, in turn, own several Georgian companies, most of which fall into the second and third categories.[21]

[21] **Fourth Category Enterprise** – An entity that meets at least two of the following three criteria by the end of the reporting period:
a) Total asset value does not exceed 1 million GEL;
b) Revenue does not exceed 2 million GEL;
c) Average number of employees during the reporting period does not exceed 10.
Third Category Enterprise – An entity that does not qualify as a fourth-category enterprise and meets at least two of the following three criteria by the end of the reporting period:
a) Total asset value does not exceed 10 million GEL;
b) Revenue does not exceed 20 million GEL;
c) Average number of employees during the reporting period does not exceed 50.
Second Category Enterprise – An entity that does not qualify as a third or fourth-category enterprise and meets at least two of the following three criteria by the end of the reporting period:
a) Total asset value does not exceed 50 million GEL;
b) Revenue does not exceed 100 million GEL;
c) Average number of employees during the reporting period does not exceed 250.

According to Georgian legislation, companies are divided into four categories for accounting and reporting purposes based on their revenue and assets. Companies in categories 1-4 are required to submit the previous year's financial statements to the "Service of Accounting, Reporting, and Auditing Supervision" by October 1. The financial statements of companies in categories 1-3 are public and published on the Ministry of Finance's reporting portal.

Despite the law requiring all companies to disclose financial documentation, several companies associated with Bidzina Ivanishvili violate the law by not publishing declarations, resulting in some outdated data.

Companies required to submit financial declarations but have not published recent ones:

- JSC Cartu Group

The last declaration of JSC Cartu Group was published in 2019.

- Finservice-XXI LLC

The most recent financial declaration of Finservice-XXI LLC is from 2021.

From the limited data available and examination of the financial declarations of these companies, it was found that companies linked to Bidzina Ivanishvili have accumulated hundreds of millions in undistributed profits, which, if desired, Bidzina Ivanishvili could withdraw tax-free.

These companies are:

- JSC Cartu Group

The company engages in commercial banking, insurance activities, issuing loans and guarantees, securities and foreign exchange transactions, as well as accepting deposits. According to its 2019 financial declarations, the company had undistributed profits of **278,303,000 GEL**. Clearly, this data needs updating, and the amount would likely be higher in recent years.

Note: From 2018 to 2021, the company was classified as a Category II enterprise. However, according to information from the Service of Accounting, Reporting, and Auditing Supervision, JSC Cartu Group was reclassified to Category IV in 2022. Since JSC Cartu Group has been violating the law and concealing financial information since 2019, precise details are unknown.

First Category Enterprise – An entity that meets at least two of the following three criteria by the end of the reporting period:

a) Total asset value exceeds 50 million GEL;

b) Revenue exceeds 100 million GEL;

c) Average number of employees during the reporting period exceeds 250.

- Finservice-XXI LLC

The company's activities include renting and managing owned or leased properties, providing services, and issuing loans. According to the 2021 report, the company has accumulated profits of **80,458,854 GEL**.

- Inter Consulting + LLC

As of the report published in 2023, the company had undistributed profits of **38,775,065 GEL**. The company operates in other financial services, excluding insurance and pension funds, and does not require licensing or special regulation.

- Georgian Holding LLC

According to the latest report submitted in 2023, the company had accumulated profits of **8,744,272 GEL**. The company engages in commercial banking, insurance, issuing loans and guarantees, securities and foreign exchange operations, and accepting deposits.

The above companies could have withdrawn undistributed profits tax-free within a four-month period, which is ample time to take advantage of the tax incentives. The fact that two companies linked to Bidzina Ivanishvili, JSC Cartu Group and Finservice-XXI LLC, have been violating the law for years by not submitting financial statements reinforces suspicions that the incentives may have been tailored to the interests of the oligarch.

High-Value Artworks and Property Exempt from Taxation

The amendments to the Tax Code not only include a one-time exemption on Corporate Income Tax for enterprises but also cover exemption from import duties on assets brought into the country by offshore companies, as well as property tax exemption until January 1, 2030.

More specifically, any offshore company will benefit from the new tax incentive if it decides to bring the following items into Georgia: artworks, collectibles, antiques, precious metals (gold, silver, platinum), precious stones (diamonds, pearls, etc.), and jewelry made from precious metals.

Before the introduction of this incentive, the items listed above were taxed at rates ranging from 12-18%, which will no longer apply following the amendments to the Tax Code.

