



ევროკავშირი  
საქართველოსთვის  
The European Union for Georgia



VAKHTANG NATSVLISHVILI

# NON-STATE FUNDING OF CIVIL SOCIETY ORGANIZATIONS IN GEORGIA

LEGISLATION AND  
PRACTICE  
RESEARCH

2019



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## ABOUT THE STUDY

### Aim of the study and target audience

Our aim is to study the legal framework and corresponding practice concerning the non-state funding of civil society organizations (CSO) in Georgia. The research analyzes various non-state funding forms and identifies shortcomings in this area. The research does not discuss the funding of CSOs by international donor organizations and state entities.

The key target audience of the research includes CSOs, public entities and business companies. We hope, the assessment of non-state funding forms of CSOs will trigger civil and political discussions about this field. We also hope that the research will prove useful to anyone interested in the development of CSOs and in general, civil society in Georgia, including to international organizations, media outlets, political parties, scholars and researchers.

### Research methodology and sources

The research involves an interpretive analysis of legal material. In assessing the implementation of legislation we rely on a secondary source – surveys, opinions and assessments of CSOs and their financial sustainability.

In conducting the research we used the following sources: (a) Georgian legislation and regulations; (b) court decisions; (c) requested public information; (d) reports of international and local organizations; (f) academic literature.

### Structure and terminology of the research

The research consists of separate chapters each discussing separate forms of non-state funding. Each chapter offers an overview and analysis of a sphere, relevant legal framework and tax policy.

The study often uses the term “civil society organization” which applies to non-entrepreneurial (noncommercial) legal entities specified in the Georgian legislation. We do not use the term “nongovernmental organization” as it is the definition with negative connotation.

During the research, we had to search for Georgian equivalents to several forms of non-state funding of CSOs. We do hope the Georgian equivalents convey relevant meaning. These terms are: Individual Volunteering; Individual Donation Corporate Donation; Corporate Volunteering; Community Foundation; Social Entrepreneurship; Corporate Social Investment; Impact-Oriented Investment; Cross-Sector Cooperation; Crowd-Funding.

## NON-STATE FUNDING IN GEORGIA: GENERAL OVERVIEW

Origination of modern Georgian CSOs<sup>1</sup> is linked to the breakup of the Soviet Union. After this historic development, the United States and European states started taking interest in supporting Georgian CSOs. Over the period between 1992 and 1995, the number of CSOs reached several thousand. These associations almost entirely depended on Western funding. Much like civil organizations of post-socialist countries, Georgian CSOs adopted liberal principles and focused their activity on the criticism of abuse of power by the state (Nodia, 2005). Over time, the scope of activities of Georgian CSOs expanded.<sup>2</sup>

According to researchers working on this topic, CSOs in Georgia are more powerful and effective organizations than in other countries. Legislative framework regulating the establishment and operation of CSOs is known as favorable. According to the official data of the Public Registry, over 26,000 CSOs are registered in Georgia. They enjoy a broad range of political and economic rights while their activity is duly controlled by the state. Professionalism and active engagement in state reformation process is usually assessed as a strength of Georgia CSOs. Georgia CSOs are often commended for their skills and capacity to work on pressing issues for the country and to set political and social agenda (Pinol Puig, 2016; Lortkipanidze & Pataraiia, 2014; Natsvlishvili, Salamadze et al, 2018; USAID, 2018). In 2013, the Georgian Parliament officially recognized the importance of CSOs in the process of development of democratic political system and committed itself to support them.<sup>3</sup> At present, the legislative body has been working on a state draft concept of CSO development; the adoption of this concept is an obligation of the Parliament of Georgia under the Open Government Partnership National Action Plan.<sup>4</sup>

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1 Under the term “civil society organizations” we imply non-entrepreneurial (non-commercial) legal entities registered in accordance with the Civil Code of Georgia (The Legislative Herald of Georgia, 31, 24/07/1997). In civil life they are usually referred to as nongovernmental organizations; however, we believe that the term “nongovernmental organizations” is inaccurate as it includes not only noncommercial associations of citizens, but also professional unions and entrepreneurial entities.

