

**IMPACT OF THE
COVID-19
PANDEMIC
ON MUNICIPAL
BUDGETS AND
REVENUES
IN GEORGIA**

December 2020



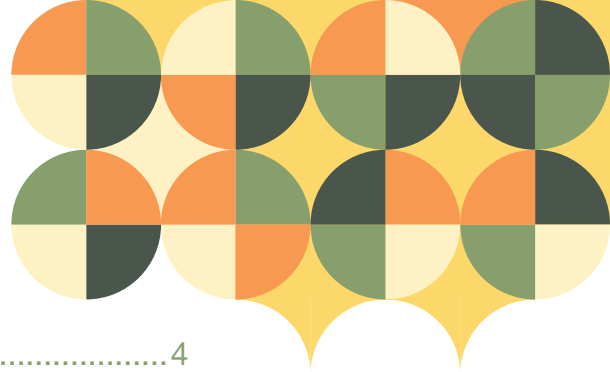
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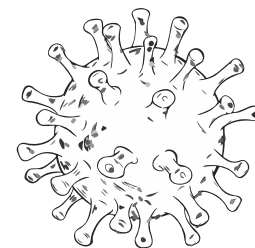


The research report “Impact of the COVID-19 Pandemic on Municipal Budget and Revenues in Georgia” is prepared by the National Association of Local Authorities of Georgia (NALAG) within the ***Fostering Regional and Local Development in Georgia, Phase 2*** project implemented by the United Nations Development Programme (UNDP) with the support of the Swiss Agency for Development and Cooperation (SDC), the Austrian Development Cooperation (ADC) and the Ministry of Regional Development and Infrastructure of Georgia (MRDI). The views expressed in the report are those of the author and do not necessarily reflect of the organizations listed above.

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Introduction

As the COVID-19 pandemic broke out in early 2020, Georgia more or less successfully overcame the initial shock and combatted the first wave of the virus's spread. Decisions taken by the Georgian government at that time were aimed at protecting both human health and economic development. The majority of its measures were implemented in the first half of 2020, most notably between March and May, when a state of emergency was declared in the country. By June, the Government had developed an anti-crisis plan and made amendments to the budget accordingly.

During the fight against COVID-19 in Georgia, the size of role played by the Government has increased. During the state of emergency, for instance, many constitutional freedoms were restricted, in compliance with the norms of the Constitution.

In the first half of 2020 (ending June 30), a total of 800 cases of the novel coronavirus had been reported in Georgia, including 13 deaths. Comparatively speaking, Georgia's results at that point were impressive when compared with most other countries.

However, the government measures taken to sustain economic development and to avoid economic recession and crisis were not so successful. In the first quarter of 2020, real GDP growth rose 1.5% compared to the same period of the previous year, although in March GDP decreased by 2.7%. In the second quarter, GDP decreased by 12.6% (month by month: April (16.6%); May (13.5%); and June (7.7%)). In the following months, a spell of economic recovery was briefly visible only for a disastrous second wave of the pandemic to hit the country in September.

When the second wave struck, government decisions were made amid slightly less uncertainty than during the first wave. After all, Georgia could call upon its own experience as well as the experiences of other countries in fighting against the pandemic in order to make shrewd decisions and to allow appropriate policies to be developed.

As an economic crisis emerged, this increased the importance of fiscal and tax policy in the country. Said economic crisis was caused largely by the forced shutdown of economic activity to combat the spread of the virus. At the same time, consumer demand dropped due to a reduction in liquidity among population, gloomy expectations, and the rearrangement



of priorities and needs. This precipitated a reduction in supply, with businesses ordinarily producing goods and offering services to foreign visitors (especially tourists) stopped altogether. At the same time, the Georgian government came under pressure to provide some sort of financial assistance to the population and businesses, as compensation for the lockdown measures.

With declining tax resources and rapid growth in spending, the Georgian government increased budgetary resources partly through grants from international organizations, but mainly through taking on unprecedented growth in liabilities (domestic and foreign loans). The Georgian government and the healthcare system have been central in the fight against the pandemic. Meanwhile, the role of municipalities and municipal budgets has been less prominent, albeit their involvement in these processes has not been passive, especially with respect to budgetary relations.

The relationships between municipalities and state budgets have been of great significance during the pandemic, with the absolute dependence of municipal budgets on the state budget somewhat limiting decentralization and reducing the independence of municipalities.


Research methodology

Research objectives




The research objectives are to conduct a systematic study of the impact of the pandemic on budget revenues and expenditures of Georgian municipalities in the first half of 2020, to carry out a diagnostic (qualitative and quantitative) evaluation of the impact, to develop recommendations to mitigate negative impacts based on gained experience and lessons learned, and to prevent similar impacts from arising in the future.

Research questions

The research entailed studying the following issues:

 The characteristics of the budget-fiscal situation of the municipalities before the pandemic;



-  The impact of the pandemic on budget revenues and expenditures of municipalities;
-  Testing the sustainability of existing budget federalism during the pandemic (new challenges and alternatives); and
-  Development of recommendations based on the experience of Georgia and other countries to mitigate the negative impact of the pandemic, and the effective implementation of measures during the second wave.

Research methods

The following methods were used in this research: a systematic approach; diagnostic analysis; interviews with experts; analysis of statistical data; empirical observations; and comparative analysis. Due to dynamics of the process, the use of inductive and deductive methods has made it possible to make logical generalizations based on facts and to develop hypotheses about how the pandemic might affect municipal budgets in the future.

A significant part of the research has been based on the study and analysis of pertinent literature, laws and regulations, and official statistics. Due to the scarcity of statistical data, these were complemented by the opinions of respondents and, subsequently, generalizations were drawn up. The COVID-19 pandemic has been periodized for structural and systematic purposes. Systematic, situational, comparative, and hypothetical analysis has been carried out on different chronological periods of the pandemic, while some peculiarities in the allocated periods are revealed in terms of budgetary relations accordingly.

Macroeconomic factors impacting upon the budgetary system of Georgia

The budgetary system of Georgia includes the budgets of the State, autonomous republics, and municipalities. It entails the mobilization of financial resources yielded from economic activity and their redistribution to fuel socio-economic development. On the one hand, budgets are affected by the systemic inter-budgetary relations and, on the other hand, they are impacted by the socio-economic environment. Accordingly, the budget of a municipality is influenced by budgets at higher levels (i.e. state and autonomous republics), by the local



environment with respect to mobilization of own revenues, and by the socio-economic situation in both the municipality and in the country as a whole.

Since the majority of Georgia's municipalities remained classified as so called "green areas" in the first half of 2020, in order to study the impact of the COVID-19 pandemic on municipal budgets, we must first study the impact of the pandemic on the state budget (since the state budget affects all local budgets). Thereafter, we need to study the municipalities in which the novel coronavirus was detected. Accordingly, this study first analyzes the factors affecting the state budget and then examines the budgets of municipalities that were directly affected by the restrictions related to the pandemic. However, to determine the scale of the impact, the data for the first quarter of 2020 are compared with the data for the corresponding period of 2019.

Preconditions and periodization

The "COVID-19 pandemic period" is already commonly referred to everyday, although only the date of its beginning is known; its end is of course yet unknown. On 31 December 2019, after the first case was reported in Wuhan City, China, it became known that a novel coronavirus (SARS-CoV-2) had emerged. The speed and scale of its spread across the world would soon become record-breaking. The World Health Organization (WHO) declared a "Public Health Emergency of International Concern" on 30 January 2020, and announced a pandemic on 11 March 2020.

At the time of preparing this research report, the pandemic was commonly being divided into first and second waves. The latter (second wave) has been observed since mid-September 2020 in the majority of countries. Overall, considering that the vast majority of countries have adopted protectionist policies to fight the pandemic, corresponding processes have been developed in closed systems and taken on country-specific characteristics.

In Georgia, we can distinguish the following three periods related to the pandemic: before the pandemic; the first wave of the pandemic; and the second wave of the pandemic. This corresponds more or less with the timelines of the World Health Organization: the period before the pandemic (31 December 2019 – 10 March 2020); the period of the first wave of the pandemic (10 March 2020 – 11 September 2020); and the period of the second wave of the pandemic (from 11 September 2020 onwards).

The officially recognized stages of pandemic control in Georgia during the first wave were as follows: "containment" of the virus's spread from 31 December 2019 to 26 February



2020; “slowing down” the virus’s spread from 26 February to 21 March 2020; “managing” the virus’s spread from 21 March to 22 May 2020 (“state of emergency”); and gradual mitigation and adaptation from 17 April to 22 May 2020.¹ According to the same criteria, within the first wave, a further fifth stage could be distinguished, namely the adoption of an anti-crisis plan and budget changes, which covers the period from 22 May to 24 June 2020.

