

# *Legal Focus*

## **Taxation of International Organizations & their Partners**

- ◆ Taxation of the UN Agencies and their Contractors
  - ◆ Taxation of the EU Contractors
- ◆ Taxation of the US Government Contractors & Grantees

### **Beneficial Tax Regimes under International Treaties**

*International treaties and bilateral agreements often fail to solve the problem of paying extra taxes in Georgia by international/diplomatic organizations and their implementing partners, grantees or contractors (beneficiary entities).*

The reasons contributing to such failure include:

- ◆ Failure to ratify relevant international and bilateral treaties and literal interpretation of the Tax Code by the tax inspectors;
- ◆ Absence of clear and specific provisions in the ratified instruments;
- ◆ Absence of domestic normative acts implementing international and bilateral

treaties, certain provisions of which require further details and clarifications;

- ◆ Lack of awareness among beneficiary entities, tax inspectors and service/goods' providers.

#### **Frequently Faced Problems**

**Income Tax paid by Georgian Employees of Diplomatic Organizations**

**VAT Paid by Diplomatic Organizations and their Beneficiary Entities**

## The UN Agencies



### *To be Enforced, Bilateral Agreements Must be Ratified by the Parliament*

In order to apply tax provisions of an international treaty over those contained in the domestic legislation, the Tax Code of Georgia requires such international treaty to be ratified by the Parliament, a general mechanism necessary for enforcement of an international agreement. Against this requirement, UN Agencies can be divided into three main groups:

- ◆ Agencies which have duly ratified bilateral agreements – UNDP, UNHCR, UNICEF, IOM;
- ◆ Agencies having agreements signed by the authorized representatives of both parties, however, not ratified by the Parliament – WHO;
- ◆ Agencies not having agreements signed or ratified by the parliament – WFP, UNFPA, UNFAO, UNIFEM;

Agencies, which have not ratified agreements, are subject to the requirements of the domestic tax law.

### **Problems Faced by UN Agencies**

- ◆ Relevant international treaties and bilateral agreements are not ratified by the Parliament;

- ◆ Ratified bilateral agreements often do not provide for the full exemption from VAT or their provisions are not clear enough;
- ◆ Exemptions and benefits do not extend to the beneficiary entities;
- ◆ Income tax payment issue is unclear for local employees of those agencies, which either have no bilateral agreements concluded or such agreements are not duly ratified;
- ◆ Filing of the annual tax declaration forms by local employees of the UN agencies may lead to further pressure from the tax authorities, since there is no clear position of the Government of Georgia on obligation of these individuals to pay income tax;
- ◆ Frequently, vendors refuse to recognize special tax status of some UN Agencies;
- ◆ There is a lack of awareness among local authorities about application and use of bilateral agreements;

### **Policy Level Solutions**

**Step I.** Parliament of Georgia ratifies relevant international treaties and bilateral agreements with all UN Agencies operating in Georgia;

**Step II.** Internal procedural guidelines/instructions implementing provisions of international treaties and bilateral agreements are elaborated and adopted by the relevant governmental bodies;

## EU Contractors



### *Tax Exemptions under the General Rules Applicable to the Financing Memorandum Extend Only to the Imported Goods*

General Rules Applicable to the Financing Memorandum (the Memorandum) were ratified by the Parliament of Georgia on March 5, 1996 and regulate tax issues related to the projects implemented based on the technical cooperation contracts financed through the funds of EU subsidies. Given the fact that this instrument is ratified by the Parliament, its tax clauses supersede those contained in the domestic legislation of Georgia. Namely, following tax privileges are in place:

Since the Memorandum did not cover taxation issue of goods/services purchased within the territory of Georgia, on April 20, 2006, the Tax Department of the Ministry of Finance adopted the Order # 564 “on Using Tax Benefits as Provided by the “General Rules Applicable to the Memorandum on Financing” Signed by the European Union Commission and the Government of the Republic of Georgia on February 24, 1994”.

<b>Type of Tax</b>	<b>Exempt Category</b>
Income Tax	Natural persons (including Georgian nationals) working on the basis of technical cooperation contracts financed through the funds of EU subsidies
Social Tax	Legal entities working on the basis of technical cooperation contracts financed through the funds of EU subsidies
Profit Tax	Legal entities working on the basis of technical cooperation contracts financed through the funds of EU subsidies
Customs Tax	Goods (including equipment and automobiles) imported based on the technical cooperation contracts financed through the funds of EU subsidies; Items for personal use, household items, food products imported by persons working on the basis of technical cooperation contracts financed with the EU subsidies (except permanent residents)
Other Taxes imposed under the Tax Law	Goods (including equipment and automobiles) imported based on the technical cooperation contracts financed with the EU subsidies;

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## Problems Faced by EU Contractors

- ◆ Local employees of EU contractor entities often pay income tax;
- ◆ The Order is new and frequently not applied. Therefore, taxation issue of goods/services purchased within the territory of Georgia remains unresolved;
- ◆ VAT is paid on delivery of services to the EU contractors (foreign organizations) within the framework of programs implemented with the EU funding where the government is the one of the participating parties.