The public is well aware of Bidzina Ivanishvili and his family's particular interest in art. According to data published by Bloomberg in 2024, the value of his art collection is estimated at 1 billion USD. This incentive would enable Mr. Ivanishvili to bring his artworks into Georgia without incurring taxes.

Considering the value of even a single piece in his collection, it's evident how much revenue the budget will forgo as a result of this change. For example, Bidzina Ivanishvili's collection includes Pablo Picasso's famous painting *Dora Maar au Chat*, which he purchased for 95,216,000 USD at a Sotheby's auction in New York in 2006. This painting by Pablo Picasso is one of the most expensive artworks in the world.

This exemption is not exclusive to any one individual but applies to everyone. Thus, other oligarchs are also given the opportunity to bring property into Georgia without taxes.

It is also noteworthy that on October 2, 2024, the Minister of Finance published Order No. 329, dated October 1, 2024, amending Order No. 996 of December 31, 2010, "On Administration of Taxes."

According to this amendment, an importer must submit a preliminary application with documentation to the tax authority to qualify for the import duty exemption. Following a review of the documentation, the Revenue Service will inform the importer of its decision regarding the exemption within 10 days.

This amendment in the Minister's order can be seen positively; however, it does not eliminate the risks discussed above.

Exemption from Property Tax

Property tax exemption is another significant benefit, providing substantial advantages to a company holding high-value property in Georgia, while representing a considerable loss for the local budget.

For this benefit, it is sufficient for an offshore company to own real estate and pay annual property tax, after which it can transfer the property to a Georgian enterprise (with the same beneficial owner) and, until January 1, 2030, no longer pay property tax on these assets. Interestingly, the transaction of transferring the assets to the Georgian company is also exempt from profit/income tax.

This property tax exemption is not coincidental, as an example illustrates how clearly it aligns with private interests.

The so-called "Rike Domes" is one of the "legacies" left to the new government, Georgian Dream, by the previous administration in 2012. After 98 million GEL had been spent on its construction, Georgian Dream halted the project upon coming to power. Since 2013, the property has been transferred to the Ministry of Economy's balance sheet, where it has become a "burden" for the Ministry. The National Agency of State Property only managed to sell the "Rike Domes" on its sixth auction attempt. The buyer of this property was "Global Victory Trust," an offshore company registered in Luxembourg. According to the real estate records, the current owner of the property remains this offshore company. Global Victory Trust is connected to a Georgian businessman active in Russia, Davit Khidasheli.

The investment obligations the company assumed are also of interest. According to documentation, "Global Victory Trust" is obligated to invest at least 20 million GEL and establish museums of wine, technology, and digital art, as well as exhibition and other spaces, on the site within 36 months.

Since the direct owner of the Rike Domes is registered offshore, if the offshore company transfers the property to a Georgian entity (with Davit Khidasheli remaining as the beneficial owner), it will be able to avoid paying property tax until 2030. Given that the market value of the Rike Domes is estimated at approximately 100 million GEL, this benefit will be profitable for the company but not for the budget of Tbilisi Municipality.

Davit Khidasheli is closely associated with Bidzina Ivanishvili. From 2007-2014, Davit Khidasheli led the Russian corporation "Sistema" for Russian oligarch Vladimir Yevtushenkov, who, in turn, has close ties with Bidzina Ivanishvili. Davit Khidasheli is also the key figure in the so-called "Cartographers' Case," as the investigation began based on a map he provided.

Conclusion

The tax amendments introduced by the ruling party, presented as measures to promote the country's economic welfare, could, in reality, become a financial burden on Georgia's budget. Given that little time has passed since the new legislative changes took effect, the examples provided in the text are speculative.

The offshore companies mentioned in the study represent only a small portion of the enterprises likely to benefit from these incentives. In reality, their scale is much larger, which will have a significant impact on the country's budget revenues.

The companies benefiting from these incentives require additional monitoring and research. Due to frequent violations of the law by large enterprises that fail to submit financial declarations, gaining an accurate picture is challenging. Weak enforcement mechanisms allow companies to evade reporting by opting to pay fines and to conceal information on their financial status year after year.

The new tax amendments suggest that they may have been tailored to specific business interests, with some companies benefiting from exemptions on undistributed profits and others from exemptions on property and import taxes. This latter exemption would be especially advantageous for both Bidzina Ivanishvili and other oligarchs from various countries.

Discussions on potential sanctions against Bidzina Ivanishvili have intensified in the West. On September 20, Voice of America reported that the United States has developed a sanctions package against the Georgian oligarch, expected to be imposed in the near future.