Pandemic and budget calendar

The budget calendar in Georgia is established by law. The chronological contrast between the stages of the pandemic’s spread in Georgia and the fight against it, and the established budget calendar will form an important basis for further systematization of materials, for their analysis, as well as for defining the peculiarities of each chronologically separate stage and the historical lessons to be learned therefrom.

By the time of the first dissemination of information about the novel coronavirus (31 December 2019), the budgets of the state autonomous republics and all municipalities for 2020 has already been approved in Georgia².

The pandemic did not hinder the implementation of monthly, quarterly, and annual reporting of the budget envisaged by the budget calendar at all levels, from the relevant executive branch to relevant legislature. From a formal point of view, it also did not affect the start of the draft budget preparation process in March 2020 for the 2021 fiscal year and the observance of the budget calendar as defined by the legislation.

During the pandemic, a significant threat to people has instigated the changes in economic, social, and cultural policies pursued by governments, and this includes new policies when it comes to budget spending and closing down the economy.

Georgian legislation allows for amendments to be made to annual budgets as needed. This power was exercised by the Georgian government after the end of the state of emergency, as changes and additions were made to the approved state budget for 2020 on 24 June 2020. Furthermore, in June-August 2020, changes were made to the budgets of autonomous republics and municipalities.

¹ Report on the measures taken by the Government of Georgia against COVID-19, 2020, Tbilisi. <https://stopcov.gov.ge/Content/files/Government--report.pdf>

² The research does not analyze data from the occupied territories of Georgia.



Situational analysis (January-March 2020)

On 1 January 2021, all budgets included in the budgetary system of Georgia³ were approved in accordance with the legislation and their implementation subsequently began. In the first quarter of 2020, the budget timeframes stayed in line with the budgets determined for that year. At this time, reports about the pandemic began to emerge from abroad, indicating the probability of risks, but this did not yet affect the rhythm of social and economic life in the country until mid-to-late-March.

Relevant measures were taken by the authorities during this period to address the anticipated risks. On 20 January 2020, Government Decree No. 164 was issued “On the Approval of Measures to Prevent the Possible Spread of the Novel Coronavirus in Georgia and the Emergency Response Plan for the Cases of Novel Coronavirus Disease.”⁴ The decree later became an important legal platform for government action, and it had been the subject of 35 amendments by June, and a total of 52 amendments by 22 November 2020.⁵

During the same period, the Inter-Agency Coordination Council was established, commonly referred to as the anti-crisis management center. Preparations and actions against the impending threat were discussed in a centralized manner at the level of central government agencies and organizations. The only norm in this process with regard to local self-government bodies was the Government Decree №546 of 17 March 2020, which responded to a request of the municipalities to take appropriate measures to restrict the transfer of passengers by M₂ category buses within their administrative boundaries from 18 March 2020.⁶

Government Decree №164 was initially preventive. It set out a plan for future action so that operational plans for state agencies (with accurate financial calculations) were to be prepared by March 1. However, the funding determined by the decree should have been allocated within the competence of its own appropriations, and/or resources “obtained” and allocated by the Ministry of Finance, including resources from the Government Reserve Fund.⁷

On 26 February 2020, the first case of the novel coronavirus was registered in Georgia. The health of the population immediately became a matter of serious concern. Nevertheless, the Georgian government acted in accordance with the scenarios defined by legislation, and continued to do so even upon the WHO’s declaration of a pandemic on March 11 2020. The legal framework accommodated for dangerous epidemics and pandemics defined

³ The research does not analyze the data of the occupied territories of Georgia.

⁴ <https://matsne.gov.ge/document/view/4821121?publication=31>

⁵ Ibid.

⁶ <https://matsne.gov.ge/ka/document/view/4825724?publication=0>

⁷ <https://matsne.gov.ge/document/view/4821121?publication=31>



by the Law of Georgia on Public Health, with the National Center for Disease Control and Public Health stipulated to take the leading role in such circumstances. The relevant system is presented in the state budget law every year and so it remained for the year of 2020.

Prior to the first reported case in Georgia, the Ministry of Internally Displaced Persons from the Occupied Territories, Labor, Health and Social Affairs of Georgia (MoIDPLH-SA) had already developed the first methodological recommendation and protocol. The Government did not suffer from any serious financial and/or budgetary delays in January-February to prevent it from taking relevant action.⁸ Moreover, even after the declaration of the state of emergency on 21 March 2020, the Government did not take the opportunity to adopt the emergency budget provided for by the Law of Georgia “Budget Code of Georgia” (Article 32).⁹

The average growth of the economy (real GDP) equaled 1.5% in the first quarter of 2020. In more detail, the real GDP growth rates classified by month were: +5.1% in January; +2.2% in February; and -2.7% in March (all compared to the corresponding month of 2019).¹⁰ At the end of the first quarter, the Ministry of Finance revised its initial forecast of 5% economic growth for 2020, to a 4% reduction.¹¹

In March 2020, compared to December 2019, the GEL exchange rate against the USD depreciated by 14.5%, compared to the same period of the previous year. Meanwhile, an increase in prices was observed, while there were decreases in exports (by 2.7%), the number of foreign visitors (by 17.6%), and tourism revenues (by 26.1%, or US\$150.7 million). In the same period, remittances increased marginally (0.1%).¹² Despite the fact that the novel coronavirus prompted adjustments to demand and supply in late March, mainly due to the declaration of a state of emergency (March 21), and the shrinking of the economy reported in

⁸ Existence of financial resources was the prerequisite for not adopting emergency budget. It was obvious from the beginning that it was not the best decision. This is also indicated in the report of the State Audit Office “On the Government Report on the Process of Performance of the State Budget of Georgia for 2020”. The report states: during the coronavirus in 2020, the state faced the need to finance measures to respond to the pandemic and negative economic effects caused by it. Prior to the amendment to the budget law, these measures were mainly funded by changes in the expenditures made in appropriations of spending agencies. In addition, some programs/sub-programs planned by the budget law were delayed, which to some extent was reflected in low rates of utilization of appropriations allocated to them. Due to the above, the shortcomings identified by the State Audit Office in the budget performance process are in some cases caused by objective circumstances. However, the conducted analysis revealed cases related to budget planning and performance, which are caused by inefficient management of budget resources”. http://parliament.ge/ge/ajax/downloadFile/142733/1-14376_auditi, pp.13.

⁹ <https://matsne.gov.ge/ka/document/view/91006?publication=46>

¹⁰ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039> .

¹¹ Ibid.

¹² Ibid.



March, the first quarter as a whole ended without economic recession. In spite of the above-mentioned significant changes to the basic budget forecast for 2020, no changes were applied to the budget either.

Situation regarding state and consolidated budget for the first quarter of 2020

In the first quarter of 2020¹³, despite the negative trends in the Georgian economy and the sharply worsening forecasts with regard to economic growth, revenues were to be mobilized at state and consolidated budget levels. The figures were much more favorable compared to the corresponding period of 2019.

Relative indicators of actual performance are determined by comparing these with the data for the quarterly breakdown of budget receivables, appropriations, and balance changes (hereinafter, budget breakdown). The budget breakdown (see Table 1) is an important tool for measuring budget performance and for budget reporting. In the breakdown of Georgia's state budget for the year of 2020, there is noticeably unequal distribution by quarter and by month: the bulk of receivables were mobilized in the second half of the year, and particularly in the months of the fourth quarter. There is also a foredated adjustment of forecasts ("forecasting" of the past period), which improves the performance indicators for the current period, because the report presents an increased sum total. For example, in the current budget breakdown for 2020, the initial VAT breakdown in the first quarter was changed to the level of the VAT rate actually mobilized in the first quarter. This contributes to a widespread practice of unequal spending, which is associated with many problems such as: non-utilization of budget funds; "budget accumulation" in the form of balances; hastily completed work at the end of the year; and pressure on the GEL exchange rate with increased monetary supply.

