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## **INTEGRATING LAND ISSUES INTO THE BROADER DEVELOPMENT AGENDA**

### **Country Case Study for the Regional Workshop on Land Issues in Central and Eastern Europe and the CIS**

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## **Part 1. Introduction: - Historical Background and the Current Situation**

### **1.1. Georgian economy**

Georgia strategically is situated as a trade and transit corridor in Transcaucasia, between Europe and Asia. In 1995 Georgia's total population was 5,411,000. According to 2000 July estimates it comprised 5,019,538 people, recent data recorded approximately 4,900,000 people. Country has an area of 69 700 square km. It shares its northern border with Russia, to the south lies Armenia and to the south-east, Azerbaijan. There is also a short frontier with Turkey, and a western coastline on the Black Sea.

In the Soviet period, Georgians enjoyed a relatively high standard of living. The country benefited considerably from a supply of cheap energy and raw materials. Industry was developed. For functioning of the giant enterprises concentrated and constructed in the administrative centers of the country, people were systematically forced to migrate from villages to cities. The majority of the large enterprises represented the part of the unified Soviet economy and today they have no perspective for further operation.

In the Soviet period Georgia was well known as a supplier of agricultural products. Georgia also produced a wide range of minerals. Principal mineral resources extracted were manganese ore and coal. Georgia also produced small amounts of petroleum and natural gas in the eastern region of the country. The sub-tropical climate of western Georgia allowed for the cultivation of tea and citrus fruits, while the dryer climate in eastern Georgia was ideal for viticulture. However the collective principle of the work was having negative effects on the agriculture, as employers of the collective farms concentrated on the quantity rather than the quality of the harvest.

The service sector particularly tourism, was well developed. Mineral and thermal springs, mild climate, fascinating nature, excellent wines, traditional Georgian hospitality, and ancient historical sites were the major attractions for travelers to Georgia. However in the centralized system of administration and control it was impossible to estimate the actual revenues generated from this sector for the country's economy.

After gaining independence in 1991, the Georgian economy experienced devastating deterioration. The termination of trading links with former Soviet republics created unfavorable conditions for local and foreign markets. War and ethnic problems caused additional severe difficulties.

In early 1994, the government embarked on a comprehensive reform program to rebuild the economy, with the support of the World Bank and the International Monetary Fund. Economic reforms included judicial, tax and regulatory reforms, the liberalization of trade, and the establishment of free currency exchange rate.

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On May 1994 President Shevardnadze issued a decree to accelerate the process of all kind of privatization.

On September 1995 the Government introduced a new currency, the lari. The success of the lari and a steady decline in the rate of inflation were the results of a strict government monetary policy.

At the beginning of 1995, the Parliament passed the country's first budget.

As a result of these economic reforms and stabilization of civil conflicts, Georgia's economy slowly began to recover.

Economic growth became even more tangible in 1996 and 1997. The situation again deteriorated in 1998 as a result of the Russian financial crisis. In 1998 the gross domestic product increased by only 3 percent. In 1999, the increase in GDP was the same: 3%.

Slow growth continued in 2000, as GDP increased by less than 2%. The drought causing 12,6% decline in agriculture output was a major contributing factor underlying this slow growth rate.

In 2001, GDP comprised 6.51 billion GEL. Service sectors (transport, telecommunications and financial intermediary business) enjoyed the highest rates of growth. Total investments for the year 2001 comprised 5,9% of GDP. The largest investors were Turkey and the USA. Industry, however, continued to be hampered by low and unstable growth.

The important indicator of the economic situation - the level of unemployment is high. The showing indicated in the official statistics (11,4 percent) is very unrealistic. That is caused by overestimating the number of self-employed people. It is also noteworthy that almost absolute majority of the people employed in the public sector receive wages less than the living minimum.

Civil war and unrest, coupled with the country's economic and social collapse, resulted in an almost complete cessation of tourism in the early 1990's. The number of travellers, both international and domestic, decreased dramatically. Tourism facilities deteriorated because of lack of funds for proper maintenance and capital repairs. Nevertheless, Georgia demonstrated its commitment to development of its tourism sector by joining the World Tourism Organization (WTO) in 1993. With assistance from international organizations, programs have been initiated to preserve and maintain Georgia's cultural and natural heritage. It is true that because of Georgia's favorable location tourism has the serious potential, however the experience of the Soviet period cannot be considered for very optimistic estimates, especially if to take into account the fact that the rehabilitation of this sector demands enormous investments and the stabilization of the economic and political situation in the country.

Georgia's international relations have diversified after the dissolution of Soviet system. Georgia was the first South Caucasian country to become a full member of the Council of

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Europe in April 1999. The World Trade Organization decided to admit it as a member in October 1999.

By 2001, Georgia's major trading partners were Turkey, Russia and Azerbaijan.

The Georgian economy still continues to experience a trade deficit and a large budget deficit. Endemic corruption and a failure to collect tax revenues are important contributors to these problems. By 2001, total tax revenues comprised 14.5 percent of GDP, which is significantly less than the average indicator in other countries of the region.

Georgia still suffers from acute energy shortages. The country imports the bulk of its energy needs, including natural gas and oil products. Its only sizable internal energy resource is hydropower, and this potential is only partially developed. Georgia privatized the electricity distribution network in 1998, and deliveries are steadily improving.

In the country there is a very hard criminal situation, which significantly hinders the development of the country, the human rights are violated. The reform of law enforcement agencies has not been carried out.

Because of Georgia's favorable location at the crossroads of Europe and Asia, the country is pinning its hopes for long-term recovery on the restoration of the "Great Silk Road", from the Black Sea across Georgia to the Caspian Sea, and on the development of an international transportation corridor through the key Black Sea ports of Batumi and Poti.

Country also hopes to benefit from the construction and exploitation of the Baku-Tbilisi-Geikhan oil pipeline and Baku-Erzrum gas pipeline, which will raise revenues and will support the development of the infrastructure. In addition the involvement of Georgia in the global projects will be the guarantee of country's secure and stable development. However in the first place the resolution of the internal problems is of vital importance for the country.

## **1.2. Agriculture**

Agricultural lands total 3,02 million ha, which make up about 43,4% of the total area of the country. There are nearly 800 000 ha of arable land (11,5%), and 332 000 of perennial crops (4,3%), which together comprise only 16 % of land area. The rest of the agricultural land is devoted to pasture (1,8 million ha, or 25,8%) and meadow-land (0,14 million ha, or 2,01%). The country also has substantial forest reserves: roughly 43% of the country's territory (2.75 million ha) is under forest cover.

Agriculture has historically been one of Georgia's most important sectors due to the country's diverse climates and relatively good soils. The crop and horticulture sector dominates primary agriculture in Georgia. Traditionally, this sub-sector provided about 2/3 of all agricultural output. Wine, tea, fruit, and vegetable canning, citrus processing, and mineral water bottling represent the major products.

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Due in good part to the loss of its export market to other former Soviet Republics, Georgia's agricultural production has declined dramatically in the ten years since independence. Georgia has turned into a net importer from being a net exporter of agricultural products. In recent years, Georgia has been far from self-sufficient in the production of some of the basic food products (such as bread flour, eggs, milk, and sugar). Exporting industries such as wine, citrus and tea are operating at no more than 15 % of capacity. There were objective reasons that have caused the downturn of this branch of economy. In the Soviet period Georgian agriculture sector produced a large quantity of those products that were necessary only for closed Soviet sphere. In particular, country began to specialize in the production of citrus and tea unusual for local agriculture. As demand on those products was very high (among other Soviet countries, Georgia had unique climate conditions for the cultivation of these products), little attention was paid to the quality of the output. The same approach existed toward wine production.

Although in the post Soviet period land parcels were transferred into private ownership of Georgian citizens, the buildings, machinery and other technical means of the state-owned collective farms had been robbed. As a result farmers received land, but they had no technical means to treat it.

The major drawback of this period was the absence of strategic program for the development of agriculture. Disintegrated collective farms had no knowledge of modern management and principles of market economy, whereas they actually received the largest areas of land parcels.

These problems were aggravated by corruption. Trade marks of strategic products - Georgian wines were sold. Farmers themselves had to seek solutions out of the existing situation.

During the first phase of post Soviet period the development of agriculture followed the old trend. Country continued to produce a large quantity of low-quality products characteristic for Soviet period. Former processing enterprises mainly privatized by ex-directors, tried to sell low-quality products on traditional old markets, however as a result of competition they went bankrupt. Farmers concentrated on local markets, but because of corruption and uncontrolled smuggling of cheap produce, they lost even local markets for the majority of their products.

Deriving from the above mentioned, the unfavorable conditions of the agriculture sector were due to economic downturn and the absence of development strategy.

Despite the poor social and economic conditions remarkable increases have been recorded in agricultural output for the past several years. Agriculture contributed 19.2 percent to the GDP in 2001. This growth indicator is largely due to the fact that the layer of farmers is slowly forming. They managed to adapt to the principles of the market economy. High quality products began to appear on local and foreign markets.

Although, the impeding factors are still many. Processing industry faces serious problems. Most of the capital inherited from Soviet days has deteriorated badly in the last ten years, and

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much of it is inoperable. Irrigation systems, which might have rescued Georgia from the drought of the past several years, largely lie in ruins.

Another problem hampering agricultural production for the domestic market is the smuggling of imported farm products from neighboring countries, which drives down the price for local competing crops.

At present, 58 percent of employed persons in Georgia are involved in agriculture. Sustained economic growth of the country at large cannot occur without achieving a significant increase in agricultural production.

To be competitive in the world agriculture marketplace, Georgia must consistently produce products that meet international standards for quality and food safety at competitive prices. Major capital investments are also needed at all stages of the agricultural production and food processing system, from better farm equipment, improved seed and plant stocks, modern processing facilities, to proper storage and transport systems to bring products to market.

## **Part 2. Land Reform and Privatization**

During the Soviet period, Georgian commercial farming was represented by collective and state-owned large-scale farms both subject to centralized management and control. In 1988 they encompassed 87 percent of all agricultural land while auxiliary family plots accounted for 5.5 percent. In the Soviet system of farming, a typical family in a village was allocated 0.25 ha for family production. Regardless, all land was owned by the state.

The process of land reform in Georgia began with Resolution # 48 of the Government of Georgia, dated January 1992 and was caused by extremely poor social conditions. Deriving from the social and economic hardship experienced after the collapse of the Soviet Union, government was forced to begin transferring land parcels to each citizen. This was considered as the primary measure for alleviating poverty. The resolution of 1992 is generally known as “the land privatization decree”, although more properly its objective was land distribution. Following this resolution, a “privatization reserve” of 850 000 ha was established. The privatization reserve encompassed less than 30 % of total agricultural area. Land from the privatization reserve was distributed free-of-charge to rural households. 1.25 ha was the maximum area of agricultural land to be transferred into ownership in the lowlands, while up to 5 ha was distributed to eligible households in the highlands. Land reform committees elected by the village managed the distribution of this land.

The distribution of land in the lowlands was carried out according to three categories:

- Citizens who were directly involved in farming had the right to receive 1.25 hectares of land per household
- People who lived in rural areas but were not involved in farming had the right to 0.75 hectare.
- People from urban areas had the right to 0.25 hectare.

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One of the major impediments that have prevented complete distribution of the entire “privatization reserve” has been the political and civil unrest in Georgia. As a result, the percentage of agricultural land distributed in different districts is highly irregular.

In Georgia the process of privatization included two forms of land management (and ownership): the first being the allotment of land parcels of up to 1.25 ha per rural family, the other is the lease of the remaining state-owned agricultural land by physical or legal entities. This process was intended to create two main agricultural sectors: a self-subsistence sector for small farmers, and a market-oriented sector controlled by large leaseholders.