Consequently, these legislative changes further reinforce suspicions that the Georgian government aims to create a favorable environment for businessmen and oligarchs to shield them from impending sanctions.

III.Legislative Changes in Georgia: Context Analysis from the Political Regimes Study Perspective

Introduction

As the Georgian Dream was starting to discuss the Foreign Transparency Act (commonly known and hereafter referred to as the "Russian Law"), the fast-track adoption of amendments to the Tax Code related to offshore companies sparked widespread public discussion about the possible reasons for passing this law and its anticipated consequences. This chapter aims to assess this issue from the perspective of comparative studies of political regimes. Specifically, the first part will review the type of political regime that Georgia represents under the Georgian Dream rule, how political and economic interests interact in such regimes, and what influence economic elites have on shaping economic policy. The second part will discuss to what extent this law might strengthen the stability of the Georgian Dream political regime and, theoretically, what impact it might have on Georgia's democratization process and Euro-Atlantic integration.

Georgia on the Verge of Authoritarianism

According to Freedom House 2024 report, Georgia is considered a hybrid regime with a trend toward autocratization.[22] This means that while regular and somewhat competitive elections are held in Georgia, there has been a growing influence of oligarchic interests on political institutions. The freedom of the opposition, media, and civil society is increasingly restricted, and political rights and liberties are systematically violated.[23] The "Russian Law," which the government passed at the cost of widespread public protests and damaging relations with international partners, has further uncovered the Georgian Dream's authoritarian intentions and its drive toward consolidating power.

In order to realistically assess the extent to which the Georgian Dream has the potential to maintain political power for an extended period of time by resorting to undemocratic methods, and to understand the logic of its functioning, it is essential to comprehend, in general, what sustains the power and viability of undemocratic regimes.

The three pillars of undemocratic rule

In political science, many theories attempt to explain the stability of undemocratic political regimes. The primary goal of these theories is to determine why some undemocratic regimes maintain their viability for extended periods, while others collapse quickly. One of the most widely known

[22] Freedom House. „Nations in Transit." 2022. Available at: https://cutt.ly/qeo1YuY1. Last accessed: 13.06.2024.
[23] Ibid

approaches is the so-called three pillars theory proposed by Johannes Gerschewski.According to this theoretical framework, the stability of any undemocratic regime depends on the combined and balanced use of three tools: legitimacy, repression, and co-optation.[24] Some authors argue that discussing the legitimacy of an undemocratic regime is inherently paradoxical, as the regime's undemocratic nature stems precisely from its limited dependence on the people's will. However, empirical studies on the longevity of political regimes demonstrate that legitimacy is the cornerstone of an undemocratic regime's stability, and it is in relation to this that other tools for maintaining power are employed. Legitimacy refers to the justification of power by the ruling authority in the eyes of the broader public.[25] The source of legitimacy can vary and may include political ideology, propaganda, practical achievements (such as economic growth), or other means that cultivate a sense among the population that the leader has both the ability and the right (despite being undemocratic) to govern the state.[26] Legitimacy does not necessarily imply active political support only; it also encompasses the passive consent of the broader public to the undemocratic leader’s political rule.
Repression is one of the backbouns of undemocratic regimes. It can range from high (e.g. indirect coercion) or low (e.g. prolonged inprisonment) intensity and can take both mass and selective forms.[27]

The third pillar is co-optation, which authorities often use to tie strategically important political groups to the regime elite. [28] Such groups may include opposition parties, intellectuals, the economic elite, and other influential actors. To achieve co-optation, the regime may use both formal mechanisms (e.g., political positions and offices) and informal influences (e.g., corrupt schemes).[29] During periods of instability and crises, undemocratic regimes are particularly prone to making "grand gestures" to secure the support of strategic groups.[30]

The stability of an undemocratic political regime depends on the balanced and strategic use of the three pillars mentioned above. Generally, legitimacy serves to gain the support of the broader masses, repression is used to intimidate active opponents, and co-optation aims to win over those groups whose support is crucial for the regime's stability, although employing violence against them may be overly risky.[31]

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[24] Gerschewski, Johannes. 2013. „The Three Pillars of Stability: Legitimation, Repression, and Co-Optation in Autocratic Regimes.“ Democratization 20 (1): 13–38, 14.
[25] Ibid.
[26] Ibid, 19.
[27] Ibid, 21.
[28] Ibid, 22.
[29] Ibid.
[30] Bertocchi, Graziella, and Michael Spagat. 2001. „The Politics of Co-Optation.” Journal of Comparative Economics 29 (4): 591–607, 606.
[31] Gerschewski, Johannes. 2013. „The Three Pillars of Stability: Legitimation, Repression, and Co-Optation in Autocratic Regimes.” Democratization 20 (1): 13–38, 25.