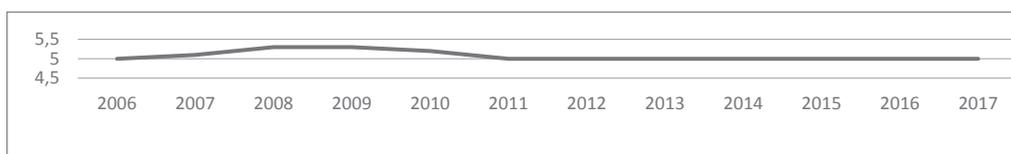
2 According to a survey by the Caucasus Research Resource Center, the highest number of CSOs work on issues of education and science, youth and civil society development whereas the lowest number of CSOs work on topics of healthcare, refugees, agriculture and environment. See, CRRC, 2018.

3 The memorandum of cooperation between the Georgian Parliament and CSOs is signed by the Speaker of Parliament and more than 200 CSOs.

4 See Open Parliament Georgia Action Plan 2017 of Georgia, commitment N1.8.

Financial sustainability is named as one of main challenges faced by Georgian CSOs. According to the 2018 CSO Sustainability Index, the indicator of financial sustainability of Georgian CSOs has not shown notable changes over the past decade (USAID, 2018) (see Table 1). The same report notes that CSOs lack diverse sources of financing and mainly rely on international grant funding (USAID 2018). A survey conducted by the Caucasus Research Resource Center (CRRRC) in 2018 supports this finding (CRRRC, 2018).<sup>5</sup> According to the survey, the share of grants from donor organizations exceeds 64% of total CSO income (see Table 2).<sup>6</sup>

**Table 1. Financial sustainability index of Georgian CSOs**



Source: USAID 2018

**Table 2. Income of Georgian CSOs, 2016**

	Source	Quantity	Share
1	Grants from donor organizations	143	64.4
2	Contributions from natural persons	39	17.6
3	Membership fees	30	13.5
4	Funding from business	20	9.0
5	State funding	44	19.8
6	Income from economic activity	53	23.9
7	Other	25	11.3

Source: CRRRC, 2018

<sup>5</sup> According to authors of the research, it proved difficult to obtain data on financial turnover from CSOs. Around 22% of respondents did not provide information on the financial turnover in 2016. Consequently, in the authors' view, caution must be exercised in interpreting the data, though some conclusions may be drawn out. See CRRRC, 2018.

<sup>6</sup> It is noteworthy that according to the CRRRC research, the total turnover of CSOs in 2016 comprised GEL 69.3 million. However, more than 80% of the total turnover accounted for one fifth of CSOs; three fourth of the latter category (29 CSOs) are registered in Tbilisi. See CRRRC, 2018.

The above data is indicative even without any additional analysis. However, with the change in the paradigm of international donor funding, the financial sustainability of CSOs may further deteriorate. As the data of Organisation for Economic Co-operation and Development (OECD) shows, international funding of Georgia has been decreasing over the past three years: in 2013, Georgia received 646 million worth international development assistance; this indicator decreased by around 100 million in 2014 and further to 448 million in 2015 (see Table 3).<sup>7</sup> For its part, the EU, one of the largest donors alongside USAID, favors the award of large grants, which notably decreased the number of beneficiary CSOs (USAID 2017). Furthermore, according to the World Bank classification, Georgia fluctuates between lower-middle- and upper-middle-income economics in the last few years (World Bank, 2017). Experts reckon that along with the improvement of Georgia's economic indicators, the international funding for Georgian CSOs will further decrease.

**Table 3. International assistance to Georgia (ODA)**

	Year	Amount (mln \$)	Difference to the previous year (mln \$)
1	2013	646.3	–
2	2014	562.5	↓ 83.8
3	2015	447.6	↓ 114.9

Source: USAID, 2017

Such a state of affairs poses a challenge to CSOs: they should start working on diversifying their sources of funding. Although since 2012, the state is authorized to award budget grants to CSOs,<sup>8</sup> a state grant cannot become a substantial source of funding. The state funding of CSOs is instable and chaotic and normally given to implement existing state approaches in this or that area (Salamadze, Paniashvili, 2017; Samaladze, Latsabidze, 2017). There is no public entity that would award a grant for the assessment of accountability of political authorities, while local gov-

7 This indicator does not differentiate between the assistance received by the state and CSOs. However, in experts' view, the decrease in total indicator proportionally affects the amount of international funding of CSOs.