Order №428¹⁴ of the Minister of Finance of Georgia of 31 December 2019 was amended several times in the process of performing the state budget for 2020, specifically through the following orders of the Minister of Finance of Georgia: №80¹⁵ of 20 March 2020; №84¹⁶ of 25 March; and №120¹⁷ of 25 May. On 24 November, another change was posted on the

¹³ 3-month review of the performance of the state budget of Georgia for 2020, Ministry of Finance of Georgia - <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>

¹⁴ Order №428 of the Ministry of Finance of Georgia of December 31, 2019 "On the Approval of Consolidated Budget Revenues of Georgia 2020, Decrease in Non-Financial Assets and Decrease in Financial Assets and Approval of the Quarterly Breakdown of the State Budget of Georgia for 2020" - Quarterly Breakdown of Changes https://mof.ge/images/File/2020%E2%80%93biujeti/ganwera/gantsera_saitistvis.pdf

¹⁵ <https://mof.ge/images/File/2020%E2%80%93biujeti/21-04-2020/80%20ganwera.pdf>

¹⁶ <https://mof.ge/images/File/2020%E2%80%93biujeti/21-04-2020/84%20gantwera.pdf>

¹⁷ <https://mof.ge/images/File/2020%E2%80%93biujeti/25-05-2020/120.pdf>



website of the Ministry of Finance of Georgia, based on the previously corrected budget¹⁸. Such frequency of changes in the budget breakdown confirms that in the first half of 2020, including the first quarter, the ongoing changes were enacted normatively without changes and additions being made to the state budget law. Given that the budget breakdown was changed several times during the quarter, the plan appeared to be more post-factum than pre-determined however.

**Table 1. Receivables and payables (Georgia) for January-March 2020
(in thousands of GEL)¹⁹**

Indicators	First Quarter Plan (corrected)	Performance	Quarterly performance %
Receivables	3,857,311.6	3,736,504.9	96.9%
Value of Receivables which are Revenues	2,817,082.5	2,839,478.2	100.7%
Payables	3,507,602.3	3,462,783.7	98.7%
Value of Payables which are Costs	2,754,029.7	2,750,152.4	99.8%

Consolidation for 2020 (defined by order #428 of December 31, 2019 and corrected by order #84 of March 25, 2020 of the Minister of Finance of Georgia) and the receivables plan (determined by the first quarter plan of 2020 and defined by quarterly breakdown of the state budget) was performed to a level of 106.9%, while the payment of state budget payables was equal to 93.6% of what was planned. According to the adjusted breakdown (Table 1), these figures are 96% and 98.7%. To avoid the margin of error caused by this correction when compared with the corresponding period of 2019, only absolute and not relative data shall be compared.

¹⁸ <https://mof.ge/images/File/2020%E2%80%93biujeti/06-07-2020/danarti-06-07.pdf> The date of adoption is not specified.

¹⁹ Compiled by the State Treasury of Georgia, according to the data of the Budget Office of the Parliament of Georgia, in accordance with the schedule of 25 March 2020.



The amount of receivables and payables for the first quarter of 2020 was significantly higher than for the same period in 2019: receivables - 889.7 million GEL (+31.3%); and payables - 644.5 million GEL (+22.9%). Revenues and cost indicators were also greater than in the corresponding period of the previous year: revenues were up by 259.5 million GEL (10.1%) and costs were up by 768.3 million GEL (38.8%).²⁰

During January-March 2020, the state budget balance increased by 273.7 million GEL and the total accumulated budget amounted to 717.4 million GEL²¹. The total balance of the state budget in January-March 2020 increased. A positive operating balance (89.3 million GEL) was obtained, despite a negative balance being forecast for the first quarter (plan – 313.6 million GEL). The total balance of the state budget formed as a result of the change in the operating balance and non-financial assets was in deficit (-280.3 million GEL), but this was significantly better than the forecasted negative result (plan – 726.6 million GEL).²² In 2019, the operating balance of the state budget for the same period amounted to 347.8 million GEL, while the total balance was 52.5 million GEL.²³

Thus, according to the results for the first quarter of 2020, the condition of the state budget was positive, and the impact of the pandemic did not appear to have yet affected it. As for the budget deficit, this stemmed from trends of the previous period, and had thus been planned for. However, the deficit was lower than expected.

Given that the first quarter of 2020 coincided with the first and second stages of government action (the first stage being “containment” of the virus’s spread and the second stage being the “slowing down” of the virus’s spread), as well as the beginning of the third stage (“managing” the virus spread and the “state of emergency”), then only the last 10 days of March were significantly affected by the pandemic. Therefore, data for the month of March will be discussed separately (see Table 2). As can be seen from the table, even though the total balance is also negative here, it had the smallest share in March. The total operating balance in the first quarter was 280.3 million GEL²⁴, with these figures sitting at 212.5 million GEL²⁵ for January-February, and then 67.8 million GEL for March.

²⁰ http://pbo.parliament.ge/media/k2/attachments/saxelmwifo_biujetis_shesruleba_3_tve_2020.pdf

²¹ [file:///C:/Users/User/Downloads/1.%E1%83%90%E1%83%9C%E1%83%92%E1%83%90%E1%83%A0%E1%83%98%E1%83%A8%E1%83%98%E1%83%A1%20%E1%83%A2%E1%83%94%E1%83%A5%E1%83%A1%E1%83%A2%E1%83%98%20\(5\).pdf](file:///C:/Users/User/Downloads/1.%E1%83%90%E1%83%9C%E1%83%92%E1%83%90%E1%83%A0%E1%83%98%E1%83%A8%E1%83%98%E1%83%A1%20%E1%83%A2%E1%83%94%E1%83%A5%E1%83%A1%E1%83%A2%E1%83%98%20(5).pdf), pp.4

²² www.mof.gov.ge

²³ http://pbo.parliament.ge/media/k2/attachments/saxelmwifo_biujetis_shesruleba_3_tve_2020.pdf

²⁴ http://pbo.parliament.ge/media/k2/attachments/saxelmwifo_biujetis_shesruleba_3_tve_2020.pdf, pp.5.

²⁵ http://pbo.parliament.ge/media/k2/attachments/saxelmwifo_biujeti_ianvar-tebervali.pdf, pp.11



**Table 2. Receivables and payables (Georgia) for the first quarter of 2020
(in thousands of GEL)²⁶ and share of March therein**

Indicators	Performance for the first quarter	Performance for January -February	Performance for March	Share of March in quarterly performance
Receivables	3,736,504.9	2,198,540.6	1,537,964.3	41.1%
Value of Receivables which are Revenues	2,839,478.2	1,701,817.0	1,137,661.2	40.0%
Payables	3,462,783.7	2,082,500.0	1,380,283.7	39.9%
Value of Payables which are Costs	2,750,152.4	1,721,300.0	1,028,852.4	37.4%

An operating balance in the amount of 20.2 million GEL was most likely conditioned by the fact that, in the first quarter, costs directly incurred due to the COVID-19 pandemic came in late March, and were not included (nor could they have been) in the 2020 budget.

The declaration of a state of emergency for the entire territory of Georgia in March 2020 was followed by significant costs incurred in the purchase of the following items: individual protective equipment; defibrillators; respirators; patient observation monitors; contactless electric thermometers; and liquid medical oxygen. In addition, costs were incurred in the setting up of quarantine zones and maintaining retail sales prices for primary food products in the face of exchange rate volatility. Accommodation in hotels, transportation, food, security, and costs related to the creation of appropriate conditions during the quarantine period also had to be financed in the course of compulsory quarantine for Georgian citizens re-entering the country from abroad. Funding was also provided to establish a quadrilingual website (<https://stopcov.ge/>), as well as to purchase 5,000 dispensers and 80 tons of disinfectant solution.²⁷ The quarterly plan for payables from the state budget of 2020 (35,300,619.52 GEL) was fulfilled to an extent of 37.6% (13,288,802.56 GEL) in the first quarter.²⁸ Across the board, entities spent considerably more than in the corresponding period of 2019.²⁹

²⁶ Compiled according to the data of the Treasury Service, Budget Office of the Parliament of Georgia, as of 25 March 2020.

²⁷ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>

²⁸ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>, pp.270

²⁹ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>, pp.102-130



Funding of municipalities in the first quarter of 2020

The volume of spending in the first quarter of 2020 from the funds allocated by the state budget for the first quarter of 2020 for the implementation of regional projects was equal to 37,000 thousand GEL, while cash expenditure amounted to 35,086.50 thousand GEL (see Table 3), and 305.0 and 44.3 thousand GEL from the High Mountainous Settlements Development Fund, respectively.³⁰ The three-month appropriation plan for the budgets of autonomous republics and local self-governing units (code: 56.04) from “transfers to local self-governing units”³¹ was fulfilled to the extent of 94.1% (56,126,613.0 GEL instead of 59,624,900.0 GEL).³²

Table 3. Funds transferred to local self-government from the fund of projects to be implemented in the regions of Georgia (in thousands of GEL)³³

		Whole of 2020 (planned)	First quarter of 2020 (actual)
1	Kakheti	48,129.3	4,571.5
2	Imereti	80,389.0	10,241.6
3	Samegrelo-Zemo Svaneti	58,723.4	5,090.2
4	Shida Kartli	35,032.7	3,028.4
5	Kvemo Kartli	46,952.1	4,732.9
6	Guria	22,813.2	2,933.3
7	Samtskhe-Javakheti	37,385.4	559.9
8	Mtskheta-Mtianeti	28,254.7	3,307.4
9	Racha-Lechkhumi-Kvemo-Svaneti	19,961.0	621.4
	Total	377,640.8	35,086.5

³⁰ http://pbo.parliament.ge/media/k2/attachments/saxelmwifo_biujetis_shesruleba_3_tve_2020.pdf pp.9-10

³¹ Operative information of Treasury Service on changes in receivables, payables, and balance of the state budget of Georgia for 2020

³² Ibid,

³³ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>



The amount allocated under the Rural Support Program amounted to 40,392.0 thousand GEL, of which 434.3 thousand GEL was transferred during the research period.³⁴

The annual plan for financial assistance to be transferred from the 2020 state budget to budgets of autonomous republics and local self-governing units of Georgia was set at 519,340.2 thousand GEL.