The government claims that the purpose of adopting the Offshore Law is to bring economic benefits to the country; however, they have not provided any factual evidence to support this assertion so far.[32] A legal analysis of the law shows that only Georgian and foreign companies owning financial assets in offshore jurisdictions will directly benefit financially from the tax relief. Consequently, it is likely that the actual goal of the law is to strengthen the support of the Georgian economic elite and attract certain types of economic groups from abroad that will back the Georgian Dream in the future to maintain a favorable economic environment. Thus, the law could contribute to the consolidation of power by the government, as economic and financial actors interested in tax relief will help ensure that the Georgian Dream remains in power.

The subsequent chapter will discuss why support from economic elites is particularly important for political regimes like Georgia's and what influence economic interests have on political processes.

Georgia – An Eurasian Patronal Regime

In the 1990s, following the liberation of several states from dictatorial rule, a phenomenon referred to as the "third wave of democratization," the theory of transition gained a dominant place in the study of political regimes. This theory posits that newly liberated states must navigate a transitional and linear process of democratization to achieve liberal democracy.[33] When analyzing the democratization process in post-communist countries, researchers traditionally focused primarily on assessing the quality of formal political institutions since the international actors' recommendations were mostly related to reforms of these formal political institutions. However, by the 2000s, it became clear that the quality of democracy in transitional states was not necessarily improving, and many of them were trapped in a sort of "gray zone" between democracy and authoritarianism. To describe this qualitatively new situation, the term "hybrid regime" was established.[34] The end of the transition paradigm prompted researchers to critically reassess the historical and political experiences of Third Wave states and to pay greater attention to the role of informal interests and actors in the region.[35] In this context, many scholars noted the excessive influence of economic interests on political life in the post-communist region, leading to the development of conceptual frameworks such as "kleptocracy," "patronalism," "clientelism," and "cronyism."[36] However, to fully explain the systemic connection between formal political institutions and informal economic or societal interests, it is necessary to

[32] Radio Liberty. „The Parliament beats presidential veto on the Offshore Law". 29.05. 2024. Available in Georgian at: https://cutt.ly/1eo0wXcz. Last accessed: 13.06.1998.
[33] Schmitter, Philippe C. Review of Democracy's Third Wave, by Samuel P. Huntington. The Review of Politics 55, no. 2 (1993): 348–51.
[34] Carothers, Thomas. "The End of the Transition Paradigm". Journal of Democracy 13, no. 1 (January 2002): 5-21.
[35] Magyar, Bálint, Alena Ledeneva, and Bálint Madlovics. 2022. The Anatomy of Post-Communist Regimes: A Conceptual Framework. Budapest: Central European University Press, 10.
[36] Ibid, 11.

theoretically demarcate the boundaries between spheres of public life and identify the logic of their interactions.

According to the German sociologist Claus Offe, human social action can generally be distributed across three spheres: (1) political, which relates to state institutions and the principles governing their functioning; (2) economic, which refers to regulations and contractual relationships associated with the market economy; and (3) social, which involves actions stemming from belonging to social groups (e.g., fulfilling cultural and traditional obligations).[37] In their book "The Anatomy of Post-Communist Regimes" Bálint Magyar და Bálint Madlovics rely on this theoretical framework to explain the political processes occurring in post-communist states. They argue that the clear separation of these three spheres of public life has taken a definitive form in Western European societies, whereas in the post-communist region, the political, economic, and social spheres are not clearly demarcated. This lack of distinction is attributed both to the broad network of informal structures that developed during the period of Soviet influence and to the comparatively weaker tradition of secularism in these societies.[38] Empirically, insufficient separation among the public, political, and economic spheres is manifested in the fact that actors operate with a singular, composite "identity" across all three spheres—economic and social interests influence political interests, and consequently, formal political institutions are intensely affected by informal influences arising from group and economic interests.

