

TAX AND LEGAL NEWSLETTER

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Amendment to the Law

In July 2020 number of significant amendments (14.07.2020, № 6817-rs) were made to the Tax Code of Georgia. The amendments affected the chapter of VAT in full and other articles as well.

The draft of VAT was developed to approximate tax legislation with the EU VAT Directive (2006/112/EC). As a result, the VAT reform based on international practice will improve the investment environment, reduce disputes, and simplify the fulfillment of tax obligations. There is an opportunity to develop internal procedures for the application of European Court decisions and interpretations in practice.

Value Added Tax Reform

According to the amendments, the VAT regulations of the Tax Code have been completely revised. The following articles stand out from these amendments:

Economic activity for VAT purposes

The following activities have been considered as economic activities for VAT purposes:

- ▶ Entrepreneurial activity
- ▶ Activities of persons providing goods/services
- ▶ The use of the property to obtain regular income, while one-time, irregular transactions (other than the supply of non-residential property) are not subject to VAT.

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Economic activity is not usually considered to be the activity of public institutions within the scope of authority delegated to it by the state. As an exception, some types of state authorities' activities, which will be considered as economic activities, are defined.

To avoid restriction of competition, the Government of Georgia will have the right to further define the list of activities, the implementation of which will be considered to be economic.

Transactions subject to VAT

The taxable transaction under VAT was defined as the supply of goods and/or services in exchange for compensation in the territory of Georgia within the scope of economic activity, as well as the importation of goods. The delivery of assets during the reorganization, contribution to the capital, or delivery of all the assets of an enterprise, as well as temporary importation of goods, is no longer considered a VAT taxable transaction.

Taxation of advance payment with VAT

Taxation of advance payments will also apply to continuous and regular deliveries, except for cases of regular and uninterrupted delivery of goods (electricity, natural gas, water, and other similar goods).

Taxation of free of charge supply by VAT

According to the amendment, the free delivery of goods will be taxed only if the relevant person has credited VAT on this expense. The provision of services free of charge will be taxed only if these activities are not related to the purpose of the payer's activities or are performed for the personal benefit of the employee. In addition, the supply of goods by a VAT payer for the personal use of its employees or the supply/use for a purpose other than the purpose of its business shall be taxable with VAT, if the payer has fully or partially credited VAT on these goods or expenses.

Transfer/use of goods in the form of a sample or a small gift will not be subject to VAT. A small value gift shall be defined as a good or service, the transfer of which is free of charge, and the value of which, excluding VAT, does not exceed GEL 50 per natural person in one calendar year. Advertising and representation expenses are not considered a small value gift.

The free delivery of goods will be taxed at cost-price, instead of the market price.

Taxation of buildings or structures of one's own production with VAT

According to the amendments, the production of real estate (fixed assets) or the repair of one's own fixed assets for its own purpose will be taxed only if the person could not receive VAT credit in case of purchasing these goods/services from another person.

Taxation of leasing operation with VAT

In case of delivery of goods for the period specified in the lease agreement or with installment payment, the actual transfer of goods shall be considered as the delivery of goods for VAT purposes. Accordingly, the leasing transaction will be taxed with VAT at the moment of the actual transfer of the goods. In addition, the accrued benefits of leasing services will not be taxed with VAT.

Special scheme for taxation of the delivery of individual goods

Under the amendment, the taxation of the supply of used items, works of art, collectible items or antiques, becomes possible based on the profit margin.

In this regard, a new term - the taxable dealer - has been determined, which is defined as - any taxable person who, in the course of economic activity, buys or uses a used item, a work of art, collectible items or antiques, or imports these goods, in his name or another person, based on agreement, according to which the commission is paid when buying or selling goods.

VAT payable on the delivery of goods to the taxable dealer will be paid according to the profit margin received by the taxable dealer, and the profit margin is defined as the difference between the delivery price of the goods and its purchase price. The taxable amount is calculated by dividing the amount of profit margin received by the taxable dealer by 1.18.