The agricultural land reform process has involved number of agencies at the national and local government levels. At the national level, a special committee was established to deal with all aspects of land reform and to manage the land reform in the collective and state farms. This committee was later incorporated into the Ministry of Agriculture and Food Industry, and was vested with responsibility for planning and implementing land reform, and proposing land legislation to be ratified by the Parliament.

The land privatization decree (Resolution # 48) was followed in September 1992 by a Government resolution on the reorganization of collective and state farms. As a result, the Soviet era large-scale farms have largely disintegrated, although they still exist (in some instances) as joint stock cooperatives leasing state land.

The allotment of agricultural land began somewhat spontaneously and lacked the necessary legal guarantees. To rectify this situation, on June 28 1993 Georgian Cabinet of Ministers adopted Decree #503. This Decree authorizes local land reform committees the issuance of the receive-delivery Act, which to this date is considered as the main document for granting ownership of agricultural land to households.

On March 1996, the Parliament of Georgia legitimized the acts issued by the Government of Georgia and issued the “Law on Private Ownership of Agricultural Land”. According to this law, all governmental resolutions granting agricultural land ownership rights to the citizens of Georgia were considered legitimate.

By 1996, nearly 4 million land parcels total of 930 000 hectare were allotted to 1 400 000 person. However, the majority of new owners have not obtained the receive-delivery act, because they were unwilling or unable to pay for it (26 GEL per parcel). This has prevented initial registration of land and hampered the development of the land market. In addition, the Government has been unable to finance the preparation of surveys and other legal documents necessary for the registration of ownership to the land.

The Parliament of Georgia issued the “Law on Land (Immovable Property) Registration” in 1996. The problem was that since 1992, when agricultural land was first privatized, the transfer of ownership rights on land was not being properly registered. The existing system only recorded initial owners, and this was not sufficient for recording subsequent transactions. Also, the existing system failed to meet the requirements of the new laws adopted during 1996-1999.

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In order to accelerate the process of initial registration of land ownership rights and the issuance of registration certificates to Georgian citizens, and to help create sound system of land cadastre and registration, a number of international organizations provided the necessary technical, financial, methodological and consulting support to the country.

With the support of USAID, on May 16, 1999 Presidential Decree #327 was issued on “Urgent Measures for the Initial Registration of Agricultural Land Ownership Rights and Issuance of Registration Certificates to Georgian citizens”.

In order to ensure that the process of initial registration be transparent and less time consuming, the State Department of Land Management (SDLM) and USAID agreed to minimize the number of documents necessary for land privatization and initial registration. Particularly for the initial registration, it is sufficient to present one or more of the following documents:

- a. Land Receive-Delivery act; or
- b. Land Distribution Lists of owners approved by the local land reform committee created on the basis of 1992 resolution, along with the plan on the allotment of land; or
- c. List of land possessors existing in the Tax Inspection Service at the time of registration.

As a result of this agreement, the problem accompanying the privatization of agricultural land in Georgia was resolved in a timely, simple, inexpensive manner. This simplified initial registration also expedited the formation of a land market in Georgia, for conducting secondary transactions: sales, leases, mortgages, and the like.

From 1999 until December 2001, as a result of the USAID project, 1 325 000 agricultural land parcels have been registered. This has included:

- Carrying out cadastral planning works on these parcels, which established or verified the area of land parcels;
- Preparing relevant registration documentation;
- Registering the above in local land registration offices (Public Registries); and
- Granting Registration certificates to landowners.

The Decree allowed the registration of the ownership of land parcels free of charge even if the area of land parcels allocated to each household was 15% more than area set by norms. In reality, since allocation took place based on prior and often incomplete land survey records, the area of the allocated land parcels often did not correspond precisely to the norms set by Resolution of 1992. The approach adopted by the Decree thus prevented technical and social problems with landowners when conducting cadastral works.

According to the recent data, to this date approximately 1 700 000 agricultural land parcels have been initially registered.

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Private ownership did not exist on nonagricultural land prior to November 1997. Land parcels possessed by private persons were deemed owned by the state.

The initial phase of privatization of nonagricultural land included land parcels with apartment buildings and individual houses. The Civil Code established that nonagricultural land parcels under individual houses and apartment buildings were owned by their residents.

The second phase of privatization covered industrial land. Parliament issued a special law in 1998, "Declaration of Private Ownership of Nonagricultural Land in Use by Physical and Private Legal Persons", which declared private ownership of nonagricultural lands possessed by entrepreneurs. The law did establish a one-time symbolic payment for obtaining ownership rights that was equal to the annual land tax.

Initial registration accompanied the process of privatizing industrial land. Enterprises were required to submit certain documents to the Registrar in order to have land privatized.

The above measures allowed successful implementation of the land reform throughout large areas of Georgia. The conditions that allowed such successful results included effective use of already existing documentation, avoidance of unnecessary bureaucratic steps, and the establishment of an affordable fee for initial land registration. However major contributor to this success was the donor community.

Analysis of the reform reveals number of mistakes that were made during the process. In the distribution process, land was considered as means for self-subsistence, not as real estate. Land reform didn't consider the distribution of land on equitable basis. Employers of collective farms were given priority. One argument for the chosen approach is that these people with long-term experience of farming have lost jobs and it was necessary to compensate it somehow. But it wasn't taken into account that this part of the population who received largest share of land parcels, was not flexible to adjust to principles of market economy. May be it would be more equitable to compensate employers of ex-collective farms through reallocating property they have created, and to allocate land on the rest families not according to categories, but other principle, like according to the number of family members. As for the majority of rural households land represents the major source of income regardless whether the members of these households did or did not work in the collective farms.

As a result of land reform land parcels were accessed by rural households who knew how to cultivate it, but were absolutely unprepared to adjust to the market economy principles.

The lease of land was linked with corruption. Influential state officials received the most fertile land parcels. They had neither experience nor interest in farming and sub-lease land. Without adequate irrigation system and technical means, plus non-existence of insurance, inability to pay taxes, sub-lessees themselves don't use land efficiently.

Because of the chosen kind of allocation the average area of the land parcel in private ownership doesn't exceed 0.22 ha, which indicates that the privatized land is very fragmented and is not a subject of interest for banks.

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Deficiencies of the privatization process include that the majority of agricultural land parcels are still owned by the state and are leased out and majority of pastures are not privatized.

### **Part 3. Identification and Characterization of Critical Land Issues in the Country**

#### **3.1. Critical problems**

Among reforms implemented for the economic stabilization of Georgia, land reform is considered as the most successful of all. Nonetheless, several problems exist that impede the creation of a sound system of land management and use.

##### a) Underdeveloped agribusiness

Agriculture is important sector of the country's economy. Despite the fact that Georgia has a serious potential for local agriculture demand and export production processing, the government has failed to recognize it as priority field and to embark on measures for the development of this sector.

There are numerous reasons that underlie this problem:

- Low prices on the agricultural produce – because of uncontrolled import of cheap produce;
- The agro-processing industry is not functioning;
- The packing industry does not exist;
- There are not developed transport companies for cargo transportation;
- Insurance for commercial risks cannot be easily obtained;
- Farmers have inadequate access to agricultural means – seed and plant material, machinery, water and so on. The market of these materials does not exist in Georgia due to the high custom duties and other taxes;
- Farmers lack technical knowledge of state-of-the-art agricultural techniques;
- To receive land by lease one has to pay bribes;
- There are no links and feedback between the government and the farmers;
- Unfavorable tax policy – VAT and profit tax do not encourage agricultural productivity;
- High interest rates on credits;
- Limited information for entrepreneurs wishing to receive credit on how to apply for a credit efficiently, and which credit institution is best to approach for their specific needs;
- Unwillingness by banks to accept fragmented agricultural land as collateral.

##### b) Complicated institutional structures

There are several governmental structures in Georgia dealing with land issues. These are the State Department of Land Management, the Ministry of State Property Management, The Ministry of Agriculture and Food, the Ministry of Urbanization and Construction under which

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functions the Bureau of Technical Inventorization and the Department of Geodesy and Cartography.

**The State Department of Land Management (SDLM)** is a major agency in land administration matters. It is headed by a chairman and six deputy-chairmen. The functions of the SDLM include:

- Land registration and cadastre (activities the SDLM is mainly occupied with at present);
- Land valuation;
- Land reform, land arrangement and disputes over property;
- State control over land use and protection, as well as natural resources;
- Land Statistics;

The central office of the SDLM is responsible for developing state land management policies, designing and implementing programs, and assisting in the preparation of legislation on land management issues. Decentralized regional and local offices carry out land registration and cadastre operations. The SDLM doesn't currently carry out land use planning.

One of the SDLM's institutional strengths at present is that it is responsible for both land registration and the cadastre. This combination provides favorable circumstances for coordinating two informational systems on land ownership and ensures that the registration and cadastral systems function effectively and efficiently.

**The Ministry of Agriculture and Food** is responsible for agrarian reform. It has to formulate agrarian reform policies to be implemented by the SDLM as part of its land reform.

**The Ministry of State Property Management** auctions out land parcels existing in state ownership.

**The Ministry of Urbanization and Construction** shares responsibility with the SDLM for land use planning and policy formulation. The Bureau of Technical Inventorization (BTI) is subordinate to the Ministry and has records on real estate.

**The State Department of Geodesy and Cartography** regulates surveying and mapping activities conducted by state organizations and the private sector.

Often it is very hard for the landowner to understand which agency provides which service. Frequently, the registration of real estate is accomplished not in the Public Registry (in the registration office of State Department of Land Management), but in the Bureau of Technical Inventorization. The information about land is recorded and registered in registration offices, but the information on building-construction is recorded and registered in BTIs. This causes the duplication of the information, in most cases in these agencies take place the existence of mutually exclusive information on one and the same property, which is destroying for the protection of ownership rights and land market. For several years there is a dispute among these agencies about their functions, the information is not being exchanged.

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There is no independent agency for registering rights on land and real estate. The specific function for administering and disposing of state property and on the other hand real estate registration function are not differentiated: local registrars are also considered to be deputy heads of SDLM's land management offices, and as a result they are unable to make decisions independently, though they are independently responsible for their actions.

Land management agencies themselves are under double subordination as they are an organic part of the SDLM, and at the same time they are subordinated to local government. For past two years, land management regional offices have been established in the regions. Their heads are persons appointed and lobbied by the proxies of President, and consequently local land management agencies have one more body they must be accountable to. As a result of this overly complicated bureaucratic structure, decisions dealing with serious problems related to land management, disposition and registration, are often delayed, and made in personally favored and non-transparent manner.

The existing situation creates less possibility for transparency and more chances for corruption. Moreover, if we consider low salaries of registration office staff that are frequently not issued for several months, it will be easy to imagine those obstacles that citizens will face in the registration and disposition processes of real estate.

c) Scarce technical and financial capabilities

Since the activation of land reform in 1996, technical and financial support has started to flow. Significant funds have been allocated by international organizations for cadastral as well as registration activities. However, problems related to technical and financial needs still remain unsolved. Incoming donor grants still finance only a small part of the technical equipment needs of the governmental structures such as State Department of Land Management. Regional offices of the State Department of Land Management are poorly equipped, and all land and title information is recorded by hand and maintained in written form, without any computer database. Unfortunately, it is noteworthy that donor assistance is the only substantial source of technical and financial support received by the country's land agencies. The State Department of Land Management does not receive sufficient funds from the State to repair or maintain regional offices, to purchase computers and software, or to create and update comprehensive databases that could provide an accurate picture of land market development in the country.

d) Corruption

Corruption is the most critical problem hampering the successful implementation of economic reforms. Limited access to information, as well as pervasive corruption practices, make it difficult for landowners, entrepreneurs, farmers and other interested parties to overcome artificial barriers that are created by bureaucratic structures. Such impediments emerge when someone who is willing to sell a house or acquire a land parcel goes to a state agency. State bureaucrats are well-schooled in corruption and in creating mechanisms that enable them to extort more money from people.