8 The wording adopted in 1996 did not include state entities among grant giving subjects. At the end of the second decade of independence, in 2009, Georgia set up a common fund for financing CSOs (which stopped functioning in 2013, though without undertaking a liquidation procedure) while the amendment to the Law of Georgia on Grants, adopted in 2010, extended the list of grant giving subjects to include a legal entity in public law. The 2011 amendment added a Ministry of Georgia to this list while the 2017 amendment further extended the list of grant giving subjects to include an Office of State Minister of Georgia and ministries of Autonomous Republics of Abkhazia and Adjara (Legislative Herald of Georgia, 19-20, 30/07/1996).

ernments have no grant-making power.<sup>9</sup> It is also worth to note that more than 80% of grants awarded by public entities accounts for organizations registered in Tbilisi (CRRC, 2018).

There is a variety of non-state funding mechanisms, including individual and corporate donations, volunteering, social entrepreneurship, cross-sector cooperation, community foundations, and social investments. A low level of popularity of these non-state funding mechanisms in Georgia have various explanations. We should firstly overview a normative environment regulating non-state funding.

The legislation does not prevent CSOs from receiving non-state funding. The Civil Code of Georgia and other sectoral laws allow CSOs to apply various forms of non-state funding. The Law of Georgia on Volunteering, adopted by the Parliament in 2016, notably simplifies the use of volunteer work by CSOs. The Tax Code of Georgia, normally, taxes CSOs in a way similar to business companies. Under the so-called Estonian tax model that entered into force on 1 January 2019,<sup>10</sup> the taxable amount for levying the profit tax on a CSO is not a type of income, but the conformity of the spending of CSO to charitable purposes declared in its charter.<sup>11</sup> Such approach exempts CSOs from profit tax.<sup>12</sup> Furthermore, the Tax Code provides mechanisms for encouraging corporate funding of CSOs.<sup>13</sup> At present, the Parliament of Georgia is in the process of considering draft legislative amendments concerning social entrepreneurship, whereby the state aims at supporting the development of social entrepreneurship and enhancing opportunities for social entrepreneurs to obtain soft loans and grants; furthermore, according to the draft law, the state commits itself

9 Civil Society Institute works on the issue of CSO state funding. With the EU support, the Institute has conducted a research on international and local practice of state funding and is now in the process of developing a Georgian model. For more information, see Salamadze, Paniashvili 2017. Consequently, this issue will not be discussed in detail in this review.

10 The Estonian tax model has been in force for enterprises since 1 January 2017.

11 Article 10 of the Tax Code of Georgia lists forms and types of charitable activities which include: human rights protection, protection of environment, development of democracy, culture, art, sport, education, science, health protection, development and protection of social welfare. See Tax Code of Georgia (Legislative Herald, 3591, 17/09/2010).

12 The explanatory note of the tax amendment says that "From 2019, the taxation of organizations performing economic activities will be carried out according to new principles of levying profit tax, which actually means that they are exempt from this tax because they do not distribute the profit." See <https://info.parliament.ge/file/1/BillReviewContent/177558?> [Last accessed on 18.03.2019]. Characteristics of so-called Estonian tax model are discussed in detail in relevant chapters.

13 Article 117 of the Tax Code allows business to deduct the amount given to a charitable organization as well as the market price of goods and/or services provided for free from taxable income, "but not more than 10 percent of the amount remaining after the deductions from gross income, envisaged under this Code." See Tax Code of Georgia (Legislative Herald of Georgia, 3591, 17/09/2010).

to give, in the event of equal conditions, preference to goods and services of social enterprise in public procurements.<sup>14</sup>