The special transfer provided in the 2020 state budget of Georgia for the Autonomous Republic of Abkhazia amounted to 8,000.0 thousand GEL, of which 2,000.0 thousand GEL was transferred as of three months. The amount allocated from the High Mountainous Settlements Development Fund of Georgia amounted to 8,495.0 thousand GEL.³⁵

Table 4. Financial assistance given to the budgets of territorial units by the end of Q1 of 2020 (in thousands of GEL)³⁶

Year	Total transfer		Targeted transfer		Special transfer		Capital transfer	
	Planned (2020)	Actual (Q1 2020)	Planned (2020)	Actual (Q1 2020)	Planned (2020)	Actual (Q1 2020)	Planned (2020)	Actual (Q1 2020)
2019	379,413.4	30,222.8	11,800	2,960.0	98,498.4	21,388.0	269,138.9	5,889.8
2020	519,340.2	56,906.1	16,400.0	3,000.0	123,540.0	18,772.6	379,400.2	35,133.5

Due to the economic downturn in March and the state of emergency being declared due to the pandemic, the Government decided to make adjustments to its initial plans for the first quarter. As a result, the planned indicators for receivables and revenues increased from 3,078,077.0 and 3,019,077.0 thousand GEL³⁷ to 3,300,483.3 and 3,222,105.7 thousand GEL, respectively³⁸. The Government's optimistic approach may have been based on the fact that all budget indicators for the first quarter of 2020 exceeded the corresponding period for 2019. Looking at performance for the first three months of 2020, the funds transferred to the local self-governments from the fund of projects to be implemented in the regions of Georgia were 1.9 times higher, and the financial assistance given to the budgets of territorial units

³⁴ Ibid.

³⁵ Ibid

³⁶ Ibid, pp.40; See similar data for 2019 see: <https://mof.ge/5249>

³⁷ 31.12.2019 budgeting - https://mof.ge/images/File/2020%E2%80%9393biujeti/ganwera/gantsera_saitistvis.pdf

³⁸ 25.03. 2020 budgeting - <https://mof.ge/images/File/2020%E2%80%9393biujeti/21-04-2020/84%20gantwera.pdf>



was six times higher, compared to the corresponding period of 2019. The Government's optimistic approach alone would not be sufficient of itself to explain this phenomenon however, particularly when we see that the indicators for the second quarter are significantly reduced. In particular, the planned figures of receivables and revenues were re-

duced, respectively, from 3,639,734.0 and 3,540,534.0 thousand GEL³⁹ to 2,845,255.1 and 2,778,490.8 thousand GEL⁴⁰. Meanwhile, the performance forecast for the second quarter of 2020 was made in the last week of the quarter and it was equal to the performance of the first quarter. The actual performance of revenues and costs for the first quarter of 2020 was 3,233.5 million GEL and 3,040.0 million GEL, respectively, while for the second quarter this was 2,844.6 and 2,968.4 million GEL⁴¹.

In the first quarter of 2020, the revenues of the consolidated budget amounted to 3,233,485.0 thousand GEL (106.6%) instead of the forecasted 3,034,077.0 thousand GEL, while the amount received from taxes amounted to 2,982,873.8 thousand GEL (106.5%), instead of the forecasted 2,801,100.0 thousand GEL. VAT performance was recorded at 108% (planned 1,126,000.0 thousand GEL versus actual 1,216,445.6 thousand GEL). Elsewhere, the deficit of the consolidated state budget of 2020 was 0.6% of GDP, instead of the planned 2.4%.

Thus, budget revenues exceeded expectation in this period. There was a lag in costs, although this did not affect the budgets of municipalities. Budget revenues at the state and consolidate levels were generally unaffected by the novel coronavirus during this period.

Anti-crisis state budget

The amendments made on 24 June 2020 to the Law of Georgia on the State Budget for 2020 of December 10, 2019 were precipitated by a whole range of reasons. The first of these was the deepening crisis in the economy and the changes in the macroeconomic indicators and their forecasts due to the unforeseen crisis. The real GDP growth was determined at 4.0% instead of the forecasted 5% (5.1% in 2019), while nominal GDP stood at 50.3 million GEL instead of 53.1 million GEL (50.0 million GEL in 2019), and the current account deficit rose to 8.8% instead of 3.5% (5.1% in 2019). Accordingly, grim reality of the second quarter was reflected in the corrections made to the budget for 2020 (see Table 5).

³⁹ 31.12.2019 budgeting - https://mof.ge/images/File/2020%E2%80%93biujeti/ganwera/gantsera_saitistvis.pdf

⁴⁰ 25.03.2020 budgeting - <https://mof.ge/images/File/2020%E2%80%93biujeti/21-04-2020/84%20gantwera.pdf>

⁴¹ https://mof.ge/finansebis_statistika_naerti_biujeti



Table 5. Receivables and payables (Georgia) for January-June 2020
(in thousands of GEL)⁴²

Budget indicators	Six-month plan		Six-month performance	Corrected versus planned (%)
	Forecast	Corrected		
Receivables ⁴³	7,661,401.9	3,857,311.6	8,010,173.4	96.9%
Value of Revenues among Receivables	5,009,223.2	2,817,082.5	5,087,527.4	100.7%
Payables ⁴⁴	3,698,702.0	3,507,602.3	3,462,783.7	98.7%
Value of Costs among Payables	7,422,121.6	2,754,029.7	6,897,114,705.1	99.8%

The approved budget costs were reduced by 600 million GEL. This included reduced costs from March (including administrative expenses, business trips, and fuel), as well as a further reduction in capital costs (in tourism and other less promising sectors).⁴⁵

The need for budget correction stemmed from a need to maintain budget order: the increase in the budget costs for healthcare, treatments, diagnoses, and quarantine measures against COVID-19 was so significant, that more than a reshuffle of budget funds would be required. During the state of emergency, the Georgian government argued that under the Organic Law of Georgia on Economic Freedom, due to the declaration of the state of emergency, it was allowed to operate beyond the fiscal parameters set by law in order to ensure uninterrupted financing of the abovementioned essential measures.⁴⁶ It was around this time

⁴² Compiled according to the data of the Treasury Service, Budget Office of the Parliament of Georgia, as of 25 March 2020. Subsequently, the result indicators change by the corrected breakdown, including that receivable indicator is already less than 100%.

⁴³ <https://www.mof.ge/4536>

⁴⁴ <https://www.mof.ge/images/File/2020%E2%80%93biujeti/06-07-2020/danarti-06-07.pdf>

⁴⁵ <https://info.parliament.ge/file/1/BillReviewContent/251231>

⁴⁶ Explanatory card on the draft law of Georgia on amendments to the law of Georgia “On the State Budget of Georgia for 2020” -<https://info.parliament.ge/file/1/BillReviewContent/251231>, pp.1; Expenditures outside the state of emergency, before and after, cannot be explained by what is said. The government explains the latter as follows:

“It is noteworthy that an important determinant of the effectiveness of planned measures at the crisis stage is the existing framework for public financial management and the flexibility of budget system. The Organic Law of Georgia on Economic Freedom provides for specific regulations related to fiscal limits in the event of the state of emergency. The mechanisms for clarifying the annual budget law facilitated redistribution of appropriations to mobilize necessary resources, resulting in a smooth budget process before the amendment to the state budget law. “Taking into account all of the above, the agenda is to apply changes to the state budget for 2020 and reflect both the updated macroeconomic and fiscal parameters in it, as well as appropriations necessary for further financing of measures defined by the anti-crisis plan.”pp.3. However, this explanation rais-



that the anti-crisis plan was developed by the Government. Financing the anti-crisis plan measures to alleviate the negative effects of the pandemic was crucial when correcting the budget. The cost of the anti-crisis plan of the Government of Georgia for social protection, healthcare, and business support was set at 3.4 billion GEL, which was reflected in the newly-amended budget.⁴⁷

The budget corrections were made to overcome the trend of falling behind in state budget payments (445 million GEL) in the first half of the year. In the first and second quarters, receivables exceeded expectations, while payables fell behind. Receivables in the first quarter exceeded the planned amount by 1.5% (54 million GEL), and in the second quarter by 7.4% (294.7 million GEL), while payables in the same period fell behind the quarterly planned amounts by 1.3% (44.8 million GEL) and 10.4% (400.2 million GEL) respectively.⁴⁸

This marked a continuation of the existing stimulus-oriented budget policy. Initially, the state budget for 2020 was optimistic in the light of the positive budget and economic results of 2019. However, payables lagged behind receivables in reality. Nevertheless, the imbalance was eventually maintained and legalized, with approved receivables of 14.6 billion GEL and payables of 14.4 billion GEL. The forecasts were thus increased to 18.4 billion GEL (26.6%) for receivables and to 15.9 billion GEL (10.3%) for payables. Therefore, plans were put in place to accumulate a budget balance of 2.5 billion GEL by the end of 2020⁴⁹.