Transactions such as initial registration, sales, mortgages, and leases of land and real estate

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involve several state and private agencies. Real property owners, entrepreneurs, farmers and regular citizens are usually mistaken by obtaining too many unneeded documents for the processing of a specific transaction. In some cases, transaction parties register their property at one place, when it should be registered at another. For instance, a citizen who purchases real property may register it with the Bureau of Technical Inventorying, the sole responsibility of which is to provide technical data on the property. In accordance to Georgian law, however, ownership rights to real estate must be registered only at the Public Registry.

Many people do not realize that there are resources, such as Public Registry, where information on every officially registered transaction is available for every interested person. Moreover, those who do know of and use such services usually are improperly subjected to unofficial fees and taxes, and required to pay several times more than the official fee to obtain desired information.

Georgia is a country of agriculture and its main resource is land. Therefore, development of agriculture must be a national priority. However, massive corruption and abuse of power block efforts and attempts to develop agrarian sector in Georgia. Because of the lack of transparency and political will on the part of state officials, credits and investments set aside for the development of agriculture do not reach their goal. Lack of information on the terms for receiving international donor organization grants and favorable credits severely limits farmers to access them.

This situation is extremely difficult in regions, for the reason that there are no good means for circulation of such information in rural areas. This helps reinforce a situation where farmers' rights can be suppressed.

Unfortunately, there are many instances of corruption and extortion of money at various regional governmental agencies and structures, including traffic police and tax service. Farmers are often forced to make unofficial payments of money to tax service officials, traffic policemen, land registrars, and heads of land registration offices.

Corrupt practices result from the limited awareness of farmers as to their rights. This in turn leads to the emergence of many different obstacles farmers may encounter in the course of their activities:

- Biased and uncooperative attitude towards farmers at land management agencies;
- Abuse of authority at regional registrars' offices;
- Limitation of farmers in the process of development of agricultural farming;
- Deception of farmers at tax inspection services;
- Illegal actions by traffic police and constrained activities of farmers in the course of product transportation;
- Bribery during certification of products at markets;
- Illegal treatment and bureaucratic attitude towards farmers at different local governmental bodies.

e) Quality of cadastral and registration information

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In the modern world, information is a most valuable asset. Reliable and accurate information is essential for progress in the emerging land market.

Insufficient technical and financial capabilities, and poorly managed statistical data at the Department of Statistics and the State Department of Land Management have resulted in the low quality of available information on the land market. Responsible staff in these departments lacks training necessary for developing modern approaches to information management.

Due to these reasons starting from 1997 seven-donor organizations work in order to bring this system in order, however it is still far from perfection. Despite the fact that USAID Land Market Development Project provides relevant bodies with cadastral information, printed out on paper, along with the digital version, they still do not process and use them. Often the information prepared by the Project is kept in a storage area just for a display and nobody thinks to update it. Such kind of an attitude may place under doubt the justification of the spent money. This concerns to updating the printed and not digital information. In such conditions it is unclear what is going to be done with the digital information acquired as a result of other donors' working.

Despite the substantial financial support, private companies still lack financial and technical means for producing reliable cadastral information. As a result of inaccurate cadastral activities (in particular, inaccurate measurement of the land) it is not possible to verify actual land boundaries, which frequently cause neighbor disputes.

To date the registration offices of State Department of Land Management do not have strength to independently prepare the documentation necessary for registration. Projects of several donor organizations functioning in Georgia are limited by gathering the cadastral information and creating the informational system, but they do not accomplish registration and related works, or if they do it is delayed in time. Unless relevant registration works follows this cadastral works, the information will outdate after certain period of time.

Another problem is the selection of staff. To date about 40 percent of registrars have no relevant qualification, knowledge and experience. Some are not aware with the land-related legislation, which hinders owners as well as the development of civilized land market.

Creation of cadastral and registration systems is still being accomplished in a fragmentary way. Progress made in particular areas (cities, districts, regions) significantly differs from case to case, and it does not refer to effectiveness of the existing cadastre, which lacks features of a unique system of identifying coordinates. There is no doubt that effectiveness of the national land cadastre will increase as more and more territories are covered, and as data are integrated into a unique system. This is anticipated to be fulfilled in 4-5 years time.

A critical problem hindering donors' efforts to establish a unified system of registration is that the registration of rights on real estate is often carried out simultaneously in two agencies – in

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the registration offices of the SDLM, and in the BTIs, in spite of the fact that law clearly identifies the Public Registry as the exclusive locus for the purpose of land title registration.

The lack of unified informational base creates obstacles to the representatives of banking, insurance and brokerage spheres to obtain the complete information on a property, which is to be mortgaged or sold. Banks do not recognize the information about the property ownership existing in BTIs, which reduces the number of market transactions.

Thus, further efforts have to be directed toward ensuring the availability of accurate cadastral data and clarification of property registration procedures, which will significantly enhance and support the development of a dynamic land market in Georgia.

f) *Poor urban and agricultural land management*

In the Soviet period there existed mixed state and private ownership on urban territories. Privatization of apartment buildings was carried out without privatization of land underneath building units. Urban land was mainly state-owned. Law on Declaration of Private Ownership on Non-agricultural Land in Use of Physical and Private Legal Entities was determined to speed up the privatization of land underneath and related to privatized commercial and industrial buildings. Law on Administration and Disposition of Non-agricultural Land Existing in State Ownership adopted 1998 determined the privatization of urban land by means of public competition. Law on Urban Land Privatization was the last piece of legislation regulating ownership on urban territories.

Three state agencies are responsible for the privatization of property and land on urban territories. These are: the SDLM, the Ministry of Urbanization and Construction and the Ministry of State Property Management, whether it would be more efficient in terms of more transparent and simplified institutional structure to assign the responsibility over privatization process to the State Department of State Property Management. Municipalities do not own land necessary for the development of public projects, as privatization of state-owned land doesn't envisage the transfer of land to municipalities, but they are directly involved in the privatization process of state-owned land located within the territories under their authority.

As a result of lack of urban development plan and zoning regulations, urban land privatization isn't related to the potential use of privatized land parcels in the future. Thus the privatization price is not linked to the potential of future commercial profit. Nor the privatization agreements obligate the buyers to financially contribute to the development of infrastructure, which is necessary for supporting future development of privatized land. In this situation urban land privatization doesn't take into account the distribution of economic responsibilities and interest between private owner (the benefited party) and municipality.

The issue of self-governance in Georgia has not been decided yet, which diminishes the role of municipalities in the active land management and spatial development of urban areas. The involvement of state agencies in the aspects of land use in the locality doesn't provide the efficient and transparent use of land. It is important that municipalities are independent in the issues of land use within the urban territories, can independently approve and control the

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urban development plans and projects. State must keep the authority to provide that locally approved projects do not oppose the national interests.

Neither the legal nor institutional frameworks existing in Georgia allow today the efficient management of urban land.

The deficiencies of the privatization process included the uneconomic fragmentation of agricultural land, as a result of which more than 20 percent of productive agricultural land was lost, as today they have to be used for the construction of access roads, for the establishment of boundaries and agricultural fences.

The rural infrastructure is not taken care of. It was built for the operation of large-scale collective farms and it's not efficient for current farming in the small-scale structure. The access roads built during the land reform are in very poor conditions. Irrigation systems are inoperable. The lack of funds doesn't allow its rehabilitation. The water management is not developed. Former Water Users' Association is not functioning. Technical means are outdated, and farmers have no financial capabilities to replace them.

As a result of ignorance of modern land management practice, today 1/3 of the agricultural land are subject to soil erosion. 7.3 percent of agricultural land turned salty. Because of the absence of proper drainage system nearly 3.6 percent of the agricultural land are becoming bogged up. 5.9 percent of the agricultural land are turning into desert, as irrigation system is not properly functioning. As a result of the mentioned reasons the productivity of these lands are decreasing. Territories of fruit gardens, tea plantations are not cultivated due to the loss of markets. The land protection demands very high expenditures which farmers cannot provide without the assistance.

### **3.2. The legal framework of property rights**

Private ownership rights on property are acknowledged and protected by **Georgian Constitution**. Property is considered inviolable. Article 21 of the Constitution states: "The right to inherit and own property is recognized and guaranteed. The abrogation of the universal right of property, its acquisition, transfer and inheritance is prohibited."

**Civil Code** also contains regulations with an impact on ownership and ownership rights. These regulations concern legal rights on acquisition, transfer and inheritance of real estate. According to the Civil Code, property is any object and nonmaterial asset, physical and legal entities can own, use, dispose and acquire if it doesn't violate law and doesn't oppose moral principles. The Civil Code ensures the freedom of trading of property rights with the rule established by law. Chapter 3 of the Georgian Civil Code envisages inheritance of ownership rights.

**Law on Privatization of State-owned Property of 1997** determines legal, economic, organizational and social principles of privatization of the state-owned property, as well as basic terms of privatization and ensures the purchase of state-owned property by physical and

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legal persons or their unions. The aim of the law is to ensure formation of such ownership relations that will promote the efficient and socially oriented market economy. This law doesn't regulate privatization of land and state housing funds.

*The ownership right on land is further protected by various laws enacted by the Parliament:*

**Law on Agricultural Land Ownership adopted 1996** regulates relations related to ownership of agricultural land. The aim of the law is a) to legally ensure farms organized based on rational use of land and improve agrarian structure, b) to prevent fragmentation and irrational use of land parcels. The law determines: a) the rule for acquisition and alienation of agricultural land parcels and local estate farms, b) participation of the state in regulation of relations regarding agricultural land parcels. The law states that agricultural land is transferred in ownership only to a citizen of Georgia. A person without Georgian citizenship and citizen of a foreign country shall receive agricultural land only under lease.

**Law on Land Registration adopted 1996**, regulates rules and terms for the registration of origin, transfer, restriction or suspension of rights to a plot of land and the immovable property associated with land.

**Law on Declaration of Private Ownership of Non-agricultural Land in Use of Physical and Private Legal Persons adopted 1998** recognizes ownership rights of these persons on nonagricultural land existing in their use.

In accordance with the existing legislation, the landowner can alienate, or in other words, sell, buy, give as a gift, bequeath, mortgage or lease the land parcel existing in his ownership. The landowners have the right to use the land and related real estate according to their own interests. Ownership of real estate also carries with it certain obligations, however, such as the payment of property taxes, the observance of building and zoning codes and environmental protection laws, the avoidance of unreasonable interference with the rights of neighboring owners, and so forth.

The Georgian legislation (The Constitution of Georgia, Article 21 and the Law on expropriation procedures of ownership for public necessity of 1999) envisages the depriving of ownership through expropriation for social necessity. Expropriation is accomplished on the basis of Presidential Decree and with an accompanying Court decision for the benefit of state body or private legal entity of the private law, who is correspondingly awarded with the right of expropriation.

The expropriation necessary for the social necessity is permissible in order to carry out the following activities:

- Construction of road or main highway;
- Installment of railway tracks;
- Construction of electricity transmission and distribution lines;
- Installment of telephone networks; and
- Other similar projects and activities.

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An agency or person, who is exercising this right, must deliver information, which is published in central or relevant local press, to every landowner whose property is subject to expropriation. The authorized Expropriator, who has been awarded with the right of expropriation, must agree in advance upon the amount and timing of the compensation to be paid to the owner of the property.