Although the legislation is assessed as favorable, it is clear that the regulatory framework of CSOs needs revision. The experience of many countries shows that ensuring a real access to diverse sources of financing requires a concerted effort of the state – the policy that will encourage volunteerism, donations, cross-sector cooperation, establishment and development of community foundations. According to OECD, governments have a special role in institutionalization and development of these mechanisms and this role is not limited to the adoption of legislation alone (OECD, 2016). It is extremely important to launch public and political discussion on the role and importance of individual and corporate charity: the experience shows that despite a possible positive impact of charity, it cannot replace the obligation of the state to deal with fundamental social problems. However, the development of charity in Georgia is often viewed as a measure that replaces social responsibilities of the state.<sup>15</sup>

Unarguably, CSOs share the responsibility for not using forms of non-state funding. Georgian CSOs, having developed with the international financial assistance, did not consider, from the very outset, a membership-based and participatory model of management. Studies show that a large number of CSOs are not seen as associations accountable to citizens (Pino Puig, 2016) and that their agenda does not often consider real needs of the population (Reisner, 2018). It is noteworthy that CSOs do not, usually, speak in media about those issues which in the population's view are the most serious problems (NDI, 2018).<sup>16</sup> According to one study, Georgian CSOs see the professionalism of their employees as their main strength,<sup>17</sup> while influencing a political process as their main purpose (Lutsevych, 2013); the same study shows that CSOs approach citizens as their "beneficiaries." According to the CRRRC Barometer, the trust of population in CSOs dropped by 12 points between 2008 and 2015 and comprised 23% (USAID, 2017). According to the CSO Sustain-

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14 The draft amendments to the legislation on social entrepreneurship was prepared by the Center for Strategic Research and Development of Georgia and submitted to the Parliament of Georgia for consideration. See the chapter on social entrepreneurship.

15 Discussions underway in Georgia show that there is an inadequately high expectation, for example, in regard to benefits of the principle of corporate social responsibility (CSR) of business. Literature on this topic is explicit that all social and environmental problems cannot be settled based on a good will of the business; however, standards of ethical business conduct may contribute to settling these problems. See the chapter on corporate contributions and volunteerism.

16 According to NDI's Public Attitudes Survey, the population thinks the most important problems are jobs, poverty, territorial integrity, rising prices and inflation, affordable medical services, pensions and salaries. According to 2018 Sustainability Index, CSOs hardly speak about these issues in media. See, USAID 2018.

17 Only 27 of surveyed CSOs view membership-based management as their strength. See, Lutsevych, 2013.

ability Index, only 1% of population would like to receive information from CSOs (USAID, 2018). Consequently, it does not come as a surprise that citizen donations do not represent a significant source of CSO income. According to official data, only 6% of Georgia's population donates to CSOs and only 9% has participated in volunteering (CAF, 2017).<sup>18</sup>

Relationship between business and CSOs and business donations to CSOs is yet another problematic issue. According to the CSO Sustainability Index, business perceives CSOs as politicized institutions and shuns cooperation with them fearing tensions with the government (USAID 2017). The perception of CSOs as politicized institutions is further strengthened by frequent appointments of CSO employees to government and political positions (USAID, 2018). It should be emphasized that almost fifth of 568 business companies, interviewed within the scope of a recent survey, has never heard of the concept of corporate social responsibility whereas those, who implement social responsibility projects, decide themselves what type of public benefit project is acceptable to them and do not, normally, cooperate with CSOs in this regard. Only 8% of surveyed business companies has implemented any type of project in cooperation with CSOs (CRRC, 2018) (see Table 4).

**Table 4. Cooperation between business and CSOs**

(a) Share of CSOs having received business donations in 2016: 9%
(b) Share of business having cooperated with CSOs: 8%
(c) Share of business operating in Tbilisi, which has cooperated with CSOs: 13%
(d) Share of business operating in regions, which has cooperated with CSOs: 4%

**Source: CRRC, 2018**

On the other hand, business donation is not acceptable for a number of CSOs. An especially acute issue that has been raised on the social agenda in recent years is the protection of human rights, especially labor and environmental rights.<sup>19</sup> Several CSOs refuse to accept business donations as they think that business neglects human rights and in giving charitable donations pursues corporate interests alone. One may use a quantitative and qualitative survey of CRRC to illustrate this attitude, according to which only 20 out of 282 surveyed CSOs accepted business