Place of service delivery for VAT purposes

According to the amendments, the following two main principles will be applied to determine the place of delivery of services:

- ▶ In case of delivery of services by the business (taxable person) to other business (taxable person) (B2B) - the place of service delivery is considered to be the place of incorporation of the service purchaser;

- ▶ In case of delivery of services by the business (taxable person) to the customer (non-taxable person) (B2C) - The place of service delivery is considered to be the place of incorporation of the supplier.

Special rules for determining the place of taxation have been established for certain services.

Transactions exempted from VAT without the right of deduction

The delivery of services and goods directly related to medical and educational activities and ancillary goods/services shall also be exempted from taxation. In addition, ancillary services related to insurance and/or reinsurance provided by insurance brokers and/or insurance agents will not be taxed.

The area of application of the tax exemption in the medical and educational fields is being specified, the following will be exempted from taxation:

- ▶ Services of the provision of personnel by a religious organization, including for medical or educational activities;
- ▶ Provision of services/goods by the organization to raise funds for medical, educational and other social activities;

- ▶ Delivery of goods used only in exempt transactions in the medical, educational, cultural, sports, and social fields, unless the right to deduct VAT has arisen on the said goods.

Transactions exempted from VAT with the right of deduction

The following are also exempt from VAT with the right of deduction:

- ▶ Medicinal/treatment goods produced in Georgia, the list of which is determined by a subordinate normative act.
- ▶ Delivery of services by an intermediary acting on behalf of another person in case of international transportation of goods or participation in transactions carried out outside Georgia. Transactions exempted from VAT with the right of a deduction related to the transportation of goods will be expanded and specified, the following shall be exempted:
 - ▶ The supply of goods on the high seas or for the paid-for carriage of passengers or commercial, industrial or fishing activities or rescue or relief operations in the sea, etc.;
 - ▶ The delivery, conversion, repair, maintenance, freight or lease of ships and aircraft, and supply, lease, repair or maintenance of equipment installed or used on such ship, etc.

Calculation of the proportion of creditable VAT

The amount of turnover related to real estate or financial transactions will no longer be taken into account when calculating the proportion of creditable VAT if those transactions are ancillary to the taxable person's main business activity.

Refund of paid VAT

According to the amendment, the supplier of goods can return the paid VAT if the natural person/passenger based in a foreign country has taken the goods delivered outside of Georgia.

Effective from
January 1, 2021.

Amendments to other articles of the Tax Code

The same law, in addition to VAT, also addressed amendments in other issues, of which we would like to highlight the following:

Estimated accrual

The article 66¹ has been added to the Tax Code, according to which the tax authority is authorized to carry out an estimated accrual without tax audit based on the information in its possession, if:

- ▶ There is a reasonable assumption that an unjustified reduction of the tax amount was carried out on the taxpayer's registration card. In this case, the estimated accrual can be made only in the amount of the reduced tax;
- ▶ The taxpayer has not fulfilled the obligation to submit a tax return/calculation within the timeframe established by the tax legislation.

The estimated accrual can be adjusted by corrective accrual, and the rule of estimated and corrective accrual is determined by the order of the Minister of Finance of Georgia.

Effective from July
23, 2020.

Multinational Enterprise Group Reporting

A new Article 70¹ has been added to the Tax Code, which clarifies the group of multinational enterprises and their obligation to submit reports.

The final parent enterprise of a group of multinational enterprises, which is a resident of Georgia, is obliged to submit a report to the tax authority according to countries by December 31 of the year following the reporting year.

The procedure for submitting a report of a group of multinational enterprises shall be determined by an order of the Minister of Finance.

Effective from July
23, 2020.