### **3.3. The impact of current land issues on the poor**

Reforms carried out by the Georgian Government – resulting in the transfer of land into private ownership – have played a definite positive role during the period of crucial economic crisis in the State, and saved the peasantry from starvation. However, the laws passed by the Parliament, as well as the measures taken by the executive authorities, have not been sufficient: so far, poverty in the country has not been reduced to a sufficient degree. What are the reasons for this fact, and what should be done in future?

Traditionally, land has been one of the major capital assets for households. Land has especial importance for rural households, since on average it contributes 2/3 of their income. This source of income is also important for households living in small villages. Nearly ¼ of their income is received from this source. Moreover, approximately 90% of the country's households have some income from land.

Although wages have begun to contribute a relatively greater proportion of the average incomes of Georgians, they still do not represent as important source of income as income from land. At present, wages provide only 26-30 percent of total incomes for Georgians. Furthermore wages represent a less important source of income for rural households, constituting only 10-12 percent of their income, while being more important for urban households, where wages constitute 38-40 percent of their income. One important fact should also be mentioned: from self-employed in agriculture, 80-85 percent work their own land plots.

The above showings indicate the importance of effective land management and complementary reforms in agriculture for the reduction of poverty in the country. Despite the fact that more than half of the population in the state are involved in agriculture, the authorities of Georgia have not adequately recognized agriculture or rural development as priority fields for national investment and policy development. Hence, there is no state policy that would be oriented on the needs of the farmers. The acting legislation and the executive structures are not flexible enough to become a guarantee of land accessibility.

As a result of privatization carried out in Georgia, 70% of agricultural lands still remain in the state ownership. Privatization of only one fourth of the land also resulted in uneconomic fragmentation of land. Because leasing of land has been linked with corruption, smaller farmers were limited in their ability to gain access to larger areas. As a result, peasants do have land, but not enough to engage in truly profitable agricultural activity, since he can hardly manage to feed his own family and doesn't have a surplus of produce for profitable sale. The leased land has tended to fall into the hands of wealthy and/or influential people. In

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this situation, needy peasants remain as a cheap source of labor, while they have a great potential of becoming wealthy.

There are practically no state subsidies that can be used to “level the playing field”. Peasants and other small farmers cannot get the machinery and other devices, fuel, mineral fertilizers, pesticides, good quality seed and plant materials needed to treat the soil thoroughly and obtain a profitable harvest.

Agricultural products processing industries are not functioning and accordingly there is no demand on the products of peasants.

The current taxation system cannot be considered as a mechanism supporting or encouraging further development of the farming in Georgia. VAT on agricultural products discourages farmers from getting more land.

The existing credit system is not appropriate for the development of agriculture: one-year term credits with high interest rates (18% being the lowest in today’s credit market) are not attractive to small farmers. Furthermore, neither the land nor the village house owned by the farmers is readily accepted by the banks as collateral. Thus, it becomes impossible for the farmers to obtain credit, even on unfavorable terms.

In cases of natural disasters, the farming business is totally insecure. One form of insurance company activity is lacking in the country: insurance of commercial risk.

The low level of farm management theoretical knowledge and training also hampers the rational use of land by the peasant. There are no consultation services in marketing, planning for the farmers. The principles of land reform and knowledge about his property rights and obligations are not always made clear to the farmer. As Poverty Reduction and Economic Growth Program document reports, “there are nearly one million small farmers in the country. Their work could be much more effective if more attention were paid to their training and education”.

The unfavorable social and economic conditions result in psychological problems among farmers, such as Nihilistic approaches to solving the problems, expectation of external help, a common trend in the society that everyday problems will be solved by someone else: i.e., the state has to solve them.

In order to enable land policy to have positive impacts for the poor, agrarian reform is required as the problems associated with rational land use result largely from unfavorable conditions of agriculture sector in the country.

Agrarian reform—if it leads to effective agricultural production and income—has great potential to reduce poverty. If the greatest possible number of small farmers will have an opportunity to make profit using their land, whereas the great number of farmers cannot currently do, it will have a strong influence on reduction of poverty.

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## Part 4. Characterizing the Recent Status of the Land Market

### 4.1. General overview of the land market

The transfer of land and related real estate from state possession into private ownership, the legal declaration of the rights and obligations of private ownership, and establishment of a system of simple and efficient land title registration has facilitated the process of formation of Georgia's land/real estate market.

The land market is more actively developing in urban areas. Generally its formation varies across regions or rayons. The dynamic of land market development is higher in those rayons where tourism/resort development is underway, as well as in regions where it is possible to establish agricultural activities that are based on the cultivation (and processing) of high-value agricultural crops.

As of January 25, 2002, land sales increased by 70% compared to the analogous showings of the previous year. Transactions on non-agricultural land have increased from by 68%, whereas transactions accomplished on agricultural land parcels have increased by 71%. The table below depicts the growing tendency of land market development.

Table 1. Data on land sales transactions as of January 2001 and 2002

Year	Number of land sales transactions		
	Total	Non-agricultural land	Agricultural land
As of January,2001	4,456	1,828	2,628
As of January,2002	10,877	4,517	6,357

As a result of privatization about less than 30 percent of agricultural land have been transferred into private ownership. About 35 percent of agricultural land left in state ownership are leased. The leased lands are the best quality land parcels and do not represent the part of the land market. In most cases privileged persons have gotten hold of these lands and do not even cultivate them. To date if an entrepreneur is interested in maintaining the agribusiness and he needs land, it is easier for him to take land in lease through giving the bribes, than to buy land from private owner. In addition the process of leasing the land and then monitoring is very non-transparent and corrupted. Similarly, there are state-owned agricultural land, which are not even leased left out of the market and legislation doesn't envisage the possibility to additionally purchase land from the state. The privatization of those lands will significantly support the development of land market.

#### *The accessibility of the information on real property for sale*

The growth of the real estate market will demand access to reliable information on real estate for sale. At present, the most widespread way of obtaining information about real estate is to read advertisements placed in the newspapers. From this point of view, the activity of

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brokerage firms is also noteworthy. Presently, real estate brokerage firms can be classified into three main groups:

- Well-known agencies, with 8-10 years of working experience, including
  - Members of Real Estate Association of Georgia
  - Independently functioning agencies
- Medium size agencies, which have small staff (usually, about 2-3 agents), small offices, and only 2-3 years of experience
- Officially unregistered brokers
  - Agents, so-called “black brokers” (who work on the street market and have some experience)
  - “Newly baked” brokers, who have decided to work in this field because they have not been able to find any other profitable job. Their experience and knowledge is extremely limited.

The most prestigious agencies (category one) having certain professional experience tend to concentrate their work on the sales of higher-value real estate which tends to yield the best commissions. However, since the majority of the population cannot afford to purchase this kind of property, they are forced to use the services of the non-professional brokers or street brokers. Due to the low professionalism of mediators and their ignorance of the recent changes in land legislation, their information is often inaccurate or not complete, and may lead to the development of legal disputes among parties involved in a particular real estate transaction.

The relevant local government body and the relevant territorial organs of the Ministry of State Property Management provide information about the disposition of state property. Information about any state property which is to be sold through competitive bidding, auction, lease-buy back, or direct sale is published in the official publication of the Ministry of State Property Management, or in the local press (if privatization is accomplished by the territorial body of the Ministry of State Property Management). At the same time, other means of information can be used. Information should be published at least one month before the date set for the privatization of state property. The published information should include the address and land area covered by the premises to be privatized, a thorough description of the buildings located on them, and the terms for selling the property. In case of necessity, additional information is delivered to the buyer.

The publishing of information on selling of state land through competition or auction is organized by the territorial body of the State Department of Land Management, which in agreement with local architectural agencies, obtains and registers applications from interested purchasers. During the two weeks after receiving an application, the SDLM office informs the applicant through a written notice that its applications have been received. After publishing the information, the SDLM office allows all interested persons to preliminarily acquaint with the land parcel and for this they create necessary conditions.

#### **4.2. Land Registration and cadastre**

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A land cadastre is a set of data about a) landowners and users, b) the nature of their interest in land (e.g. owner's title, type and duration of rights, restrictions, and responsibilities), and c) land parcels (e.g. location, boundaries, size, and improvements). A cadastre may also contain some other data, such as land value, land use, soil fertility, etc. Therefore it can be a strong and effective tool in the hands of government, society and individual landowners to plan, manage and control land/real estate market.

At present, it is possible to list progress made in recent years towards the creation of a cadastral database:

- Aerial surveys of the major part of the country have been obtained;
- Legal registration of land and property is proceeding intensively; and
- Application of cadastral data for the purposes of physical/town planning, real estate valuation, and bank mortgages has started.

Land registration is one of the crucial components of Georgia's land cadastre. Public Registry should possess all necessary records on the boundaries, as well as the quantitative-qualitative and legal conditions of the land parcel or related immovable property. In accordance with current legislation, legal rights pertaining to the land or related real estate are subject to obligatory registration. State registration in Georgia is accomplished through the unified system of record maintenance determined by law in the Public Registry.

Due to the lack of a public registration system during the early years of the land privatization process in Georgia, landowners were not able to fully protect and use their rights, such as: sales, lease, mortgage and similar rights. In 1996 the Parliament of Georgia adopted the Law "On Land Registration" and later, in 1997, a new Civil Code, which has made possible the conduct of various transactions on land.

To accelerate the registration process, in May 16, 1999 the President of Georgia issued Decree No: 327 "On Urgent Measures for the Initial Registration of Agricultural Land Ownership Rights and Issuance of Registration Certificates to Citizens of Georgia".

On the basis of this Decree, it was made possible to:

- Significantly hasten the process of initial registration of agricultural land parcels and to accomplish the registration process throughout the whole territory of Georgia;
- Greatly reduce the cost to of private owners to complete the initial registration of private ownership right on land, (since the Decree mandated that the initial registration of land parcels for the citizens of Georgia should be accomplished free of charge);
- More easily accomplish legal and unimpeded secondary transactions on agricultural lands (sales, lease, hypothec, etc).

The responsible agency for land registration, as well as land cadastre is SDLM.

The chief registrar of SDLM administers land cadastre and registration. The SDLM has one central office, 62 rayon and 7 urban offices. These offices are supervised by zone registrar,

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responsible for operations in zone and other registration activities. The distribution of functions between rayon and regional offices is not complete.

There is no fee established for initial registration. The registration fee for secondary registration has been reduced to 7 GEL from 26 GEL, because the latter was considered to be high taking into account the average income of Georgian citizens.

The cheap, fast, effective and simple registration system created in Georgia allows both physical persons, as well as legal entities, to accomplish the unimpeded registration of ownership rights on a specific land parcel, after submitting the relevant documents and paying the fee established by law. However because of corruption and low qualification of registrars, citizens cannot fully benefit from positive outcomes.

### **4.3. Valuation System**

Valuation practices in Georgia are regulated in accordance with the Law on Auditory Activities of 1998. A Statement of Appraisal becomes a legal document only if the appraiser (either a company or individual) is officially licensed by the state. The state licensing body is Council of Audit under the Parliament of Georgia (particularly under the Committee of Budget and Finance). The Council of Audit is the governmental structure responsible for issuing licenses for the exercise of valuation activities.

The Council issues three types of licenses: 1) General Audit; 2) Banking Audit; and 3) Insurance Audit. The last two licenses involve financial audits of banks and insurance companies exclusively, therefore, the License for General Audit covers all other types of audits, starting from the audit of businesses' financial activities to the appraisal of real estate or other property.

In the Georgian legal system, the term “appraisal” is identical to the term “audit. In other words, the entities licensed by the Council are equally eligible to conduct audits of financial statements and to appraise property.