<sup>18</sup> Georgia is 124<sup>th</sup> among 139 countries by the indicator of volunteering and 137<sup>th</sup> by the indicator of donations to CSOs. See, CAF, 2017

<sup>19</sup> According to UNDP survey, the labor rights are the most frequently violated rights in Georgia. See UNDP 2017.

donation (CRRC 2018).<sup>20</sup> CSOs interviewed in one of the surveys assert that their aims starkly differ from those of business and that they consider any effective bilateral cooperation as a possibility of a very distant future (CRRC, 2018). In this regard, a Corporate Social Responsibility Club, which was established in 2015 and includes representatives of up to 90 CSOs, public entities and academic institutions, has failed to achieve any tangible results yet (USAID, 2018).

As the available quantitative and qualitative studies show, the use of non-state funding mechanisms is of spontaneous and one-off nature and does not rest on a long-term strategy. This means that CSOs themselves have to take efforts to gain trust among population and to mobilize volunteers and donations. The use of non-state funding mechanisms is not supported by the state policy either. In this research we will explore the legal framework of each and every non-state funding form, tax policy and a relevant practice.

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<sup>20</sup> As of today, CSOs do not have an obligation to make public received business donations or joint projects with business. In order to prevent any illegal and corrupt deal between a CSO and a business company, it is important to impose an obligation of CSOs to publish information about received financing.

# 1. INDIVIDUAL VOLUNTEERING

## Overview of the field

Volunteering is an integral part of charitable activity. The International Labour Organization defines volunteering as activities performed willingly and without pay for social benefit (ILO, 2008). Volunteering is known to significantly increase the impact of CSOs. According to a global research, volunteers contribute around \$400 billion to the global economy annually (Points of Light Institute, 2011). The UN General Assembly, the European Parliament and the Council of Europe encourage the governments to support and promote volunteerism (ECNL, 2014). Since the UN proclaimed 2001 as the International Year of Volunteers, over 70 laws were adopted across the world to promote volunteering (ECNL & ICNL, 2009).

Studies show that volunteering is not widely practiced in Georgia (USAID, 2017).<sup>21</sup> Experts attribute this to the Soviet experience where a mandatory, state-imposed volunteering led to the distortion of the concept of volunteering (G-PAC, 2015). However, this cannot be the only or major reason; to neutralize this opinion it is suffice to say that youth, who should comprise a large group of volunteers, have not experienced the forced volunteerism but do not engage in volunteer work. Moreover, instead of increasing, the number of volunteers in Georgia has been decreasing.

According to the World Giving Index, 18% of Georgian population did volunteer work in 2015 (CAF, 2016) as compared to 21% in 2014 (CAF, 2015). The indicator further deteriorated in 2016, as according to the data of Charities Aid Foundation, only 9% of Georgia's population did volunteer work (CAF, 2017). In the Rating for Global Volunteers Georgia is ranked 124<sup>th</sup> among 139 countries (ibid.). According to a most recent CRRC survey, 5,901 persons from 282 surveyed CSOs did volunteer work (CRRC, 2018). At the same time, local opinion polls showed 8% increase, between 2012 and 2015, in people who believed that volunteering was an important aspect of good citizenship, with the indicator of such people standing at 73% (CRRC, 2015). According to 2018 survey, some 37% of population is willing to cooperate with CSOs which would work on tackling important issues for the community and country (CRRC, 2018).

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21 It must be noted that indicators of volunteering vary in European countries. According to a survey conducted in the EU, the highest indicators of volunteering, around 40%, are seen in Austria, Great Britain, the Netherlands and Sweden; a corresponding indicators of Germany, Denmark, Luxembourg and Finland range between 30% and 40%, whereas the lowest indicators – below 10%, are seen in Greece, Lithuania, Italy and Bulgaria (GHK, 2010).