Leasing / renting property by a non-resident natural person / enterprise

According to the amendments, if a non-resident individual/enterprise receives remuneration for rent/lease from a person who is not a tax agent, then the taxable amount of income tax is the difference between the gross income received from Georgian source during a calendar year and the deductions related to this income.

Effective from July
23, 2020.

Exemption from Personal Income Tax

Amendment was made to Article 82(1(f.c)), surplus gained from the supply of assets owned for more than two years, (except where the transferor of assets uses the assets for economic activity before their supply) is exempt from Personal Income Tax, the use of an asset for economic purposes shall not be taken into account if 2 years have elapsed between the date on which it was used for economic purposes and its transfer.

Effective from July
23, 2020.

Further distribution of dividends received

Subparagraph (e) has been added to Article 98¹(2), according to which further distribution of dividends received by corporations, companies, firms and other similar entities (other than a permanent establishment of a foreign enterprise) established under foreign legislation shall not be considered as distributed Profit, in case such entities have transferred management to Georgia.

Effective from July 23, 2020.

The subject to Corporate Income Tax

Subparagraph (g) has been added to Article 98³(3), according to which a person is not taxed for the supply of goods, services and/or transfer of funds free of charge to a person who is taxed based on a new (so-called "Estonian model") model.

Effective from July 23, 2020.

A benefit that is not considered as salary income

Subparagraphs "e" and "f" have been added to Article 101(3), according to which the following shall not be considered as salary income:

- ▶ The benefit received by paying the insurance premium in favor of the employee by the employer within the framework of compulsory insurance under the legislation of Georgia;

- ▶ Transfer of accommodation and/or provision of catering services and/or reimbursement of expenses related to the same services by the employer to the employee, if all the following conditions are met:

- ▶▶ accommodation/catering is provided based on the nature of the employer's activities and is a necessary condition for the employee to properly fulfill its obligations under the employment contract and/or accommodation/catering of the employee, without provision by the employer, requires the employee to incur unreasonable expenses and/or to spend unreasonable time;

- ▶▶ Transfer of housing and/or provision of catering services and/or reimbursement of expenses related to the same services is not part of the remuneration provided for in the employment contract between the employer and the employees.

Effective from July 23, 2020.

Deduction of reserves for possible loan losses

According to the amendment to Article 109(2), it is stipulated that banks and credit unions, under the rules established by the

National Bank of Georgia on the classification of assets and the creation and use of reserves of possible losses by commercial banks, shall deduct the reserves of possible losses of the loan defined by the same rule.

Effective from July 23, 2020.

Taxation of interest at the source of Payment

With the amendment to Article 131 (1), interest paid by or on behalf of a non-resident permanent establishment or resident to an organization shall no longer be taxed at the rate of 5% of the amount payable at the source of payment.

Effective from July 23, 2020.

Property taxable with Property Tax

Article 201(1)(a) has been amended and, in addition to the property envisaged before, the resident enterprise/organization has been required to tax the following property with property tax:

- ▶ Real estate, yachts (motor-boat), helicopters, airplanes, and other means of transport received (in ownership) within the framework of the collateral to ensure the fulfillment of the contractual obligation.

► Real estate, yacht (motorboat), helicopter, airplanes, and other means of transport purchased at the auction, direct sale, or purchased otherwise instead of the fulfillment of monetary obligation (except for sanctions imposed by criminal and administrative rules).

Effective from July 23, 2020 and applies to legal relationships arising from 2020.

Sanctions for tax violations

As a result of the amendment to Article 282(4), in case of application of the penalty provided for activities without registration as a VAT payer, the penalty shall no longer be used for tax reduction in the tax return.

As a result of the amendment of Article 286(1), the sanction for the entrepreneurial activity of transportation of goods without a waybill was reduced, for not issuing a waybill at the buyer's request or for refusing to accept a waybill when purchasing goods and for the goods, the value of which exceeds 10,000 GEL, the sanction in amount of 500 GEL was applied instead of 10,000 GEL.

Effective from July 23, 2020.