In conditions where personal interests exert excessive influence on political processes, a patronal system emerges, in which political power is based not on abstract and universal principles, but on a hierarchical system of exchanging material and personalized sticks and treats.[39] Such patronal networks typically exist outside formal political institutions; however, the main pillars of real political power often derive from these informal networks.[40] At the helm of these networks are patrons with symbolic and material power, who are typically referred to as oligarchs in the context of Eurasian politics.[41]

Patronal power is underpinned by three main pillars: (1) access to material resources necessary for rewarding allies; (2) the ability to perform punitive and rewarding acts, which requires direct influence over political institutions; and (3) the capacity to oversee clients and sub-patrons (relatively

[37] Ibid, 31.
[38] Ibid, 12.
[39] Hale, Henry E. 2014. Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective. New York, New York: Cambridge University Press, 9.
[40] Magyar, Bálint, Alena Ledeneva, and Bálint Madlovics. 2022. The Anatomy of Post-Communist Regimes: A Conceptual Framework. Budapest: Central European University Press, 41.
[41] Hale, Henry E. 2014. Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective. New York, New York: Cambridge University Press, 30.

lower-ranking patrons who are subordinate to the main patron but have their own clients), indicating the need for organized networks essential for the exercise of power. [42] Therefore, to maintain power, a patron must possess sufficient material wealth as well as political power and governance resources. After the dissolution of the Soviet Union, patronalism emerged as the primary form of political and social life in Eurasian states, though its intensity varied by country. [43] According to Henry Hale's classification, the least patronal countries include Croatia, the Czech Republic, Hungary, Poland, Slovenia, and East Germany. Countries with moderate patronalism include Estonia, Lithuania, Latvia, Serbia, and Slovakia, while the most patronal states are Albania, Armenia, Azerbaijan, Belarus, Bulgaria, Georgia, Kazakhstan, Kyrgyzstan, North Macedonia, Moldova, Romania, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.[44] In these latter countries, individuals with economic power have successfully used their financial resources to influence politics.

Regarding Georgia, Hale notes that it is one of the states in Eurasian political regimes that constantly experiences episodes of both democratization and autocratization. He also indicates that the main leader at the top of the patronal pyramid changed as a result of the Rose Revolution, yet the system and the architecture of relations remained largely unchanged, despite some progress in institutional reforms and the reduction of corruption. Furthermore, while the patronal networks during Shevardnadze's rule were primarily chaotic and self-regulating, the strengthening of state administrative functions and tendencies towards unilateral governance under Saakashvili's administration contributed to the reinforcement and systematization of these networks.[45]

The form of state organization most compatible with patronalism is a strong presidential republic, where the president not only formally heads the state but also embodies the singular patron at the top of the patronal pyramid.[46] In such a system, both formal and informal sources of power converge. At first glance, a parliamentary model, due to its theoretically pluralistic nature, may seem less compatible with a patronal society. However, if a single political group and its associated informal network dominate the legislative body through elections, that group's interests can extend its power over the entire political system and economic resources via a parliamentary majority.[47]

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[42] Ibid, 31.
[43] Ledeneva, Alena V. 2006. How Russia Really Works: The Informal Practices That Shaped Post-Soviet Politics and Business. Ithaca; London: Cornell University Press, 25.
[44] Hale, Henry E. 2014. Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective. New York, New York: Cambridge University Press, 61.
[45] Ibid, 13
[46] Ibid, 82.
[47] Ibid, 372.

Unlike Russia and Ukraine, where numerous and often conflicting oligarchic groups have infiltrated politics,[48] in Georgia, long-term political power has been held by a single oligarch, Bidzina Ivanishvili, who accumulated his wealth in Russia.[49] From 2003 to 2010, patronalism in Georgia primarily manifested in a hierarchical model of presidential governance, where political institutions somewhat reflected the interests of economic elites, and individual oligarchs (e.g., Davit Gamkrelidze, Levan Gachechiladze, Kakha Targamadze, and Badri Patarkatsishvili[50]) sporadically managed to gain political power. However, after 2012, under the rule of the Georgian Dream, Georgia became a clear example of the domination of formal political institutions by powerful informal financial interests.

Although the party's founder, Bidzina Ivanishvili, does not formally lead any political institution, nor is he inovlved in daily political processes, and has officially "retired" from politics several times, it is widely accepted among the public that the Georgian Dream party lacks its own political identity, serving primarily to unconditionally protect Ivanishvili's interests. The party's main role in the public sphere has been to function as a façade for his informal and covert power. Following Ivanishvili's return to politics in 2023, this time as the honorary chairman of the Georgian Dream, from where he holds the authority to propose a candidate for prime minister,[51] it became even clearer to the public that he never truly left politics, and that the Georgian Dream has always been aligned with his financial and political objectives.