Thus, there is a huge discrepancy between a positive attitude of citizens to volunteering and a real practice. Such a huge difference may be explained by a variety of factors. However, before moving onto the analysis of legal and tax regulation of volunteerism, it should be emphasized that the level of trust in CSOs, which should be primary beneficiaries of volunteer work, is low in the country. According to recent data, 28% of the country's population trust CSOs (G-PAC, 2014); only 27% of population thought that CSOs worked on important issues in 2015 (USAID 2017). According to the 2018 survey, CSO is trusted by 28% of population, i.e. nearly the level of trust in courts (32%) which are often criticized by these organizations (CRRC, 2018). This data suggests that CSOs themselves have to work hard towards gaining trust of population and consequently, mobilizing volunteers.

It should be noted that in 2015, the Ministry of Sport and Youth Affairs began to implement the Volunteer Work Development Program within the framework of Youth Policy Development Program. The program aims at strengthening the institute of volunteering on the national level, raising civil awareness of youth through volunteering and increasing number of youth willing to volunteer across Georgia. A common database of volunteers was set up under the program.<sup>22</sup> However, this database is not public and CSOs cannot use it directly. The Ministry itself uses volunteer work of youth in various sports and youth events.

## Legal framework

A proper legislative environment is known to be a major factor for the promotion of volunteerism (UNV, 2015). The concept of volunteering was alien to the Georgian legislation until 30 December 2016. Therefore, there was a risk of applying Labor Code provisions to volunteer work;<sup>23</sup> in addition, lack of legal regulation of volunteering added ambiguity to the rights and responsibilities of volunteers and host organizations (ICNL & ECNL, 2009). At the end of 2016, the Parliament of Georgia adopted a law which was drafted by CSOs to regulate relations between volunteers and host organizations across the country.<sup>24</sup> The law defines volunteer relations and its subjects and determines their rights and responsibilities as well as legal guarantees.

According to the law, "volunteering is a socially useful activity voluntarily and gratuitously performed by natural persons, using their knowledge and skills, under organized conditions." A socially useful activity, according to Article 2(2) of the law, is an

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22 Electronic registration can be performed on the official webpage; see, <http://volunteers.youth.gov.ge/>.

23 For example, in Turkey, a CSO was fined for the failure to provide health insurance to a volunteer. The legislation of Turkey did not know the concept of volunteer and therefore, the state supervision body regarded a volunteer as an employee (TUSEV, 2013).

24 The Law of Georgia on Volunteering. According to Article 1(3), the law does not apply to volunteer relations, where one party is a political union.

activity in any of the following areas: “protection of human rights, democracy, development of civil society and mass media, education, science, culture and art, poverty reduction and social security, healthcare, protection of the environment, youth and children’s issues, gender issues, conflict resolution, support to refugees and internally displaced persons, migration, promotion of business and economy, support of agricultural development, physical education and sports, protection of animal rights, civil security emergency response and fields related to the preparation of the population for such emergencies.” Thus, the notion of socially useful activity is broad enough to encompass all types of CSO activities.

According to the Law on Volunteering, a volunteer may be a natural person who has attained the age of 16 whereas those below 16 may be engaged in volunteer relations only with the consent of their legal representative or a guardianship or custodianship authority.<sup>25</sup> It should be emphasized that when doing a volunteer work a natural person retains a status of unemployed and consequently, the right to benefits and allowances provided under the Constitution and the legislation of Georgia.<sup>26</sup> The Law also lists host organizations of volunteer work, which alongside resident or non-resident non-entrepreneurial (non-commercial) legal persons or their branches includes legal entities in public law, local self-government bodies and educational and medical institutions (Article 3.5). The Law does not impose any limitation on working hours save the prohibition in Article 9, whereby the duration of the working hours for volunteers from 16 to 18 years of age shall not exceed 36 hours a week. Moreover, the Law does not prohibit host organizations to use volunteer work without entering into formal relations; however, the Law does not apply to such individual, spontaneous activities.

The Law allows to establish volunteer relations in oral or written form; though if volunteer relations last for more than one month, a written agreement is required. In this case, an agreement must specify the nature and duration of volunteer work, the rights and obligations of the parties, and, if applicable, the benefits related to volunteer status. Apart from traditional grounds, an agreement may be terminated due to gross violation of the conditions of the agreement and other circumstances that make it impossible for the volunteer to perform the activities under the agreement. In addition, at the request of a volunteer, the host organization issues a volunteer certificate containing details of the work performed by the volunteer (Article 8).