The License for General Audit covers a wide range of activities. Many auditors claim that the structure of licensing is far from being perfect and needs serious reformation. The problem is aggravated by the absence of recognized appraisal standards. Auditors also note that, since low qualifications are widespread, the prestige of the profession and trust of clients is decreasing very rapidly.

There are currently about 400 licensed individuals and about 200 companies that operate under the General Audit License.

Unfortunately, the majority of these license holders have low qualification. These auditors conduct “pro forma” audits for small businesses that are required to include the findings of an independent auditor in their annual financial statements – otherwise, the State tax inspection cannot legally receive their statements. In such cases, the typical auditor charges \$25-\$100

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and signs a standard conclusion without even looking at company's financial documents. Since many small companies exist in Georgia, the demand for such conclusions is large enough to support a fair number of Auditors. Auditors of low qualification make more than 80% of their annual income from this activity.

It is estimated that only about 10% of all licensed Auditors have appropriate professional qualifications and are qualified to perform international quality appraisals. Most of them have either joined an established auditing company or founded their own. Such auditors serve rich companies, international organizations, foreign investors: i.e., those clients who can afford to pay enough to receive professional services.

Auditing companies note that less than 20% of their income is collected from the fees charged for real estate appraisals. Some have mentioned that if modern standards are not introduced and their personnel are not relevantly trained, that share of income is going to decrease due to the low demand. Since recognized standards have not been introduced, today's appraisal practice is based on the roughest calculations and in many cases the final figure is far from being realistic. Such practices have decreased the client's trust in auditors and in the Georgian appraisal practice in general.

Many auditors suffer from the pervasive corruption at the Council of Audit. Illegal practice include forcing potential licensees to pay for training services provided by the Council; afterwards, candidates are forced to pay unofficial fees for passing state examination (actually they have to pay twice – once for written test and again for the verbal exam). The management of Council eagerly receives “gifts” from licensees, and the “privileged” auditors are more welcomed than regular ones after two years, when a license expires.

According to the unofficial information, auditors must spend up to 2 000 GEL (\$900) in official and unofficial fees to obtain a license. However, for the consumer, the major problem is not the high fees, but the low qualification of licensees who pay for knowing nothing.

As mentioned above, the Council has its own training program that potential licensees are forced to attend. Auditors note that the low quality of training is offered only for financial audit and not for appraisal practices. Certainly this is natural, as the Council does not have any standards for appraisal, and this is not the problem of the Council only – all auditors admit that there are no recognized standards for conducting appraisals.

The Civil Code of Georgia defines and regulates a number of economic and legal transactions that take place everyday in the country. Today, there are several common transactions in the country that necessitate appraisal service. However, the growing number of real estate and other transactions in Georgia are rarely accomplished with the use of appraisal services.

Number of problems arises from the absence of an appraisal, or the provision of unqualified valuation services. Many of the problems identified below are caused by non-existence of modern appraisal standards in the country.

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**Prices Understated.** Real estate transactions (such as resale, mortgage, lease etc.), when officially registered, oblige one of the parties of transaction to pay 2% of the agreement price to the state budget. In order to minimize the amount of tax payable, the parties engage in unofficial agreement to report reduced agreement prices. Generally, if an appraiser is used, he must participate in this subterfuge.

**Market vs. Book Value.** Very often investors and other interested parties want to know the value of a certain enterprises' assets. There is a very significant difference between market (real) value and the book value of assets. In many cases book values are significantly overstated, and such figures become useless for investors.

**Collateral Value.** Through international credit lines and already with their own financial resources, Georgian banks have made credits more readily available to entrepreneurs. All credit transactions involve collateral (real estate is the most common collateral) that is appraised by the credit officers of the banks, even though this is an inherent conflict of interest. Services of independent evaluator are rarely, if ever, used.

**Other Activities.** There are other activities that currently use appraiser's service, but unfortunately these services are generally conducted by unqualified personnel. Such activities are foundation/liquidation of companies, court decisions, heritage, expropriation etc.

Considering the fact, that the number of real estate transactions is increasing, the problems described above are going to become more acute.

#### **4.4. Financial services**

##### The use of non-agricultural and agricultural land as security and for credit

As a result of successful implementation of land reform, land and real estate has increasingly become part of the market turnover as liquid assets. As a result, banks and credit associations have gotten more actively involved in the land market. A significant position within the credit portfolios of the leading banks of Georgia is currently occupied by land and related real estate, which represent their main guarantee for loans.

Funds received based on a hypothec agreement enable owners to upgrade technical means, purchase necessary raw materials, and expand their farms or their production process.

Since enactment of the relevant legislative basis, in particular the "Law On Declaration of Private Ownership of Non-agricultural Land in Use of Physical and Private Legal Persons," the total number of the hypothec loans on urban land issued by Georgian banks by the end of years 1999, 2000 and 2001 is given in Table 1.

Table 1. Hypothec loans issued by the end of years 1999, 2000 and 2001

	Since enactment of the Law – by the end of 1999	By the end of 2000	By the end of 2001	January 2002
Tbilisi	435	904	1,745	6,983
Rayons	44	89	728	2,627
Total	479	993	2,473	9,610

In Table 2 is given the number of hypothec loans for each year from enactment of the legislative basis to date:

Table 2. Hypothec loans for each year from enactment of the legislative basis to date

	Oct. 98 – Oct. 99	Oct.99 – Jan. 00	Jan. 00 – Jan. 01	Jan. 01- Jan. 02	Total
Tbilisi	435	469	841	5,238	6,983
Rayons	44	45	639	1,899	2,627
Total	479	514	1,480	7,137	9,610

By years, the following percentage share of issued hypothec loans is covered by Tbilisi:

Oct. 98 - Oct. 99	- 90.81%
Oct. 99 - Jan. 00	- 91.25%
Jan. 00 - Jan. 01	- 45.71%
Jan. 01 - Jan. 02	- 73.39%

Despite the fact that the larger share of financial capital issued on the real estate market as hypothec loans is accumulated in the capital, Tbilisi, the regions of the country are also becoming more involved in this process. If in 1999 the total number of hypothec loans issued in regions was 44, by January 25 of 2002 this number increased to 1,899.

It is noteworthy that banks are more interested only in non-agricultural land. Agricultural land existing in ownership of farmers and village houses are only rarely accepted by banks as collateral.

For the past several years, six branch offices of the ACDI/VOCA--a private, nonprofit organization offering favorable credits for the development of agriculture—have been operating throughout Georgia. However, one-year credits with an 18% annual interest rate are still not adequate for the financing needs of most peasants and farmers, since few can afford them.

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## Taxation system

Taxation legislation has been subject to frequent amendments. As a result it's no longer systemized legal document. Its unique characteristic is confusing and complex language that leads to legal disputes between Tax Department and taxpayers. The acting taxation system cannot be considered as a mechanism supporting further development of the farming in Georgia. Since on the basis of legislation the farmer, who will decide to process his own produce, to package it, to label it and to sell it, will be taxed as an entrepreneur and will have to pay 20 percent of his produce as VAT tax. Last year minister of Agriculture and Food managed to lobby that the amount of turnover subject to VAT taxation be increased from 24,000 to 100,000 GEL, which has been a significant relief for farmers, especially for small farmers. Furthermore the farmer has to pay another 20 percent of his profit. Such an environment limits he farmer in increasing the size of is farm, on the one hand, and restricts the owners of small processing ventures, on the other.

The practice of neighbor countries can be used as an example for establishing liberal tax policy in Georgia. In Azerbaijan farmer has to pay only one fixed land tax. Apart from this, custom duty on chemical means is equal to zero. The same tariff rate is established in Armenia. Farmers in Turkey also benefit from favorable tax policy and subsidies. It is obvious that agricultural produce of these farmers is cheaper and destroys markets for the Georgian products. In Georgia custom duty on the import of chemical means equals 34 percent, to import of fuel applies custom duty plus excise tax.

The Tax Code of Georgia establishes land and property taxes. The property tax is related to possession of ownership. The tax is calculated and established by the tax inspection department.

The amount of the property tax is different for persons and legal entities.

In case of private (physical) persons, the property tax is calculated based on the inventorization value (not the market value) of the property. Criteria for establishing the inventorization value are determined by the body of local self-governance. Relevant criteria include the replacement of the real estate according to square meters, i.e. the inventorization cost of one square meter is determined. Tax inspection evaluates property based on the criteria elaborated by the body of local self-governance and then determines the tax.

The annual amount of the property tax is 0.1% of the inventorization value of the property. Payment is made in two equal parts, by June 15 and October 15 of the tax year.

Legal entities pay the property tax on the balance value of the movable and immovable property, as shown on their accounting balance. The enterprise property tax amounts to 1% of the total balance value of the property. Payment is done once a quarter, in equal parts.

The property tax does not include the land tax, which is paid separately. The land tax rates are determined according to the categories of non-agricultural and agricultural land and relevant zoning classifications. Annual land taxes on non-agricultural land vary from 12 to 36

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tetris (smaller unit of GEL) per 1 square meter. Base rates of the annual tax on agricultural land are differentiated according to administrative units and are determined per hectare in GEL. The land tax is calculated by multiplying the base rate by area of agricultural land in hectares and varies according to land function: e.g. pasture – 3 laris, mowing land – 6 laris, as to the annual tax on arable land, it equals the average of 36 laris per hectare.

In accordance with existing legislation, in order to register the ownership right, an owner needs to fully cover the land tax, including the debt of previous years. Existing legislation does not envisage any benefits, from the point of view of covering the land tax stage by stage. In frequent cases, it is hard for the owner to cover the land tax of previous years at once, and he is obliged to decline to privatize land parcel in use and register his ownership rights.

### Investment climate

Attracting investments is the most important pre-condition for the economic revival of the country and its further development, preceding from the fact that it is the direct and effective way of overcoming the crisis.

At the initial stage of political and economic reforms, Georgia's investment policy was oriented to the foreign investors, proceeding from the fact that local investors had very little resource possibilities. For this purpose, on June 30, 1995 there was elaborated a "Law On Foreign Investments," according to which the favorable tax benefits were extended only on the foreign investors and enterprises founded through foreign investments. This differentiation between foreign and local investors has resulted in:

- Harm to the interests of local investors, particularly small investors;
- Encouraging the flow of domestic capital to foreign countries;
- Significant reduction of competitiveness of those enterprises functioning without the aid of foreign investments.

These factors served as pre-condition for the legislative changes, as a result of which foreign investors have the same rights and protections as "physical persons and legal entities of Georgia". All the tax incentives were abolished. The "Law on Support and Guarantees of Investment Activities," adopted in 1996 and amended in 1998, protects foreign investments from discrimination. The foreign investor independently determines the volume of investments and sphere of investing. He is granted with the guaranteed right to accomplish the repatriation of gained profit, other finances and owned property to the foreign country.

Any investor can open the bank account in GEL, as well as in foreign currency, purchase the assets and securities, and acquire credit from local, as well as foreign banks.

Under the Investment Law the investment itself includes money, stocks and other securities, chattel and real estate, the right of usage of the land and other natural resources (including concessions), patents, licenses, know-how, experience and other intellectual property, as well as other property or intellectual valuables and rights.

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Unlike local investors, law does not award foreign investors with agricultural land ownership right. Whereas the number of laws, having branch specificity, regulate the activity in the spheres of agriculture, energy, transport and tourism. Also, the legislation determines such spheres of activity, where is prohibited the accomplishment of investments.

The rights of foreign investors are protected by international agreements as well. Georgia has signed agreements with various countries “On the Protection and Encouragement of Foreign Investments”. The total amount of investment in the agricultural sector has been very low for the past 10 years. A larger investment share out of the total amount comes on transport, warehousing and communications. The process of real estate privatization without land hindered attracting local investments in agricultural sector. Later this situation was corrected and currently remaining objects are being privatized along with the land parcels located underneath these objects.