Bidzina Ivanishvili maintains a strong influence over political institutions primarily through the granting key positions to individuals close to him. For instance, the current Minister of Internal Affairs, Vakhtang Gomelauri, is a former head of his personal security; the head of the State Security Service, Grigol Liluashvili, was previously the executive director of one of Ivanishvili's companies; former Prime Minister Irakli Garibashvili was Ivanishvili's personal assistant; former Chief Prosecutor and current Supreme Court judge Shalva Tadumadze held the position of Ivanishvili's personal lawyer; and former Minister of Health Ekaterine Tikaradze was a dentist close to Ivanishvili's family, among many others.[52] These examples indicate that Ivanishvili controls political institutions through informal connections, operating beyond constitutional order and completely disregarding democratic principles such as meritocracy, checks and balances, accountability, and transparency.

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[48] Ledeneva, Alena V. 2006. How Russia Really Works: The Informal Practices That Shaped Post-Soviet Politics and Business. Ithaca; London: Cornell University Press, 163.
[49] Ibid, 106.
[50] Hale, Henry E. 2014. Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective. New York, New York: Cambridge University Press, 126.
[51] Civil Georgia. „Honorary Chairman" to Formally Wield Power According to GD Updated Status." 10.01.2024. Available at: https://civil.ge/archives/576653. Last accessed: 06.08.2024.
[52] Transparency International Georgia, „Oligarch Bidzina Ivanishvili – the Real Ruler of Georgia and the Architect of Georgia's Pro-Russian Shift". 29.05.2024. Available at: https://transparency.ge/ge/post/. Last accessed: 06.08.2024.

Another key indicator of Ivanishvili's excessive informal influence is the tendency of high-ranking officials to equate Georgia's national interests with Ivanishvili's personal interests. For example, in 2022, when the European Parliament adopted a resolution discussing Ivanishvili's negative influence on Georgian politics and his close ties to Russia, the then-Prime Minister Irakli Garibashvili sent a protest letter to the President of the European Commission President, Ursula von der Leyen, stating that "the mentioned passages in the European Parliament's resolution lack any justification and aim to discredit the governance system in Georgia."[53] Furthermore, in 2022, the then-chairman of the Georgian Dream party and the country's acting Prime Minister, Irakli Kobakhidze, linked the ongoing private dispute between Swiss bank Credit Suisse and Ivanishvili to Western countries' attempts to push Georgia into war.[54] This perspective subsequently became one of the main narratives of the Georgian Dream's anti-Western propaganda, culminating in the assertion that the U.S. had informally sanctioned Ivanishvili for refusing to engage in the war.[55]

Thus, when discussing the potential motives behind the adoption of the "offshore law," it is reasonable to assume that, in addition to the co-optation of economic elites and large business groups, the real aim of this law is to protect Ivanishvili's political and economic interests. The law would enable him to bring in his assets registered in offshore zones without incurring additional costs under favorable tax policies. This hypothesis becomes particularly credible given that the primary motivation for economic intervention in a patronal system is precisely the protection and maximization of the patron's/oligarch's economic interests.[56]

Neolibralism and Foreign Capital-Dependent Economy

In Georgia, as in many post-communist transitional economies, the economic development model since the 1990s has been based on liberalization, privatization, and deregulation policies aimed at building a market economy focused on attracting foreign capital and investments.[57] This approach took the form of state ideology during the governance of the United National Movement, which viewed neoliberal economic policy not only as the main means for the country's economic

[53] Interpressnews. „Irakli Gharibashvili sends a letter to Ursula von der Leyen". 18.07.2022. Available in Georgian at: https://www.interpressnews.ge/ka/article/719766-irakli-garibashvili-ursula-pon-der-laiens-cerilit-mimartavs. Last accessed: 06.08.2024.
[54] Civil Georgia. „As Ivanishvili Battles Swiss Bank, GD hints at U.S. pushing Georgia into war". 11.05.2022. Available at: https://civil.ge/ka/archives/489858. Last accessed: 06.08.2024.
[55] Tabula Magazine. „O'Brien about Ivanishvili: For such an influential individual, to be this badly misinformed is just shocking", 14.05.2024. Available in Georgian at: https://tabula.ge/ge/news/718153-. Last accessed: 06.08.2024.
[56] Magyar, Bálint, Alena Ledeneva, and Bálint Madlovics. 2022. The Anatomy of Post-Communist Regimes: A Conceptual Framework. Budapest: Central European University Press, 363.
[57] Timm, Christian. 2013. „Economic Regulation and State Interventions: Georgia's Move from Neoliberalism to State Managed Capitalism." PFH Forschungspapiere/Research Papers, 14.