Despite the budget stimulus, the economy continued to slow down, significantly reducing the tax revenues for the state budget. In particular, the reduction of VAT is noteworthy, which was caused by the declining economic situation (including reduction of imports in the first half of the year), as well as by government decisions, in particular the introduction of a VAT refund mechanism (resulting in a reduction of 600 million GEL). Overall, the VAT forecast decreased by 14.6% (644 million GEL).

es more questions: if everything was going according to the plan, why was there a need to change the forecasts with a back-date? Instead of changing the forecast post-factum, it was necessary to make corrections in parallel with the changes in the budget law, as the change in the normative act is made by the same kind of normative act.

⁴⁷ pp.2.3 <https://info.parliament.ge/file/1/BillReviewContent/251231>

⁴⁸ http://parliament.ge/ge/ajax/downloadFile/142733/1-14376_auditi

⁴⁹ http://parliament.ge/ge/ajax/downloadFile/142733/1-14376_auditi



Table 6. Tax revenues of the state budget for 2020 (million GEL).⁵⁰

Name	Law on State Budget for 2020	Draft amendment to the Law on State Budget 2020	Difference	Change (%)
Income tax	3,415.0	2,990.0	-425.0	-12.4%
Profit tax	970.0	840.0	-130.0	-13.4%
VAT	4,398.0	3,754.0	-644.0	-14.6%
Excise tax	1,400.0	1,325.0	-75.0	-5.4%
Import tax	80.0	70.0	-10.0	-12.5%
Other tax	202.0	0.0	202.0	-100.0%
Tax revenues	10,465.0	8,979.0	-1,486.0	-14.2%

The impact of the pandemic on municipal budgets

Common signs of the pandemic’s impact on municipal budgets were reflected in budget corrections during 2020. In the first half of 2020, the reduction of VAT and property taxes was reflected in revenues of municipal budgets. The reduction of local revenues was mainly compensated by reductions in costs/programs not related to social protection, education, healthcare, and communal infrastructure. However, during this period it became impossible to maintain spending on – cultural, educational, or sports events due to the pandemic. Moreover, office expenses, fuel, business trips, and other costs were eliminated or reduced due to quarantine and remote working. Below, we discuss in detail what led to the correction of municipal budget.

Sharing effect of VAT

The relationships between self-government budgets and the central state budget are determined by the budgetary tax system. The Tax Code of Georgia defines general state taxes and local taxes.⁵¹ Currently, the latter include property (including land) taxes. Meanwhile,

⁵⁰ <https://sao.ge/Uploads/2020/6/83%90.pdf>

⁵¹ <https://matsne.gov.ge/ka/document/view/1043717?publication=169> (Article 6)



the mobilization of resources for municipalities in connection with local taxes is complicated by normative-legislative as well as technical-organizational and administrative issues.

The municipal budgetary system of Georgia was hit by the pandemic, putting it in a vulnerable situation. This was caused in part by the peculiarities of its historical development, the financial and material constraints of the municipalities, as well as the so-called transitional period announced in 2019 in relation to the revenues of municipal budgets.

By 2019, the share of municipalities in the consolidated budget of Georgia (12,907.2 million GEL) was 15% (1,935.7 million GEL), including 900.5 million GEL (7% of the consolidated budget) for Tbilisi and 1,035.2 million GEL (8%) for all other municipalities put together. The share of the autonomous republics was 2% (296.52 million GEL). The population of Georgia in 2019 was 3,723,500, of which the population of Tbilisi made up 1,140,700. The average size of self-government budget revenues per capita in Georgia was 520 GEL (in Tbilisi – 789 GEL, and in other municipalities - 400 GEL). This inequality is even greater among individual municipalities. The reason behind this inequality is the tax base of local governments. Local taxes include property tax and since 2019 they have also included a part of VAT. The influence of each municipality is relatively minor with regard to property. Re-sources, water, and forests have not been transferred into their possession. The issue of land tax remains unresolved for the following two reasons: non-existence of a land code; and the absence of a tax exemption for agricultural land up to 5 hectares (which would allow for differentiated taxes to be imposed according to the given profit indicator).

The share of VAT in the total revenues of municipalities in 2019 amounted to 48.9% (946 million GEL). Of this, 50.04% (473.4 million GEL) of VAT was distributed in Tbilisi, which amounted to 43% of Tbilisi's budget in 2019 (1100.45 million GEL). The share of VAT (472.5 million GEL) in the revenues of all other municipalities put together was 45.65% in total.

In 2020, the projected amount of revenue to be received by each municipality as a result of VAT distribution was limited, compared to the previous year. The maximum growth rate was 25%⁵², however it is unclear what will happen if the volume of VAT mobilization is less than previously determined. The state budget has mechanisms in place for such cases, however municipalities do not.

According to the corrected budget, VAT in the amount of 880.6 million GEL was set to be transferred to the municipalities, distributed according to the percentage set for each municipality. The share of Tbilisi for 2020 was set at 45.34%.

⁵² https://matsne.gov.ge/ka/document/view/4734727?publication=0_189/1962



The current VAT system is designed with the permanent increase of VAT in mind, so when the amount of VAT decreased and inflows for municipalities became unstable, they faced problems due to the instability of the tax inflow. Importantly, VAT showed a tendency to decrease even before the pandemic struck. This dip was later exacerbated and the shortcomings of the existing distribution system were left fully exposed. Delays in VAT supply have put pressure on municipalities to take internal budget loans by government decree, requiring additional time and human resources, as well as incurring transaction costs.

Following correction of the state budget, when it was determined that the budgets of self-governments could not receive their planned revenues due to the VAT reduction, the municipal budgets were also corrected. All municipalities corrected their budgets within one month of receiving the anti-crisis budget. Despite this reduction, educational, social, and infrastructural projects were protected. However, there is no guarantee that VAT revenues will not decrease further in the future, leaving a high risk that this reduction will eventually affect social spending. Unfortunately, the designed mechanism does not take into account tax fluctuations and is designed only with growth in mind. Moreover, the risks with respect to VAT reduction were not considered at all in the study of financial risks attached to the draft budget.

Specifics of municipal budgets

After budget corrections, revenues and costs of the state budget performed according to the new plan. The budget data for the first and second quarters of 2020 were formally “corrected” and “backdated.” This step corrected the “failure” of tax revenues at the macro level, but it did not affect the budgets of municipalities, because the “failure” of the second quarter hampered the revenues of municipal budgets (especially from VAT and property tax). This led to massive changes in budgets, as the absorption of payments fell behind in the first two quarters, at both central and municipal levels. This lag has been corrected by the budget changes. In general, it should be noted that the stimulus budget model chosen by the Georgian government is based on the concept of “pouring” money into the economy and, therefore, the budget balance is strengthened at the expense of grants and loans.