There are many potential areas in the country in terms of attracting investments and credits for the development of businesses. Though unstable social-economic situation, non-existence of political will and civil tension cannot create favorable conditions.

Another hindering reason for attracting the investments and maintaining them is the criminal situation existing in the country. Entrepreneurs, businessmen and investors do not feel protected by the state. There are frequent cases of physical assaults, kidnapping for the purpose of money extortion. Police cannot solve any case of kidnapping, which creates a doubt in the public that police and law enforcement bodies are involved and interested in those kidnappings.

If the state will not take urgent measures for guaranteeing the safety of individuals, including structural reforming of the law enforcement bodies, even local investors as well as foreign investors will be discouraged to carry out their activities on the territory of Georgia.

## **Part 5. Integrating Land Issues into the Broader Strategy of Country Development**

### **5.1. Overall land policy**

Land privatization has generally been considered as a significant and successful reform of independent Georgia. Acknowledgement of private ownership rights on land is an important step forward towards the construction of a free democratic state and the development of a viable market economy.

While many improvements are still needed, Georgia has nevertheless achieved a significant success in the establishment of a legislative and regulatory environment for the perfection and protection of property rights. Laws have been adopted which acknowledge and protect private property rights on land and, at the same time, create favorable pre-conditions for the establishment of functioning land market.

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Unfortunately, a broader policy vision targeted on the creation of a comprehensive land management system still does not exist in the country. In 2001, the State Chamber of Control of Georgia inspected the legality and effectiveness of the use of unified fund of land in 1995-2000. The work of all state agencies has been assessed unsatisfactorily. As the Chamber of Control concluded it, the elaboration and implementation of unified state policy of land management has not been achieved.

Often the relevant state agencies ignore the requirements of existing legislation during the decisions made related to the use of unified fund of land. Frequently, established standards of land allocation, function change, or transference through the law are ignored or violated. There are crude violations in leasing of agricultural land, as well as in registration and collection of the lease payment. The local bodies disposing of such agricultural land condone and even encourage the law violations committed by lessees.

In 1995-2000, local governing bodies, with the consent of the State Department of Land Management, have transferred tens of thousands of hectares of highly intensive category lands into comparatively low category lands without carrying out any laboratory or other scientific researches preliminarily.

The Georgian law “On Administration and Disposition of State-owned Non-agricultural Land” has also been massively violated. The local Commissions on Management and Disposal of Non-agricultural Lands do not follow the competition and auction principles. The above-mentioned environment facilitates the creation of careless, non-economical, and in certain case illegal attitudes towards the land fund.

In the absence of a unified state policy of land management, the national strategy of Georgia’s land reform program is no more than the sum of current and planned international donor projects functioning in the sphere of land management.

## **5.2. Integrating land issues into National Strategy of Poverty Reduction and Economic Growth**

In Soviet times absolute poverty was rare in Georgia. The breakdown of the Soviet system not only exacerbated the living conditions of poor, but also created a significant number of newly impoverished households. Disruption of production and trade, hyperinflation, massive unemployment, energy crisis, civil war and forced migration from conflict regions, led to massive poverty. At present more than 60 percent of the population is subsisting below the living minimum. Benefits of social security provided by the state are too small to provide assistance compatible with the current needs of the average Georgian citizens.

Poverty has significantly increased in rural areas. Social infrastructure has suffered a heavy blow. In many villages, day care centers, school and hospitals, have been closed. Road building and repair has been neglected.

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The existing poverty rate in country and its severity indicates the necessity to approach this problem from a long-term perspective, in order to fully and effectively address the issue. This process is closely related to the joint initiative of the World Bank and International Monetary Fund called “Highly Indebted Poor Countries” Initiative and the program of the IMF in Georgia (PRGF). The program began to be implemented on the basis of the Interim Document of Poverty Reduction and Economic Growth Program of Georgia worked out by the Georgian Government with the support of the society at large and approved on November 28,2000. On January 12,2001 the interim document was approved by World Bank and IMF and 3-year program – PREGF was supported, that allowed country to receive 141 billion dollars of favorable credit. The Georgian Government with support of the international organizations and society at large, in line with Interim Document of PRGF, prepared the Poverty Reduction and Economic Growth Program of Georgia, main goal of which is the elimination of poverty, support to economic growth, improvement of social conditions, raising the living standards of the population and ensuring the participation of poor citizens in the country’s development process.

Primary objectives highlighted in the program are:

- Rapid and sustainable economic growth;
- Creation of job opportunities in legal sector of the economy;
- Effective and fair distribution of resources created in the country.

This program is Georgia’s comprehensive short-term as well as long-term strategy for overcoming the social-economic crisis in the country and supporting its further development.

At this point in time, this program is only a discussion document prepared by special working group and provided for consideration to society at large. It must now be made operational, with specific assignments of responsibility to State authorities, private parties, and international donors. In addition to the assignment (and acceptance) of such responsibility, clear and measurable targets need to be established, and concrete allocations of budgetary resources will also be needed to convert the “paper plan” into a realistic plan for action.

Statements from non-governmental organizations, local and foreign experts, donor organizations, and citizens will be considered in drafting the final strategic document of Poverty Reduction and Economic Growth Program, the implementation of which will serve to overcome the existing social-economic crisis and ensure economic development.

For the purpose of the Poverty Reduction and Economic Growth Program, special attention must be paid to the following land management measures:

- Undertake further privatization of vacant state-owned agricultural lands - total area 100.6 thousand hectares, of which: 48.0 thousand are arable land, 20.7 thousand hectares - land under perennials, and 31.9 thousand hectares - grasslands;
- Undertake privatization through purchasing of rented agricultural lands, which were leased by the State - total area 259.7 thousand hectares, of which: 178 thousand hectares area arable land, 22.6 thousand hectares land under perennials, and 59.1 thousand hectares - grasslands;

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- Introduce a relevant cadastre and registration system for the country and further improve the corresponding legislative base;
  - Elaborate the State's targeted program of soil fertility upgrading and identify sources of finance;
  - Develop a viable land and real estate market through the involvement of banking and insurance system and establishment of private institutions of real estate evaluators, soil specialists, surveyors and lawyers.

Effective land policy can be a foundation for bringing about renewed agricultural growth. Deriving from the volume of agriculture and the number of people employed in it, PRGP recognizes development of this sector as having an important role in the economic growth of the country. Since agriculture and agricultural business represent one of the major sources of income of the population, agrarian reforms along with measure for improved land management are considered to be important factors for alleviating rural poverty.

Main directions for development of the agriculture sector, as highlighted in the document, are:

- Develop rural infrastructure and re-equipment and restoration of inputs and material-technical basis. Taking into consideration the lack of State financial resources, practical steps towards attraction of foreign investments should be made in order to ensure rehabilitation of irrigation and drainage nets, main structures, magisterial and distribution channels, and pumping stations.
- Establish Water Users Associations (WUA) that will privatize small farmland schemes on the first stage. The next step requires privatization of secondary schemes by WUAs. Hence, the State will preserve its responsibility on maintaining only the main schemes that will save significant financial resources.
- The material-technical basis is in a distressing situation and it requires provision of agricultural machinery and trailers for farmers in the framework of active participation of donor countries and organizations; it is also important to establish a favorable business environment for private investments and to focus on purchasing of large amounts of comparatively cheap and qualitative agricultural machinery, that will give possibility to service-centers to renovate depreciated machinery in several years. Establishment of private and mixed service-centers in the regions will be useful for this purpose.
- The development of agro-processing enterprises, which represent a link between farmers and credit institutions, is also a measure of great importance. Attention should be paid to the enlargement of the local goods market that can be achieved through a policy oriented on improving product quality and safety. It is essential to strictly control useful and dangerous material tolerance in the products.
- In order to preserve soil fertility it is necessary to conduct soil research and to develop appropriate recommendations. It is essential to use efficiently agricultural machinery and technologies, to introduce crop rotation, proper utilization and protection of soil, and to elaborate a seed rotation system suitable for small farms.
- The formation of a Rural Credit Policy is a means to promote sustainable entity formation, to establish Guarantee Funds, to raise the interest of Credit Unions' towards the Agriculture Sector, and to introduce insurance mechanisms, etc. This will reduce the risk factor that is a heavy burden on poor people employed in the Sector.

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Stimulation of the process for creation of rural savings and re-investment should be ensured.

- It is reasonable to optimize existing tax and customs regime in accordance with the WTO regulations.
- It is necessary to conduct a targeted regional policy envisaging specificities of the Sector development within a regional framework. Establishment of regional and district consulting centers for farmers will increase business awareness of micro, small and medium enterprise holders (including farmers). Special attention should be paid to the elaboration of special program of poverty elimination in highland regions and its phased implementation.

One of the priority directions of economic reform proceeding in the country is considered to be restructuring of the agrarian sector and land reform. Efforts to making the farmer's labor easier and making his farm more profitable will be the basis of poverty reduction.

### **5.3. The degree of coordination between and support from the donor community**

The donor community has made an enormous contribution to the progress Georgia has achieved in the privatization of land, in creating and developing an infrastructure for the registration of rights on immovable property, and for the emerging land market.

The USAID Land Market Development Project in Georgia commenced in October 1997 as part of USAID Caucasus Mission program which promotes a stable, prosperous market-oriented economy that empowers citizens, is governed by rule of law, and promotes basic welfare. The initial phase of the project focused on assisting the Georgia SDLM and other government bodies to form and develop the legal and regulatory framework for land privatization and registration. The objectives of the project also included:

- Supporting the privatization of land and developing registration and titling procedures;
- Constituency building and provision of public education related to land privatization.

The initial works of the USAID included participation in the process of initial registration of agricultural land parcels previously allocated on the basis of 1992 land reform, funding of cadastral surveys, preparation of documentation and issuance of ownership certificate to owner.

Private companies that cooperate as contractors with USAID Land Management Project engage in actual activities. Works considered by Land Market Development Project cover almost the total territory of the country, particularly 51 rayons, including highlands.

During the initial phase of work (to the end of 2000), the USAID contractor was Booz-Allen and Hamilton Inc - International Management and Consulting Company. At present Georgian Non-governmental Organization, Association for Protection of Landowners' Rights (APLR) and the US based nonprofit organization, Terra Institute, has replaced the mentioned company.

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Terra Institute, Ltd. under a Cooperative Agreement with USAID will provide financial and project management development in order to position the Association for Protection of Landowner's Rights (APLR) to assume full operational responsibility for; the registration of ownership of agricultural residential parcels, to continue with public education and land market policy work, and to develop a pilot effort for services to mediate among conflicting parties and resolution of legal difficulties of property owners.

Specific responsibilities of Terra Institute, Ltd. to the APLR will include: 1) financial training; 2) revenue supply, financial monitoring and contracting, 3) APLR capacity building 4) land privatization, legal reform, and land market development support, 5) SRO development support, 6) development of real estate and cadastral services associations and 7) resident advisor support.

APLR is a non-governmental organization, founded on October 1996. The principal objective of the association is to provide support for the protection of landowners' rights in the country. In addition the association works to stimulate the development of land reform and to streamline the legal and regulatory framework. Within the USAID Land Market Development Project Association expanded its activities through the country by establishing the regional offices. The rest of works include completion of Initial Registration of Agricultural Land.

By the end of 2001, with support from AID more than 1 300 000 agricultural land parcels and 9800 enterprise land parcels were registered. Furthermore the sale of 2000 enterprise and 3700 agricultural land parcels was supported.