development but also as a way to reduce corruption, informal influences, and oligarchic tendencies.[58] It should be noted that the neoliberal economic reforms of the United National Movement were implemented alongside the strengthening of the old structures of patronalism and the creation of new networks. These connections were formed in the context of unilateral governance and the construction of formal political institutions, which endowed them with a new synergy, often hierarchical and coercive in nature. For this reason, Henry Hale points out that Saakashvili's administration was one of the rare cases of patronalism, where informal networks were formed under conditions where the ruling power also had a real political ideology.

Before coming to power, the Georgian Dream actively criticized the libertarian policies of the United National Movement,[59] However, during its 12-year governance, its patronal network successfully integrated into the neoliberal market economy. Consequently, a fundamental reform of the neoliberal economic structure has never been on the agenda in Georgia, and the country continues to be characterized by high unemployment and external migration rates, a negative trade balance, and excessive dependence on foreign direct investments and tourism.[60]

The need to review the existing neoliberal economic policy in Georgia is well demonstrated by numerous statistical indicators. For example, although absolute poverty has slightly decreased in recent years, the level of relative poverty remains critically high, amounting to 19.8% in 2023.[61] Additionally, in 2023, the number of people receiving state social assistance reached a historical maximum, comprising nearly 18% of the total population (676,641 persons).[62] The level of social inequality is also consistently high—according to 2023 data, the Gini coefficient equals 0.36.[63] One of the accompanying consequences of poverty and social inequality is the mass outflow of citizens from the country: in 2023, a record number of 163,000 people left Georgia .[64]
In a patronal system, the state's economic policy primarily serves to protect the interests of the patron and their informal network. However, to disguise this motivation, the patron attempts to deliberately blur the line between private and public interests.[65] For this reason, the Georgian Dream tried to

[58] Ibid.
[59] Tabula magazine, „Economic policy in the Georgian Dream's election programme." 31.08.2012. Available in Georgian at: https://cutt.ly/5eo053sd. Last accessed: 13.06.2024.
[60] Topuria, Salome and Khundadze, Tato, 2022. „Neoliberal status quo: why the free trade agreement between Georgia and the EU is not working", 6. Friedrich Ebert Foundation, Available in Georgian at: https://cutt.ly/meo2uda7. Last accessed: 13.06.2024.
[61] Social Justice Center. „Pro-govenrment media manipulates with poverty related statistical data". 30.04.2024. Available at: https://socialjustice.org.ge/ka/. Last accessed: 08.06.2024.
[62] Social Justice Center. „Number of beneficiaries of the state social support system is at the historic highest point." 05.07.2023. Available: https://socialjustice.org.ge/ka/produ. Last updated: 06.08.2024.
[63] National Statistics Office of Georgia. "Poverty and Gini Coefficients." Available at: https://www.geostat.ge/en/modules/categories/192/living-conditions. Last accessed: 06.08.2024.
[64] Radio Liberty. „Never before has Georgia had so many immigrants: why Georgians leave their country and where they go". 06.05.2024. Available at: https://www.radiotavisupleba.ge/a/%E. Last accessed: 06.08.2024.
[65] Magyar, Bálint, Alena Ledeneva, and Bálint Madlovics. 2022. The Anatomy of Post-Communist Regimes: A Conceptual Framework. Budapest: Central European University Press, 616.

instrumentalize the discourse of neoliberalism to justify the adoption of the Offshore Law, linking a milder policy and the attraction of foreign capital to the country's economic growth and public welfare from the outset.[66]

It is noteworthy that foreign direct investments do not inherently lead to a country's economic development. If their inflow is not accompanied by industrial and technological development and if the rule of law and human rights are not adequately protected, it is likely that the state will become excessively dependent on foreign capital, social inequality will deepen, risks of local labor exploitation and environmental degradation will increase, and informal influences of economic actors on political processes will expand.[67]

These risks become significantly more acute and widespread when foreign capital enters the country from offshore zones, as financial assets in offshore locations are typically placed there not only due to tax benefits but also to avoid financial transparency.[68] Accordingly, the Offshore Law will provide an incentive for the influx of opaque and vaguely sourced capital in Georgia, including sanctioned capital, which may serve to undermine democracy in both Georgia and other countries, as well as to fund crime, war, and terrorism. The concentration of such actors and their interests in Georgia is expected to create a risk of isolation from the international financial and economic system, deteriorate the quality of domestic and external security, and further complicate the possibility of freeing political institutions from informal influences.