Exemption of real estate delivery from VAT

Article 309(79) was amended and, consequently, the supply of real estate the construction permit of which was valid as of August 8, 2008, and the provision of related construction and installation services were exempt from VAT from 1 January 2015 to 1 January 2026, is exempt from VAT with the right of deduction. According to the version before the amendment, the exemption applied to real estate and related construction and installation services provided before January 1, 2023.

The statute of limitations for exempt taxable transactions in the reporting periods from January 1, 2015, to January 1, 2023, has been increased.

Effective from July 23, 2020.

According to the law of Georgia №6815-rs as of July 14, 2020, another amendment was made to the Tax Code of Georgia:

Investment Fund

Based on the amendment Article 23¹ has been added to the Tax Code. An investment fund is defined as an enterprise established under the Law of Georgia on Investment Funds in the form of a joint investment fund or investment company, the management and administration of which, as well as the provision of depository services to the investment fund, are considered financial services.

The owners of the joint investment fund units carry out tax reporting independently. Besides:

- The Joint Investment Fund and its asset management company shall not be obliged to act as agents provided for in Article 154 of this Code.
- Carrying out activities under the Law of Georgia on Investment Funds by the owner of the joint Investment Fund unit or on his behalf does not constitute a permanent establishment for the owner of this unit in Georgia.
- Within the framework of the activities of the Joint Investment Fund defined under the Law of Georgia on Investment Funds, Corporate Income Tax shall not apply to:
 - ► distributed Profit
 - ► costs incurred or other payments not related to economic activity
 - ► free delivery of goods/services and/or transfer of funds
 - ► representation expenses paid in excess of a limited amount determined under this Code.
- Dividends paid by an investment company to a natural person or non-resident enterprise are not taxable at the source of payment and are not included in the recipient's gross income.

▶ The following expenses/allotments incurred by the investment company within the framework of the activities defined under the Law of Georgia on Investment Funds are exempt from Corporate Income Tax:

▶▶ costs incurred or other payments not related to economic activity

▶▶ free delivery of goods/services and/or transfer of funds

▶▶ representation expenses paid in excess of a limited amount determined under this Code

▶ Distribution of Profit by the investment company, if the recipient of the dividend is a non-resident or a natural person, is taxed at a rate of 15%, and when the investment company invests only in bank deposits and/or financial instruments (except in case of distribution of profits from the resident enterprise) the profit distribution will be taxed at a rate of 5%.

▶ Distribution of profit by an investment company to a non-resident or a natural person is exempt from Corporate Income Tax if the income from which the dividend is paid:

▶▶ Does not represent income from Georgian source;

▶▶ Represents income received from the sale of equity securities issued by a resident legal entity through a public offer in Georgia and admitted to trading on an organized market recognized by the National Bank of Georgia;

▶▶ Represents income received from the sale of loan securities issued by a resident legal entity through a public offer in Georgia and admitted to trading on an organized market recognized by the National Bank of Georgia, or income received in from of interest from this security;

▶▶ Represents surplus income received from the sale of loan securities issued by the Government of Georgia or an international financial institution or income received as interest from these securities or a deposit placed in a commercial bank.

To identify the amount of profit exempt from Corporate Income Tax, it is considered that this amount is allocated first when the investment company distributes the dividend.

▶ Surplus income received from the supply or redemption of a unit of an investment fund by a non-resident or natural person is taxed at a rate of 15%, and if the investment fund invests only in bank deposits and/or financial instruments, except when the investment fund invests in the shares/stocks of a resident enterprise, the excess income received from the supply or redemption of the investment fund unit will be taxed at 5%.