Along with USAID, Georgia receives support from five international donor organizations and countries:

- Cadastre and Land Register Project of Kreditanstalt für Wiederaufbau (KfW) (2000-2006) . The funding of base mapping, cadastral surveys and the establishment of six regional centres.
- Agricultural Development Project of the World Bank and the International Fund for Agricultural Development (IFAD) (1997-2002, possibly extended to 2004). The funding of base mapping, cadastral surveying and registration, and the refurbishment of offices in two rayons.
- Land Management Project (1998-2002) by the United Nations Development Programme (UNDP) and the European Union (EU). The funding of cadastral surveying and registration in one district, software development and the refurbishment of 11 rayon offices. The EU is covering the Government's contribution under its Food Security Programme.
- German Technical Cooperation (Deutsche Gesellschaft für Technische Zusammenarbeit, GTZ) (2001-2002, possibly extended to 2004). The funding of cadastral surveying and registration in Tbilisi.
- Swedish International Development Cooperation Agency (SIDA) (2000-2002). The funding of capacity building by establishing a training centre to provide courses to SDLM employees on land legislation, land registration, land information system

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(LIS), cadastral surveys, valuation and taxation, credit marketing, and office management.

One project that terminated in 2001 was funded by European Commission and granted financial support to the State Department of Land Management. The total of about 11,400,000 GEL was provided to the SDLM to support in the implementation of registration system and encouragement of land market development.

The coordination of donors' projects is the function of State Department of Land Management. The coordination is carried out on the basis of systematic meetings of the representatives of the projects of donor organizations. Projects have strictly determined the sphere and field of their activity. Unfortunately, yet there does not exist a unified cadastral and registration concept and system and each project of donor organization tries to make contribution in the construction of this system. To date it is already achieved that the donors' activities, the spheres and works do not overlap. Unfortunately, in spite of the fact that six donors work on the land issues in Georgia, still there are left certain components of the registration and cadastral system, which cannot be accomplished by the Department independently in the future. The more coordination is necessary, as well as, the change of projects' plans and targets, in order to establish unified cadastral and registration system.

## **Part 6. Conclusions and Recommendations**

### **6.1. The Policy and Regulatory Framework**

#### *6.1.1. The legislative framework of secured property rights*

The successful outcomes of the land reform carried out in Georgia included the formation of relevant legal framework for the exercise of ownership rights on land.

Ownership rights on property are recognized and guaranteed by the Constitution of Georgia and the Civil Code of Georgia that ensures freedom of trading of property rights by individuals or legal entities engaging in sales or lease transactions. Also it envisages the right to inherit property rights. However the legislation (Constitution of Georgia, Article 21 and the Law on Expropriation Procedures of Ownership for Public Necessity, 1999) considers the possibility of expropriating property for public necessity. The ownership rights on land are protected by laws: on Agricultural Land Ownership adopted 1996, on Land Registration of 1996 and Law on Declaration of Private Ownership of Non-agricultural Land in Use of Physical and Private Legal Persons adopted 1998. Recently the Law on the Privatization of Agricultural Land Existing in State Ownership has been drafted for parliamentary consideration.

The existing legislative framework allows unimpeded exercise of property rights including rights on land and creates favorable pre-conditions for the establishment of viable land market.

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*Recommendations:*

No further action needed to assure basic legal protection of property ownership rights. Association for the Protection of Landowners' Rights has to make efforts to actively lobby the draft law in legislature.

*6.1.2. Agricultural and urban land management policy*

State does not have the unified program of land management. The national strategy of Georgia's land reform is just the sum of current and planned international projects. The Poverty Reduction and Economic Growth Program of Georgia incorporates measures for improved land management as part of the agrarian reforms prioritised by the program, however it is more essential that this broad strategy be transferred into specific programs.

*Recommendations:*

To assign the responsibility of drafting the strategic plan for the implementation of measures incorporated into Poverty Reduction and Economic Growth Program of Georgia to the State Department of Land Management with agreement of Ministry of State Property Management, Ministry of Urbanization and Construction and Ministry of Food and Agriculture. This can be achieved by setting the timeframe for the submission of the plan and organizing the discussion and coordination meetings of the involved parties.

Drafting the strategic plan for improved land administration will require the broad inter-ministerial as well as civil society and citizen support and coordination and accordingly the interests of the parties have to be satisfied. Significant attention has to be paid to the involvement of non-governmental organizations in the process.

The strategic plan should:

- Identify overall political goals and strategies, and spell out priorities;
- Identify needs and priorities for the legal framework;
- Identify an appropriate distribution of responsibilities among ministries, public agencies at different levels of government and the private sector and propose changes to the institutional structure;
- Propose implementation plan with timetable and budget.

State policy has to consider the decentralization of functions to be carried out for improved land management policy and the establishment of non-governmental organizations in cities or villages that will play important role in the development of local infrastructure and will assist local population in solving the problems. This process is already under way and it is necessary to intensify it. Non-governmental organizations have gained substantial professional experience of working with foreign projects and it is necessary to involve them in reforms and ongoing processes.

*6.1.3. The privatization of the agricultural land remaining in the state ownership*

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As a result of privatization only about less than 30 percent of the agricultural land has been transferred into private ownership. 36 percent are leased out by the state and the rest are neither leased, nor privatized, they just remain in the state ownership.

Today these land parcels remaining in the state ownership are excluded from the land market and do not represent the objects of the market transactions. Those 36 percent of the agricultural land are of high quality and were initially accessed by the influential people and the heads of former collective farms. In most cases they don't cultivate land and sub-lease for long-term period of 49 years. The exclusion of these fertile land parcels from land market will significantly damage the national economy.

*Recommendations:*

It's essential to privatize agricultural land remaining in the state ownership in the shortest period, as it will support the further development of farming in the country. Today 80 percent of the active population in the country are self-employed in the agriculture and the transfer of land parcels to their private ownership will greatly facilitate the progress in overcoming the rural poverty. Privatization coupled with the liberal tax policy and favorable investment policy will benefit the population and country's economy.

Other recommended measures include:

- Actively lobby the approval of the draft law on the Privatization of Agricultural Land Existing in the State Ownership.
- Initiate public awareness campaign to introduce public with the implications of the new draft law. However the privatization of land should go beyond transferring ownership rights to private persons and take into account the necessity of developing the rural infrastructure.

*6.1.4. Secured institutional structures*

There remains considerable confusion, with gaps and overlap, in the assignment of responsibilities among state and local agencies responsible for land administration, land management, and land policy development. Some of the principal problems include the conflicts between the Bureau of Technical Inventorization (BTI) and the Public Registries, and the need to make the land registry independent of political, budgetary, and other pressure or unnecessary constraints.

The SDLM is presently in the process of redistribution of responsibilities between local, rayon and, later on, regional offices.

*Recommendations:*

Encourage a national policy dialogue on the proper organization and coordination of land cadastre, property title registration, land management and related functions, as a precursor to developing an improved institutional structure. Carefully consider and maximize the role of

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the private sector and NGOs in an improved institutional context, in cooperation with relevant public agencies.

The SDLM has to make final decision in the shortest period of time on redistribution of responsibilities between local and regional offices. Decision should be based on analysis of the level that envisages the concept of a “front-office/back-office” organization (the front office being small local units for customer services and the back office being bigger regional working groups).

#### *6.1.5. Agricultural products processing industry*

Although peasants possess some area of land parcels, they can sell only small fraction about 10-15 percent of the harvest on local markets. In order to market, peasant has to go through many bureaucratic and corruption barriers: tax agencies, traffic police, certification and so on.

In the Soviet period the major means for rural population to market their product was agricultural products processing industry. But nowadays these enterprises have ceased their operation, only the smallest part continue to operate, but with out-dated technique and machinery.

Today imported goods dominate local market, 90 percent of which is more likely to be smuggled and falsified. The price of this produce is so low that local products cannot be competitive, for the production of which entrepreneurs pay large amount of taxes and accordingly the self-value of the products increases.

#### *Recommendations:*

Rehabilitation of enterprises and the processing industry will significantly benefit rural population. This will enable them to supply these enterprises with the surplus of produce and get profit. Accordingly it is necessary to support the sale of products produced by these enterprises on both local and foreign markets.

It is important to introduce international standards and experience of certifying agricultural products, so that the export of Georgian produce can be accomplished.

It is necessary to develop transport and packing industry, which will enable the transportation of agricultural produce to neighbouring countries – especially to Russia.

It is true that imported goods have to access market, but state must engage in policy to control the counterfeit and smuggling.

#### *6.1.6. Assistance to the farmers*

Currently farmers and villagers have been left without any attention and assistance by the state. Instead of assistance state hinders activities of the farmers.

Rural population has difficulties to treat the soil properly. The existing technique is out-dated. Farmers need to acquire new land cultivating equipment with favorable terms.

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Agriculture needs pesticides, fertilizers, seeds and etc. Custom duties on these substances are very high and accordingly only smuggled goods are imported which are in most cases of very poor quality and cause negative externalities for farming.

It is worth mentioning that today Georgian farmers are still trying to continue their farming activities based on old Soviet methods and traditions.

In contrary to Georgia, neighboring countries have more liberal policy toward farmers. The Russian government subsidizes 40 percent of production of seed material. That is the reason why the pesticides and fertilizers produced in Russia are cheaper than in Georgia.

*Recommendations:*

The state should find some ways to assist farmers in purchasing new equipment, at least through the assistance of various international donors.

It is necessary to reduce custom duties and create market of pesticides, seed material, so that processing and distributing companies can enter Georgian market.

Establish educational-consultation centres, which will assist farmers in planning their activities, farm management, and financial management. They should be better informed about their capabilities, as well as have information on experience of various foreign and local farmers.

*6.1.7. Land consolidation*

The land area distributed to families during land reform was not exceeding 1.25 ha. One household was allocated 4-5 land parcels located in different areas. As these parcels were not apt to be contiguous, fragmentation resulted. Large number of small inefficient farmers was formed. Fragmented land is of poor quality and is not accepted by banks as collateral. Land consolidation is an effective means to improve agricultural production and working conditions.

*Recommendations:*

- Set up an inter-ministerial task force for land consolidation ;
- Draft a Land Consolidation Act ;
- Initiate public awareness campaign for the rural population and the decision-makers at various levels to have clear understanding of the potential contribution of land consolidation ;
- Key players would have to undergo training in land consolidation and spatial planning ;
- Pilot projects should be carried out to gain experience with the different approaches and procedures in land consolidation at community level.

*6.1.7. Rural development*

An important precondition for alleviating rural poverty is improvement of the rural infrastructure, which has been deteriorated largely for the next ten years. It will serve as a

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basis for improving the standard of living in rural areas. In this way it will be possible to stop the migration from rural areas and urbanizing of a few cities.

*Recommendations:*

The development program for rural areas should contain at least the following elements:

- Building or maintenance of roads, water supply, power supply ;
- Renewal of community facilities, such as school buildings, hospitals, etc. ;
- The development of transport infrastructure ;
- The development of telecommunication facilities ;

## **6.2. Land Registration and Cadastre**

There is no independent agency for land and real estate registration. On one hand the specific function of administering and disposing particular state property and on the other hand land registration function are not differentiated from one another.

The unified system of the registration of property rights has not been maintained as a result of conflicting responsibilities of SDLM and BTIs. Information on land and related building-constructions is spread among registration offices and BTI. There are cases of information duplication, which threatens the reliability of this information about the ownership and endangers owners as well.

The creation of cadastral systems is held in fragmentary way, as particular areas significantly differ from each other, and it doesn't refer to the effectiveness of the existing cadastre, which lacks features of an unique system.

*Recommendations:*

Establish an independent agency of land registration and cadastre, the registrars of which will not be subject to any pressure and will follow only the rule established by law and not bureaucratic directions.