**Table 7. Consolidated budget revenues in 2019-2020⁵³
(million GEL)**

Year	I	II	III	IV	V	VI
2019	1123.6	783.7	1051.0	969.3	1023.5	1215.8
2020	1049.7	913.9	1269.9	925.6	880.4	1038.6

Restoration of the budget balance in 2020 following the reduction of tax revenues in the budgets of autonomous republics and municipalities (up to 310.0 million GEL) took place, although it was impossible to fully balance the budget by reducing costs. Hence, transfers increased. In particular, transfers to the autonomous republics and local self-governments increased from 131.0 million GEL to 166.0 million GEL. The fund of the projects to be implemented in regions of Georgia was set at 400.0 56 million GEL and the fund for the development of high mountainous settlements was set at 20.0 million GEL. In the first quarter of 2020, the Government of Georgia approved the “Integrated Development Pilot Program for Regions for 2020-2022,” which envisages the implementation of targeted initiatives worth 64 million EUR in the regions of Kakheti, Imereti, Guria, and Racha-Lechkhumi-Kvemo Svaneti to strengthen the economic, cultural, and social role and functions of regional centers therein.⁵⁴

Transfers to autonomous republics and local self-governments (Code 56.04) from taxes of general state importance were financed to the tune of 56,126.6 thousand GEL (94.1%) instead of the 59,624.9 thousand GEL provided by the plan for the first quarter of 2020. Of this amount, transfers to the autonomous republics are 100.0% (planned: 2,000.0 thousand GEL; actual: 2,000.0 thousand GEL), and transfers to local self-governments by 93.9% (planned: 57,624.9 thousand GEL; actual: 54,126.6 thousand GEL). There were no appropriations from the fund of projects to be implemented in the regions of Georgia (Code 56.07) and the fund for the development of high mountainous settlements (Code 56.08), from which it was planned to allocate funding of 39,605.8 and 195.0 thousand GEL, respectively. All state trustee institutions received less funding than planned.⁵⁵

In the first quarter of 2020, the decrees № 2630 of December 18, 2019, № 2750 of December 31, and № 325 of 2020 of the Government of Georgia approved transfers to local self-governments in the amount of 37.0 million GEL, with a cash execution of 35.086 million GEL in the first quarter.

⁵³ https://www.mof.ge/finansebis_statistika_naerti_biujeti

⁵⁴ http://parliament.ge/ge/ajax/downloadFile/137337/%E1%83%A1%E1%83%90%E1%83%9B%E1%83%97%E1%83%90%E1%83%95%E1%83%A0%E1%83%9D%E1%83%91%E1%83%9D_%E1%83%9E%E1%83%A0%E1%83%9D%E1%83%92%E1%83%A0%E1%83%90%E1%83%9B%E1%83%98%E1%83%A1_%E1%83%90%E1%83%9C%E1%83%92%E1%83%90%E1%83%A0%E1%83%98%E1%83%A8%E1%83%98_6967 pp.80

⁵⁵ <http://parliament.ge/ge/ajax/downloadFile/136491/1-6039>



The impact of the quarantine regime on municipal budgets

Strict measures against the pandemic were implemented from 21 March to 22 May 2020 during which time a state of emergency was declared, with a curfew in effect from 31 March to 23 May (from 21:00 to 06:00). The first wave of the pandemic affected Tbilisi, Kvemo Kartli, Adjara, Racha-Lechkhumi-Kvemo Svaneti, Imereti, and Shida Kartli, with other parts of the country marked as “green areas” in the first half of 2020. With the emergence of clusters of the virus’s spread, strict targeted quarantine regimes were imposed in certain municipalities (March 23-May 18 in Marneuli and Bolnisi municipalities; April 10-28 in Lentekhi municipality; April 12 - May 8 in the settlements of Kobuleti municipality (Gvara, Mukhaestate, Leghva, Tskavroka); April 13-28 in the Khidiskuri administrative unit of Khashuri municipality). Moreover, on April 15, it was forbidden to enter and leave the municipalities of Tbilisi, Rustavi, Kutaisi, and Batumi. Restrictions on movement were lifted on May 5 in Batumi and Kutaisi, on May 11 in Tbilisi, and on May 14 in Rustavi. In the period of April 26 - June 4, the quarantine regime was also put into force in Tetrtskaro municipality.

Strict quarantine affected a total of 10 municipalities (Marneuli, Bolnisi, Lentekhi, Kobuleti, Khashuri, Tbilisi, Rustavi, Kutaisi, Batumi, and Tetrtskaro), directly affecting more than half of the population of Georgia (52%).⁵⁶

Therefore, the general impact of the pandemic was greatest in the above-mentioned municipalities. Below, we will consider the examples of four municipalities to see how the crisis affected their budgetary systems.

Tbilisi

Tbilisi municipality’s budget for 2020 was approved on 27 December 2019⁵⁷. The budget of Tbilisi, as well as the budgets of other municipalities of Georgia, significantly depends on state budget grants and taxes (since 2019, particularly on VAT in addition to the property). In line with the state of emergency and the anti-crisis program, the revenue base of the Tbilisi budget has since changed. This was critical with the reduction of taxes and grants as a result of the 24 June 2020 correction of the state budget (when VAT forecasts were changed and when grants for Tbilisi was reduced). On July 14, the Tbilisi Municipality Assembly adopted a resolution amending decree №51-104 of Tbilisi Municipality Assembly of December 27,

⁵⁶ <https://www.geostat.ge/ka/modules/categories/316/mosakhleoba-da-demografia>

⁵⁷ <https://matsne.gov.ge/ka/document/view/4757863>



2019 approving the 2020 budget of the Tbilisi municipality.⁵⁸ In the corrected budget, the revenue plan was reduced by 15% compared to the original budget, while taxes fell by 14% (including VAT - 15%; property tax - 12%) and grants dropped by 35% (see Table 8)⁵⁹.

Table 8. Tbilisi budget for 2020 (thousand GEL) (initial and corrected)

	Approved 2020	Corrected 2020
Revenues	833 437.4	980 969.9
Taxes	591 439.0	687 009.5
VAT	411 439.0	482 009.5
Property tax	180 000.0	205 000.0
Grants	58 963.0	90 963.0
Other revenues	183 035.4	202 997.4
Costs	818 293.0	727 165.5
Operating balance	15 144.0	253 804.4
Total balance	-203 837.1	17 392.9

In the course of budget corrections, Tbilisi's budget was reduced by 147,532.5 thousand GEL, out of which 127,570.5 thousand GEL (or 86.5%), was attributable to the reduction of VAT, property tax, and grants (70,570,5; 25,000,0; 32,000,0 thousand GEL, respectively).

The changes applied were not however sufficient to balance the six-month budget. Tbilisi has suffered considerable damage from the pandemic. The city's budget for 2020 was approved on December 31, 2019, with a revenue forecast of 980,969,900.0 GEL⁶⁰, out of which up to 60% was envisioned from transfers, grants, and VAT received from the state budget. According to the actual results of the first six months of 2020, the capital transfer performance was only 31% of the planned amount, while VAT revenue only reached 76.0% of the planned amount. Overall, the revenue plan for this period was fulfilled to the extent of 74.9% (408,612,289 GEL instead of 545,735,800 GEL), with a shortfall of 137,123,511 GEL. The amounts not received from VAT and transfers, respectively were 59,010,415 and

⁵⁸ <https://matsne.gov.ge/ka/document/view/4924331?publication=0>

⁵⁹ <https://matsne.gov.ge/ka/document/view/4924331?publication=0>

⁶⁰ <https://matsne.gov.ge/ka/document/view/4757863?publication=0>



23,821,949, amounted to 82,832,164 GEL, 60% of the volume required for the performance of the planned indicator. In addition, only 83.1% of planned property tax was recorded over this period. This led to costs being cut, similar to other municipalities. In particular, performance in the field of recreation, culture, and sports was lowest (45% compared to planned amount). Tbilisi's budget accounts for 79% with revenues and 82% with grants. Pertinently, tax mobilization has been affected by macroeconomic policy changes. In particular, in the scope of anti-crisis measures, property taxes were mainly postponed until November 1 (approximately 171 million GEL), while in the tourism sector, property taxes were exempted until the end of the year. The mechanism of an automatic VAT refund was introduced in the country, leaving a 600 million GEL shortfall across the country. The amount of VAT was also affected by the decrease in imports, which reduced the amount of VAT received at the border.

The reduction of other revenues was significantly affected by the restriction of economic activity according to the decree of the Government of Georgia N181 of March 23, 2020 "On Approval of Measures to Prevent the Spread of the New Coronavirus in Georgia." This covered most types of gambling.

Forecasts had stated that 70 million GEL would be made from gambling businesses in 2020, however, due to the indicated circumstances, this forecast proved unfulfilled. In the first six months of 2020, 3,574.4 thousand GEL was received in charges from gambling businesses, just 10.2% of the planned amount (35,000.0 thousand GEL) and is 31,907.2 thousand GEL less than the same indicator for the corresponding period of the previous year (35,481.6 thousand GEL).

The share of taxes and grants in revenues is more than 82%. These accounted for 95.4% of the actual receivables for the first six months. Receivables for the first six months of 2020, both in absolute terms and in proportion, were lower than the figures for the same period of 2019. Receivables in 2019 amounted to 535,923,700 GEL, which was 100.6% of the planned amount, and in 2020 it was 428,512,900 GEL (75.5% of the corresponding period). Within conditions of 75.5% of cash execution of receivables, the cash execution of payables was 69.5%, and budget "accumulation" amounted to 32,256,200 GEL. The policy of budget accumulation by the central government has also become a subject of "imitation" in places.