▶ The income shall be exempt from Corporate Income Tax and Personal Income Tax if it is received:

▶▶ By selling a unit of an investment fund admitted to trading on an organized market recognized by the National Bank of Georgia and issued through public offer;

▶▶ by selling of an investment fund unit or redemption of an investment fund unit, if the investment fund invests only in deposits placed in commercial banks of Georgia or securities issued by the Government of Georgia and/or the International Financial Institutes or in securities admitted to trading on an organized market recognized by the National Bank of Georgia and issued through a public offer by a public entity in Georgia.

The amendment is effective from October 20, 2020.

Amendment to the Decree

Documents for VAT deduction

By Decree №435 as of July 10, 2020, the Government of Georgia amended the Decree №401 of the Government of Georgia as of December 28, 2010 "On the Identification of Legal Entities under Public Law, the documents confirming the payment of the service fee of which are considered as VAT documents". In particular, sub-paragraph "n" was added to the first article, according to which the document confirming the fee paid in exchange for the services provided by the LEPL Digital Agency is considered a VAT document.

The Decree is effective from July 10, 2020.

Amendment to the Order

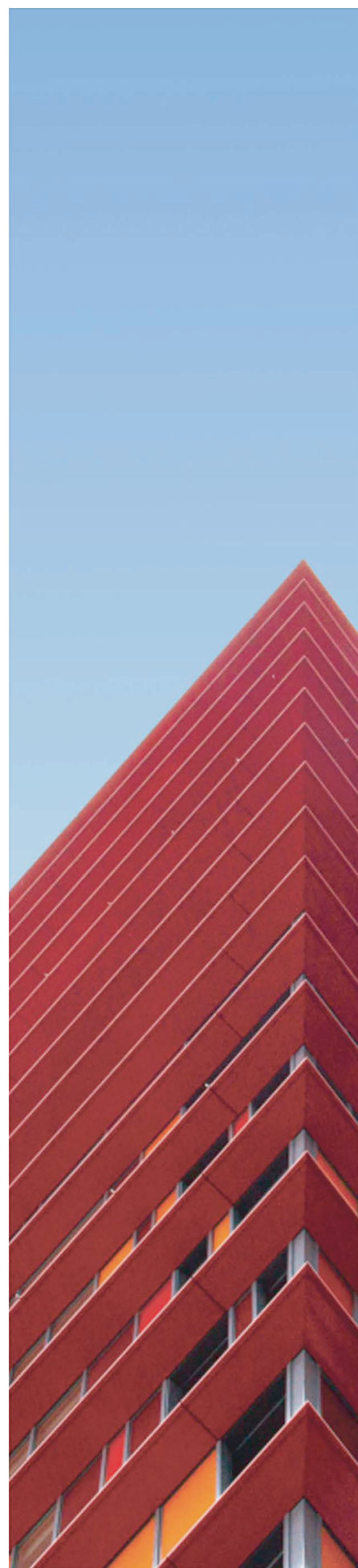
The term for pay- ment of Personal Income and/or Property Tax

On July 14 of the current year, Order №17079 (15.06.2020) of the Head of the Revenue Service was published, which amended the Order №13446 of the Head of the Revenue Service as of May 18, 2016 "On the Approval of the Methodological Guidelines on the Procedure for Preparation of Taxpayers' Registration Cards".

In particular, paragraphs 7 and 8 have been added to Article 23, according to which the deadline for payment of Personal Income Tax and/or Property tax payable in 2020 (including February, March, April and May 2020) has been extended by the Tax Code of Georgia to December 1 of 2020 for the taxpayers, who have submitted an application to the tax authority for deferral of Personal Income Tax and/or Property tax and in connection with which a positive decision has been made by the tax authority.

In this case, the penalty interest will not be accrued on the taxpayer under the Tax Code, and the data and current payments of the relevant tax return(s) submitted by the taxpayer will be reflected on the taxpayer's registration card as of November 30, 2020.

The Order is effective from June 26, 2020.





MARIAM KHUSKIVADZE
Mkhuskivadze@bdo.ge

MIKHEIL ENUKIDZE
MEnukidze@bdo.ge

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