The issuance of Presidential Decree requiring BTIs to undertake urgent measures for the transferring the data they hold to the SDLM in order to allow the formation of Public Registry as the sole source of public information on real estate.

## **6.3. Land markets/financial services**

### *6.3.1. Taxation system*

Taxation legislation is confusing and complex, as since the adoption of Tax Code huge number of amendments have been incorporated in it each year, so that it's impossible for the taxpayers to keep pace with constant changes.

Tax implications for people involved in agricultural activities are not favorable for the development of farming in the country.

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*Recommendations:*

Involve business associations in cooperation with local and international experts in drafting alternative Tax Code. Free the farmers from value added tax, introduce the progressive profit tax altering the tax brackets.

*6.3.2. Credit systems*

Credits are hardly accessible for farmers/peasants and demand very high interest rates. Banks do not accept agricultural land as collateral.

*Recommendation:*

- With the support of National Bank attract the favorable foreign credits at lower interest rate.
- Create the credit institution specializing in funding the agricultural activities.
- Assign the responsibility of managing international grants and credits to the non-governmental organization acting as contractor to the donor organization.
- Promote the development of credit unions.

*6.3.4. Valuation system*

Council of Audit is a state agency responsible for issuing licenses for valuation activities. One of the problems identified in performance of auditors is the fact that they accept bribes when auditing business financial activities or appraising real estate. Illegal practice also takes place at the Council of Audit, which requires candidates to pay unofficial fees for passing state examination and for training services. General audit – most common type of license covers broad range of activities, granting license holder too much discretion. Wide range of economic and legal transactions require appraisal service, however people avoid to use it, parties in agreement report reduced property prices in order to minimize the amount of tax payable.

*Recommendations:*

- Specify the activities covered by the General Audit.
- Adopt legislation regulating appraisal activities in separate with audit activities.
- Introduce general appraisal standards, that will assure that appraisal activities be conducted on the basis of some broadly accepted principles, and not on the roughest calculations.

*6.3.5. Investment policy*

The complex tax policy of the country and hard criminal situation hampers the attraction of investors. Kidnapping takes place frequently. If businessman doesn't have political patronage, he has no chances of successful business. Due to the same reasons internal investments are flowing out of the country.

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Law on Support and Guarantees of Investment Activities of 1996 protects foreign investors from discrimination placing foreign and local investors in equal conditions. However deriving from national interests, legislation doesn't allow foreign investors to privatize agricultural land and define areas in which investment activities are restricted. However political instability, civil unrest and poor economic and social conditions in the country hamper attraction of investments.

*Recommendations:*

State Government and Parliament has to facilitate efforts toward creating the favorable investment environment. Corruption in state agencies has to be diminished or overcome, bureaucratic systems have to be reduced and simplified, executive branch of the government have to be reorganized, donor supported reform programs must be completed, serious police reforms have to be undertaken. Without the above mentioned, investing capital in the country will simply be inexpedient for investors.

Publish material informing interested parties about the particular potential investment areas, introduce interested parties with tax implications they may encounter in the course of their activities, hold and actively participate in international conferences. The Consulting Council of Supporting and Encouraging Investments of Georgia can undertake these measures. Council has to intensify efforts toward perfecting fiscal and tax policy as important preconditions for attractive investment climate, creating favorable economic and legal environment for grants and credits and offering services for interested parties to overcome the bureaucratic and legal barriers.

It is important to facilitate development of insurance companies in the country, that especially will offer insurance service for natural disasters and meteorological phenomena in agriculture sector as well as insuring production risk.

## Annex I. Quick links about Georgia

<b>Geography</b>	
<b>Location</b>	Southwestern Asia, bordering the Black Sea, between Turkey and Russia
<b>Area</b>	26,911.32 sq mi 69,700.00 sq km
<b>Climate</b>	warm and pleasant: Mediterranean-like on Black Sea coast
<b>Terrain</b>	largely mountainous with Great Caucasus Mountains in the north and Lesser Caucasus Mountains in the south; Kolkhet'is Dablobi (Kolkhida Lowland) opens to the Black Sea in the west; Mtkvari River Basin in the east; good soils in river valley flood plains, foothills of Kolkhida Lowland
<b>Natural resources</b>	forests, hydropower, manganese deposits, iron ore, copper, minor coal and oil deposits; coastal climate and soils allow for important tea and citrus growth
<b>Land use</b>	<i>arable land: 11.5%</i> <i>permanent crops: 4.3%</i> <i>permanent pastures: 25.8%</i> <i>forests and woodland: 43%</i> <i>other: 15.4%</i>
<b>People</b>	
<b>Population</b>	4,900,000 (2002 est.)
<b>Age structure</b>	<i>0-14 years: 19.59% (male 498,575; female 478,663)</i> <i>15-64 years: 67.91% (male 1,632,338; female 1,755,910)</i> <i>65 years and over: 12.5% (male 241,824; female 381,975) (2001 est.)</i>
<b>Population growth rate</b>	-0.59% (2001 est.)
<b>Birth rate</b>	11.18 births/1,000 population (2001 est.)
<b>Death rate</b>	14.58 deaths/1,000 population (2001 est.)
<b>Net migration rate</b>	-2.48 migrant(s)/1,000 population (2001 est.)
<b>Life expectancy</b>	<i>total population: 64.57 years</i> <i>male: 61.04 years</i> <i>female: 68.28 years (2001 est.)</i>
<b>Total fertility rate</b>	1.45 children born/woman (2001 est.)
<b>Nationality</b>	Georgian
<b>Ethnic groups</b>	Georgian 70.1%, Armenian 8.1%, Russian 6.3%, Azeri 5.7%, Ossetian 3%, Abkhaz 1.8%, other 5%
<b>Religions</b>	Georgian Orthodox 65%, Muslim 11%, Russian Orthodox 10%, Armenian Apostolic 8%, unknown 6%
<b>Languages</b>	Georgian 71% (official), Russian 9%, Armenian 7%, Azeri 6%, other 7%

<b>Literacy</b>	99% of the total population (1989 est.)
<b>Government</b>	
<b>Government type</b>	Republic
<b>Capital</b>	Tbilisi
<b>Administrative divisions</b>	53 rayons (raionebi, singular - raioni), 9 cities* (k'alak'ebi, singular - k'alak'i), and 2 autonomous republics
<b>Independence</b>	9 April 1991 ( from Soviet Union)
<b>Constitution</b>	adopted 17 October 1995
<b>Executive branch</b>	<i>chief of state:</i> President Eduard Amvrosiyevich SHEVARDNADZE. The president is both the chief of state and head of government <i>elections:</i> president elected by popular vote for a five-year term; election last held 9 April 2000 (next to be held NA 2005)
<b>Legislative branch</b>	Unicameral Parliament
<b>Judicial branch</b>	Supreme Court (judges elected by the Supreme Council on the president's recommendation); Constitutional Court
<b>International organization participation</b>	BSEC, CCC, CE, CIS, EAPC, EBRD, ECE, FAO, IAEA, IBRD, ICAO, ICFTU, IDA, IFAD, IFC, IFRC, ILO, IMF, IMO, Inmarsat, Interpol, IOC, IOM (observer), ITU, OPCW, OSCE, PFP, UN, UNCTAD, UNESCO, UNIDO, UPU, WHO, WIPO, WMO, WToO, WtrO
<b>Economy</b>	
<b>Overview</b>	Georgia's economy has traditionally revolved around Black Sea tourism; cultivation of citrus fruits, tea, and grapes; mining of manganese and copper; and output of a small industrial sector producing wine, metals, machinery, chemicals, and textiles. The country imports the bulk of its energy needs, including natural gas and oil products. Its only sizable internal energy resource is hydropower. Despite the severe damage the economy has suffered due to civil strife, Georgia, with the help of the IMF and World Bank, has made substantial economic gains since 1995, increasing GDP growth and slashing inflation. The Georgian economy continues to experience large budget deficits due to a failure to collect tax revenues. Georgia also still suffers from energy shortages; it privatized the distribution network in 1998, and deliveries are steadily improving. The country is pinning its hopes for long-term recovery on the development of an international transportation corridor through the key Black Sea ports of Poti and Batumi. The growing trade deficit, continuing problems with tax evasion and corruption, and political uncertainties cloud the short-term economic picture.
<b>GDP</b>	6505,2 million GEL (2001est.)
<b>GDP – real growth rate</b>	4.3% (2001 est.)
<b>GDP – composition by sector</b>	agriculture: 19.2% trade: 12.8% industry: 12.5% transport: 11.0 (2001 est.)
<b>Population below poverty</b>	60% (2001 est.)

<b>line</b>	
<b>Labor force</b>	3.08 million (1997)
<b>Labor force by occupation</b>	industry 20%, agriculture 40%, services 40% (1999 est.)
<b>Unemployment rate</b>	11.4% (2001 est.)
<b>Budget</b>	<i>revenues: 959,7 million GEL</i> <i>expenditures: 795,6 million GEL (2001)</i>
<b>Industrial production growth rate</b>	-0.3% (1998 est.)
<b>Electricity production</b>	7.975 billion kWh (1999)
<b>Electricity production by source</b>	<i>fossil fuel: 20.38%</i> <i>hydro: 79.62% (1999)</i>
<b>Agriculture - products</b>	citrus, grapes, tea, vegetables, potatoes; livestock
<b>Exports</b>	\$320,0 million (2001 est.)
<b>Exports - commodities</b>	citrus fruits, tea, wine, other agricultural products; diverse types of machinery and metals; chemicals; fuel reexports; textiles
<b>Imports</b>	\$684,1 million (2001 est.)
<b>Imports - commodities</b>	fuel, grain and other foods, machinery and parts, transport equipment
<b>Major trading partners</b>	Turkey 17.3%, Russia 16.4%, Azerbaijan 8.3% (2001 est.)
<b>Debt - external</b>	2 900,5 million GEL (2001)
<b>Currency</b>	lari (GEL)
<b>Exchange rates</b>	\$1 - 2.235 (March 2001)

SOURCE: 1. World Factbook [On-line]. Available:

<http://www.cia.gov/cia/publications/factbook/geos/gg.html>

2. State Department of Statistics. Social-Economic Indicators of Georgia. Tbilisi, 2001.

## Annex II. References

<b>1</b>	State document	Poverty Reduction and Economic Growth Program of Georgia, material for discussion. Tbilisi, November, 2001
<b>2</b>		The Constitution of Georgia. Tbilisi, 2001
<b>3</b>		Tax Code of Georgia. Tbilisi, 2000
<b>4</b>	The State Department of Land Management	The collected legislative articles on Land of Georgia. Tbilisi, 2001
<b>5</b>	FAO and UNDP Land Management Project in Georgia	Strategy for Land Consolidation and improved Land Management in Georgia, pre-feasibility study. Tbilisi, 2001, December
<b>6</b>	Association of Biological Farming – Elkana; the Ministry of Agriculture and Food of Georgia and Association for the Protection of Landowners’ Rights	Agrarian reforms in Georgia _ Reality and Perspectives, the seminar materials. Tbilisi, 2001, March 8-9
<b>7</b>	William C. Thiesenhusen	Discussion of the draft law prepared for the second phase of land reform and privatization in Georgia. Tbilisi, 2001, December
<b>8</b>	State Department of Statistics	Social-Economic Indicators of Georgia. Tbilisi, 2001
<b>9</b>	Central Intelligence Agency	World Factbook [On-line]. Available: <a href="http://www.cia.gov/cia/publications/factbook/geos/gg.html">http://www.cia.gov/cia/publications/factbook/geos/gg.html</a>
<b>10</b>	Economic Commission for Europe, working party on land administration	Review of land administration in Georgia. 2001, November 28
<b>11</b>	State Department of Land Management	Statistical information on land use, registration and land market