In the first six months of 2020, the rate of payable performance was 69%, a 5% reduction compared to the same period of 2019, and in monetary terms 4,358.0 thousand



GEL more was spent (compared to the first six months of 2019). The tendency of costs increasing against declining revenues is a local manifestation of the state budget policy. Therefore, payables in the Tbilisi budget increased in light of declining revenues. The latter were reduced due to a reduction of tax revenues going to the state budget and the

allowances afforded by the Government's anti-crisis plan to reduce property and VAT. This, in turn, was reflected in the corrected budget approved by the Tbilisi City Assembly on 14 July 2020.

Marneuli

Marneuli municipality is connected to Tbilisi with respect to daily economic activities. Indeed, there is circular migration from this municipality to the capital. Many residents of the municipality bring agricultural products to Tbilisi, sell them, and return home in the evening. There is counter-movement as well, meaning some from Tbilisi are employed in Marneuli. Responding to the pandemic, a strict quarantine regime was implemented in Marneuli for the first time, which created problems for the export of agricultural products to the markets and shopping centers of Tbilisi. Apart from a lack of quarantine experience, people were not properly informed, with particular difficulties in communicating directly with the non-Georgian population of the municipality, many of whom lack knowledge of the Georgian language. Accordingly, there were risks affecting product sales and potential product shortages in Tbilisi, as well as falling prices for products in Marneuli and a risk of increased prices in Tbilisi. This problem was largely solved through the intervention of the central government and the mobilization of significant administrative resources. Forms of cooperation with business structures were established through the direct intervention of government structures, and the latter ensured the functioning of value chain production, transportation, sales, and consumption. This example revealed the weaknesses of the mechanisms of the Georgian economy. In particular, the weak development of the value chain including a lack of wholesale and retail trade systems and a shortage of warehousing farms.

The budget of Marneuli was adopted on 24 December 2019⁶¹, and was subsequently corrected on 27 July 2020 in accordance with the changes made to the state budget on June 24.⁶²

⁶¹ <https://matsne.gov.ge/ka/document/view/4744747?publication=0>

⁶² <https://matsne.gov.ge/ka/document/view/4945029?publication=0>



Table 9. Marneuli municipality budget for 2020 (initially planned and corrected)

Budget	2020 (planned)	2020 (corrected)
Receivables	34,927.5	33,549.9
Revenues	34,513.7	33,329.9
Taxes	18,408.8	20,537.2
VAT	12,408.8	14,537.2
Property tax	6,000.0	6,000.0
Grants	10,579.7	4,943.6
Other revenues	5,525.2	7,849.1
Payables	40,602.1	33,549.9
Costs	20,976.4	19,354.7
Operating balance	13,537.2	13,975.2
Total balance	-5,524.5	150.1
Balance (receivables-payables)	-5,674.6	0.0

Frequent changes in the budget have been noticeable in Marneuli. Corrections were mainly introduced and legalized in the expenditures rather than making attempts to set a balance between revenues and expenditures. This practice is considered positive, which has not been attainable for the central government.



Table 10. Marneuli municipality budget corrections

Date of correction	Receivables	Revenues	Payables	Costs
26.12.2019	33549.9	33329.9	33549.9	19354.7
09.01.2020 ⁶³	35955.3	35735.3	35955.3	19354.7
23.01.2020 ⁶⁴	38710.2	38354.2	44384.9	20551.5
12.02.2020 ⁶⁵	38768.0	38354.2	44442.6	20551.5
11.03.2020 ⁶⁶	38891.4	38477.6	44566.0	20737.8
06.04.2020 ⁶⁷	38891.4	38477.6	44566.0	20937.8
12.06.2020 ⁶⁸	38891.4	38477.6	44566.0	20943.8
27.07.2020	34927.5	34513.7	40602.1	20976.4
07.08.2020 ⁶⁹	34927.5	34513.7	40602.0	21038.4
25.08.2020 ⁷⁰	35203.3	34789.5	40877.9	21045.6
21.09.2020 ⁷¹	34978.1	34564.3	40652.7	21113.2
15.10.2020 ⁷²	35263.1	34564.3	40937.7	21351.2
13.11.2020 ⁷³	35263.1	34564.3	40937.7	21522.9

Under the quarantine regime, changes were applied to the municipality budget three times, but the forecasts for receivables and payables did not change. The forecasts were changed only under the influence of changes made in the state budget; the VAT rate was reduced.

⁶³ <https://matsne.gov.ge/ka/document/view/4770321?publication=0>

⁶⁴ <https://matsne.gov.ge/ka/document/view/4778779?publication=0>

⁶⁵ <https://matsne.gov.ge/ka/document/view/4797610?publication=0>

⁶⁶ <https://matsne.gov.ge/ka/document/view/4820488?publication=0>

⁶⁷ <https://www.matsne.gov.ge/ka/document/view/4846421?publication=0>

⁶⁸ <https://www.matsne.gov.ge/ka/document/view/4894069?publication=0>

⁶⁹ <https://www.matsne.gov.ge/ka/document/view/4958830>

⁷⁰ <https://www.matsne.gov.ge/ka/document/view/4972415?publication=0>

⁷¹ <https://www.matsne.gov.ge/ka/document/view/4997544>

⁷² <https://www.matsne.gov.ge/ka/document/view/5016594?publication=0>

⁷³ <https://matsne.gov.ge/ka/document/view/5032624?publication=0>



Bolnisi

The Bolnisi municipality budget for 2020 was adopted on 16 December 2019, and was subsequently corrected on 25 August 2020.

Table 11. Bolnisi municipality budget for 2020 (initially planned and corrected)

	2020 (planned)	2020 (corrected)
Receivables	40079.6	40227.9
Revenues	36157.0	36305.3
Taxes	4729.6	4693.8
VAT	933.6	1093.8
Property tax	3200.0	3600.0
Grants	8321.0	7909.1
Other revenues	23702.4	23702.4
Payables	40079.6	40227.9
Costs	26283.9	25534.8
Operating balance	9873.1	10770.5
Total balance	-3709.6	-3709.6
Balance (receivables-payables)	0.0	0.0

The main change in the Bolnisi municipality budget came from the reduction in the VAT forecast. Property tax was also reduced. It is important to note that the stability of the municipality's budget is based on a high level of "other revenues" accounting for 65.5% (23,702.4 thousand GEL) of Bolnisi municipality's budget revenues (36,257.0 thousand GEL). This is mainly derived from fees for the extraction of natural resources⁷⁴.

⁷⁴ <https://www.matsne.gov.ge/ka/document/view/4972446?publication=0>



Rustavi

Due to corrections made to the state budget as of 24 June 2020, subsequent amendments to the municipal budget of Rustavi saw a reduction in forecasted figures for receivables, revenues, and taxes, but an increase in payables and costs. Therefore, if the balance for the initially approved budget was -1,774.7 thousand GEL, with these enforced changes it was changed to -8,169.1 thousand GEL (i.e. the figure dropped 4.6 times). The municipal budget deficit is significant, with the difference between revenues and costs (operating balance), the difference between operating balance and non-financial assets (total balance), as well as the difference in the balance of receivables and payables all being negative. This situation is found in virtually all municipalities, which indicates that the principle of balancing municipal budgets is in jeopardy.

Table 12. Rustavi municipality budget for 2020 (initially planned and corrected)

	2019	2020 (planned) ⁷⁵	2020 (corrected) ⁷⁶
Receivables	59,035.1	54,331.3	55,785.4
Revenues	56,875.1	52,628.9	54,785.4
Taxes	34,789.5	33,907.3	38,753.6
VAT	22,695.4	23,007.3	26,953.6
Property tax	12,094.0	10,900.0	11,800.0
Grants	13,997.7	15,104.6	10,790.8
Other revenues	8,087.9	3,617.0	5,241.0
Payables	60,566.2	62,500.4	46,384.7
Costs	36,490.5	38,961.2	38,457.2
Operating balance	20,384.6	13,667.7	15,561.4
Total balance	-704.4	-7,692.1	-1,297.7
Balance (receivables-payables)	-1,531.1	-8,169.1	-1,774.7

⁷⁵ 27.08.2020- On Amending the decree №158 of Rustavi Municipality Assembly of December 20, 2019 on the Approval of the Budget of Rustavi Municipality for 2020

⁷⁶ 20.12.2019-On the approval of the budget of Rustavi Municipality for 2020

<https://matsne.gov.ge/ka/document/view/4974518?publication=0><https://matsne.gov.ge/ka/document/view/4739167?publication=0>



Revenues of Rustavi municipality amounted to 31,271.3 GEL (compared to a planned 42,599.8 GEL), while costs amounted to 25,621.8 thousand GEL (compared to a planned 28,231.1 GEL). Meanwhile, revenues were also lower than in the corresponding period of the previous year (2019 – 37,639.6 GEL), although costs were higher (2019 – 24,691.1 GEL)⁷⁷. During the first nine months, 20,847.2 thousand GEL was mobilized in the form of taxes, which is 73% of the forecast. Of the taxes received, 17,137.4 thousand GEL was VAT, which is 80% of the forecasted amount (21,430.3 thousand GEL).⁷⁸

The approved plan of the municipal budget of Rustavi for 2020 amounted to 57,560.1 thousand GEL (according to decree N158 of the Rustavi Municipality Assembly of 20.12.2019; state registration code 190020020.35.160.016594), taking into account the implemented changes, the budget parameters were specified and set at 62,500.4 thousand GEL.