Internatinoal Leverages and Geopolitical Reshuffle

To explain the differing outcomes of the democratization process in post-communist states, Lucan Way and Steven Levitsky focused their study around the international influence of democratic states and proposed the theory of leverage and linkage.[69] The degree of influence from Western countries is determined by how susceptible a given country is to democratization pressures from the U.S. and the European Union.[70] Specifically, it considers the state's ability to bargain with the West and its vulnerability to the West's punitive economic, strategic, or political decisions in response to patterns of authoritarianism.[71] Linkage, on the other hand, encompasses the combination of economic,

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[66] Radio Liberty. „The Parliament beats presidential veto on the Offshore Law". 29.05. 2024. Available in Georgian at: https://cutt.ly/1eo0wXcz. Last accessed: 13.06.1998.
[67] Topuria, Salome and Khundadze, Tato, 2022. „Neoliberal status quo: why the free trade agreement between Georgia and the EU is not working", 33. Friedrich Ebert Foundation, Available in Georgian at: https://cutt.ly/meo2uda7. Last accessed: 13.06.2024.
[68] Johnson, Simon, and Daron Acemoglu. 2024. „Dark Offshore Money Threatens Democracy". Project Syndicate. 2024. Available at: https://cutt.ly/weo2pUln. Last accessed: 13.06.2024.
[69] Way, Lucan A., and Steven Levitsky. 2007. "Linkage, Leverage, and the Post-Communist Divide." East European Politics and Societies: And Cultures 21 (1): 48–66, 48.
[70] Ibid.
[71] Ibid, 50.

political, geographical, social, organizational, and other types of connections with Western countries, the intensity of which determines how effective the mechanisms of influence from the West will be. For instance, the effectiveness of terminating trade-related agreements will be greater the more dependent a country's economy is on trade and investment with Western partners; likewise, the impact of tightening border policies will be stronger the more frequent the cross-border migration movements are.[72]

It is reasonable to assume that the Georgian Dream is aware of the existence of these mechanisms. Georgia is closely dependent on economic, political, diplomatic, and humanitarian support from Western states, which can be used as leverage against the government should the country face imminent threat of authoritarianism. A clear example of this is the U.S.'s reconsideration of its relations with Georgia in light of the adoption of the "Russian Law," which led to visa sanctions imposed on around 30 individuals associated with the Georgian Dream.[73] It is likely that Bidzina Ivanishvili, who has previously considered himself sanctioned,[74] aims to create a space in Georgia protected from sanctions for his assets through the Offshore Law. This space may also become attractive for Chinese, Russian, or Iranian companies anctioned by Western states. Consequently, it is possible that tax incentives could facilitate closer ties with regional authoritarian regimes, and the Georgian Dream might view this alliance as an alternative to partnership with the West.

Conclusion

This chapter discussed the possible motivations behind the adoption of the Offshore Law by the Georgian Dream from the perspective of various theories developed in the study of political regimes and their combinations. The hypotheses related to the potential outcomes of the law were also articulated through this lens. While it is possible that the actual impact of the law on economic and political processes may differ from the thinking outlined in the chapter, the rapid authoritarianism characteristic of the recent period of the Georgian Dream administration, the pursuit of isolation from democratic states, and the search for allies in authoritarian regimes strongly suggest that the Offshore Law, like the Russian Law, aims to further subordinate the country's economy and politics to oligarchic interests. Specifically, through the Offshore Law, the Georgian Dream is likely to attempt to win over profit-generating businesses and economic elites, protect and expand Bidzina Ivanishvili's personal wealth, and strengthen ties with undemocratic allies such as Russia and China.

[72] Ibid, 56.

[73] Tabula magazine. „What we know about sanctions against the Dream and those sanctioned?" 06.06.2024. Available in Georgian at: https://cutt.ly/Peo2IG7Z. Last accessed: 13.06.2024.

[74] Radio Liberty, „We will reconsider in no time" - O'Brien on imposing sanctions against Ivanishvili", 14.05.2024. Available in Georgian at: https://cutt.ly/Jeo2AfHN. Last accessed: 13.06.2024.