Georgia), **profit, social, property, excise** and any **other taxes** including **general state taxes related to rent, accommodations or transportation**. US entities are also exempt from **customs tax** on import of goods for personal use of the personnel of USG (other than Georgian nationals) or US private organization. Non-US entities are entitled only to the exemption from **VAT** and **customs duties** on import and delivery of goods/services within the assistance projects.

Special procedures for implementing the above benefits is elaborated and set out in the instructions implementing the Agreement. The Ministry of Finance is in charge of issuing special VAT exemption letters to the USG contractors/grantees based on the information submitted by the USG. However, the letters do not automatically grant exemptions from customs taxes for the goods to be imported within the assistance projects. There is a special procedure to be complied with in order to enjoy customs tax exemptions.

## USG Contractors & Grantees



Taxation issues of the US Government Assistance are regulated under the Bilateral Agreement between the Government of the United States of America (USG) and the Government of the Republic of Georgia Regarding Cooperation to Facilitate Humanitarian and Technical Economic Assistance (the Agreement) and instructions adopted based on the Order of the Ministry of Finance implementing the Agreement.

Tax advantages envisaged in the Agreement and the Instructions differ based on whether the beneficiary entity is the US or non-US implementer. Higher level of support is offered to the US entities implementing USG assistance projects. They benefit from exemptions from: **income** (on salaries of employees who are not nationals of

## Problems faced by the USG Contractors/Grantees

Due to the lack of awareness among the USG Contractors and Grantees regarding the procedures for benefiting from exemption from customs taxes, imported goods are often stalled at the customs. Subsequently, there are fees applied and often penalties imposed for delaying goods at the customs.

## Legal Support

*To eradicate the problems related to taxation, international agencies and their contractors need expertise of legal counsel with the knowledge of international and bilateral treaties, significant experience of working on drafting tax documents and instructions as well as ability to dialogue with the Georgian tax authorities.*

CFS Legal Attorneys offer strong international law background and extensive legal drafting experience. Our attorneys have participated in the process of drafting tax instructions and related documentation. Their approach to resolving legal issues is result oriented and their records include experience of assisting contractors of various international agencies, like UN and EU in resolving tax matters with successful outcomes.

## List of Relevant Treaties & Agreements

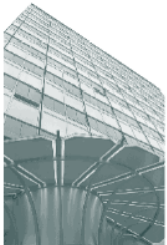
<b>Year</b>	<b>Name of the Treaty or Agreement</b>
1946	Convention on the Privileges and Immunities of the United Nations
1947	Convention on the Privileges and Immunities of the Specialized Agencies
1961	Convention on Diplomatic Relations
1969	Convention on the Special Missions
1993	Agreement between the United Nations and the Government of the Republic of Georgia (GOG) Relating to the Establishment of a United Nations Interim Office
1994	Standard Basic Assistance Agreement between the GOG and the United Nations Development Programme;
1996	Agreement between the GOG and the United Nations High Commissioner for Refugees
1999	Basic Cooperation Agreement between the United Nations Children's Fund and the GOG
-	Basic Agreement between the GOG and the United Nations World Food Programme (WFP)
-	Basic Agreement between the World Health Organization and the GOG
1994	Cooperation Agreement between the International Organization for Migration and GOG
1994	General Rules Applicable to the Financing Memorandum
1992	Bilateral Agreement between the Government of the United States of America and the Government of the Republic of Georgia Regarding Cooperation to Facilitate Humanitarian and Technical Economic Assistance

## CFS Legal Guledani & Partners

offers:

- ◆ *Special expertise in tax issues for entities implementing donor funded programs*
- ◆ *Access to most accurate and up to date legal information*
- ◆ *Assistance in dialogue with tax authorities and third parties*
- ◆ *Assistance in complying with the legal requirements*
- ◆ *Assistance in obtaining exemptions from VAT and customs taxes*

## Benefit from our Expertise



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*CFS Legal Guledani & Partners is a law firm founded with participation of CFS Investment Bank, first independent full services investment bank in Georgia.*

*Our full range of legal services allows us to provide highly skilled and superior, cost-efficient legal services suited to each client's needs. We serve as attorneys and legal counselors to public and privately held corporations, financial institutions, non-governmental organizations and individuals.*

*Our attorneys have extensive knowledge of the Georgian legislation and international law as well as understanding of business climate in Georgia.*

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