Findings and Recommendations

Summary

On 24 June 2020, as part of the Government's anti-crisis program, a major correction of the state budget took place. This triggered changes in the budgets of all municipalities, reducing their revenues and corresponding results. It was found however that the state budget corrections did not entail a reduction in grants. In the first half of 2020, state grants were not reduced in any municipality except Tbilisi (from 100 million GEL to 55.4 million GEL). On the contrary, the amount of grants increased after the changes implemented in the state budget for 2020, rising to 166 million GEL, instead of the 131 million GEL provided for in the initial budget.

The main damage was done to the budgets of municipalities due to a relaxation of VAT in the country. The reduction in VAT reduced each municipality's own percentage share of this source of revenue. In addition to the economic crisis and the slowdown in domestic economic activity, collection of VAT was hampered by a reduction of imports into the country. The amount of VAT received was reduced as a result of the introduction of the VAT refund mechanism.

⁷⁷ https://rustavi.gov.ge/file_manager/16/cc7cfe92e0a2d24517eff5ece7c64e6c.pdf

⁷⁸ https://rustavi.gov.ge/file_manager/16/cc7cfe92e0a2d24517eff5ece7c64e6c.pdf



Municipal budgets also did not receive the forecasted amount of property tax, which was due by June 15. The central factor here was the decision of the central government to largely postpone payment of property taxes until November 1, and to exempt the tourism sector from such payments altogether until the end of 2020. Thus, the Georgian government supported businesses by using tax mechanisms at the expense of the municipal budgets. As a result, after the state budget correction on June 24, the VAT and property tax forecasts were reduced.

Prior to the amendments made to the budget, appropriations were made through changes in the expenditures. The application of the principle of expediency in budget performance has led to some asymmetries in the financing of programs and sub-programs. In the first half of 2020, programs and sub-programs worth more than 60 million GEL had zero utilization, while more than 200 million GEL had less than 30% utilization. This was not due to COVID-19, but, as concluded by the State Audit Office, was due to inefficient management of budgetary resources.⁷⁹ Thus, the impact of the pandemic on municipal budgets was not due to strategic or tactical changes, but to changes in the flow of sources of funding that could be associated with a particular government decision or economic situation.

Due to delays in VAT collection, its transfer to municipalities has decreased. To compensate for the lack of VAT, the Ministry of Finance used an adaptive management method and recommended on-site funding cuts for appropriations (mainly for LEPLs and NNLEs). The repayment of already incurred liabilities through loans from the state budget for the next period was usually implemented through reducing a VAT breakdown. This practice was viable until the changes made to the state budget on June 24.

The issue of VAT for municipal budgets is greater than that of appropriations not being received due to the pandemic. Even without the pandemic, the pre-existing mechanism for using VAT as a source for local budgets was problematic and posed a constant threat to the stability of municipalities. The pandemic has of course accelerated the manifestation of systemic deficiencies. In the event of an equalizing transfer, municipal revenues would ordinarily be tied entirely to the state budget. However, being reliant on a single tax, which is variable and depends on many domestic and external factors, is highly risky.

No significant differences were observed in the impact of the pandemic on municipal budgets across municipalities with varying degrees of spread of the virus. This is due to the centralized management of processes during this period. The municipalities did not directly receive anti-pandemic funding, neither in their own budgets nor in the form of transfers. The municipalities under quarantine regimes, their residents, and officials

⁷⁹ http://parliament.ge/ge/ajax/downloadFile/142733/1-14376_auditi, pp.13.








naturally faced a significantly difficult period compared to so called “green zones”, but impact on the budgets was similar across all municipalities. Revenues and costs of municipal budgets were heavily affected by the state of emergency. The specific issues of individual municipal budgets were determined mainly by their usual income base rather than the extent of the quarantine measures therein.

In the first half of 2020, the total volume of costs exceeded the costs of the corresponding period in 2019. The total balance (deficit) of the consolidated budget in the first quarter of 2020 was -316.9 million GEL, and in the second quarter it was -759.8 million GEL. This was a result of optimistic planning for 2020. Budgetary estimates were made without legislative changes, costs increased to fund pandemic measures, and receivables were reduced amid declining tax revenues. These trends threatened the budgetary balance at both central and local levels.

Findings

Informed by the conducted analysis, the following conclusions have been drawn:

-  The main element in the composition of municipal budgets in Georgia in the first half of 2020, as was the case in previous years, was state financial assistance. The share of transfers and grants received from the state budget amounts to between 60% and 95% of municipal budget revenues.
-  The current budget policy of Georgia is the main factor affecting the budgets of municipalities (especially when it comes to income), and current fiscal-economic processes within the municipalities are additional factors to bear in mind.
-  The budgets of the state, autonomous republics, and municipalities for the year of 2020 were approved in December 2019 with some very optimistic parameters and forecasts. This was based not only on the expectation of high economic growth, but also on the decision to take on an unprecedented amount of loans in the budget, which marked a continuation of the 2019 policy with regard to budget deficit and government debt.
-  The budgets of municipalities in the first half of 2020 were impacted indirectly by the primary impact of the crisis on the state budget.
-  The biggest impact on the budgets of municipalities was the reduction of VAT which was due to objective (economic shrinkage) and subjective (government benefits) reasons.



As part of the pandemic mitigation measures, government decisions on property tax exemptions significantly reduced municipal revenues.



Other revenue shortfalls in municipalities also occurred, mainly due to government decisions (i.e. adjusting transfers or administrative interventions in the economy).

These impacts were felt differently in individual municipalities (for example, gambling business revenues (and tax collection therefrom) in Tbilisi and Batumi increased when economic activity was limited).



In the first half of 2020, strict quarantine regimes were implemented in ten municipalities (Batumi, Bolnisi, Tbilisi, Tetrtskaro, Lentekhi, Marneuli, Rustavi, Kobuleti, Kutaisi, and Khashuri). In total, 52% of the population of Georgia lives in these municipalities. Despite popular expectations to the contrary, no evidence was found that the impact of the pandemic on the budgets of these municipalities was any different than in the other “green” municipalities.



The pandemic has not changed the relationship between state and municipal budgets. Due to their dependence on the state budget, after the changes in the state budget of Georgia on 24 June 2020, all municipalities corrected their budgets accordingly.



The actual performance of tax revenues (against the forecasted figures) has led to structural changes in the budgets of municipalities (including changes in revenue and cost parameters). A common characteristic of these changes was found in revenues and receivables, costs, and payables.



The first half of 2020 was better than 2019 in terms of budget receivables and payables. The budgets for 2020 were so optimistically planned and resources were attracted on such a scale that the level of implementation for all parameters, regardless of whether the budget breakdown (plan) was implemented, was actually higher than for the corresponding period of 2019.

Recommendations

Based on the above findings, the following recommendations are made to improve Georgia’s budgetary system:




The existing policy should be changed to provide a balanced budget policy that ensures the adequacy of revenues and costs (i.e. to move to a spending policy determined by the amount of revenue received from ongoing economic activities).





Based on the lessons learned from the first wave of the pandemic, any decision made by the central government to change the local tax should be agreed with each munic-




ipality, and if this decision reduces tax revenue at the local level, then this deficit should be compensated from the state budget.

 Municipal budgets should be protected from non-immanent, volatile revenues and should be provided with guaranteed revenues. The Ministry of Finance should study the effect of VAT sharing on local budgets and, if necessary, use additional financial instruments to ensure financial equalization of municipal budgets.

 Ensure the full utilization of local self-government opportunities and their full partnership in the fight against the pandemic, by accelerating reforms and changes to strengthen them financially and materially.

 Establish procedures for the publication of monthly results of municipal budget performance and the resolution of technical issues.

 The state audit of municipal budgets should be conducted annually. For this purpose, the current norm of hearing a report on the audit of municipal budgets at the Parliament of Georgia once every two years should be changed to annually. State audits should be conducted in relation to the use of unspent budgetary funds by municipalities as well.