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25 According to principles of international law on child’s rights, volunteer relations shall not conflict with the minors’ best interests, or prejudice their moral, physical and mental development, or restrict their right and opportunity to acquire compulsory primary and basic education. An identical provision is included in Article 3(3) of the Law of Georgia on Volunteering.

26 Due to the absence of such provision a citizen, for example in the Czech Republic, could be stripped of unemployment allowance in case of engaging in volunteer work (ECNL & ICNL, 2009). The threat would be similar in Georgia, had this provision was not included in the law.

Rights and obligations of volunteers and host organizations arise upon entering into volunteer relations. According to Article 4 of the Law, a host organization shall inform the volunteer of his/her rights and obligations. Upon the request of a volunteer, the host organization shall compensate him/her for expenses incurred by him/her in the performance of volunteering activities, including travel, food, communication, accommodation and if need be, consular service expenses. The host organisation also has the obligation to ensure a safe environment to volunteer and provide a volunteer with timely and full information about expected threat and danger. It must be underlined that the host organisation shall compensate volunteers for any harm to health of a volunteer in the course of performing volunteering activities and for necessary costs of treatment (Article 6). Moreover, Article 7 of the Law imposes an obligation on the host to compensate any damage to a third party caused by a volunteer's unlawful actions during the performance of volunteering activities. This rule is in full compliance with fundamental principles of civil law.

A volunteer also has obligations to a host organization. Article 4 of the Law requires from a volunteer to perform his/her activities in accordance with legal and ethical principles and the agreement entered into with the host organization; also, to take care of the property of the host organization and in a timely manner inform the host organization of any circumstances which preclude him/her from performing agreed activities.

Thus, the legal regulation of volunteering is in line with international volunteering principles and legal guarantees effective in other countries (CSI, 2011; ICNL, 2014). Consequently, legal provisions regulating volunteer relations do not require any substantial amendment or improvement.

## Tax policy

When the Law on Volunteering was adopted, the author of the draft, Civil Society Institute, asserted that in addition to regulation of volunteer relations, it was necessary to amend the Tax Code so as to establish a preferential tax regime encouraging volunteering. The Parliament, however, disapproved of this opinion and made no relevant amendments to the tax law.

Although volunteers do not receive salaries, their work for CSOs requires some expenses such as, for example, transportation and communication expenses. According to the Law on Volunteering, such expenses shall be covered by a host organizations (Article 5). The Tax Code qualifies the compensation for volunteer

expenses as a taxable income and consequently, levies income tax.<sup>27</sup> As a result, the cost of volunteer work increases for CSO as it has to “top up” the compensation amount with income tax (CSI & ICNL, 2011). Such tax approach is known as volunteer tax in the relevant literature. According to the Tax Code, a CSO employee gets compensation for business travel expenses and representational expenses and in contrast to a volunteer, this compensation is income tax-exempt (Article 101(3), subparagraphs “a” and “b”). Moreover, the value of assistance provided by an organization to its employee for educational purposes, when the employee requires the education to perform tasks under his/her labor agreement, is not included in salary income (Article 101(2), subparagraph “a”). It must be noted that were this approach applied to volunteer work, volunteering could become more attractive for citizens as host organizations would be allowed to finance retraining of volunteers.

Apart from tax benefits, the international experience knows numerous mechanisms of promoting volunteering. Such mechanisms include a state program for volunteer education, a possibility to receive academic credits for volunteer hours, discount vouchers for volunteers for various cultural institutions, et cetera<sup>28</sup> (ECNL & ICNL, 2009). The Georgian legislation does not provide for any of the instruments.

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27 According to Article 100(3) of the Tax Code, gross income shall be income earned in any form and/or through any activity, namely: a) salary income; b) income earned from economic activity, which is not related to employment; c) other income not related to employment and economic activity. Thus, compensation for expenses given to a volunteer shall be viewed as income and a host organization, as a tax agent, shall deduct income tax (except for exemptions set in the Tax Code).

28 These issues will be reviewed in the research of international practice of non-state organizations.

## 2. INDIVIDUAL DONATION

### Overview of the field

Individual donation is a donation by a natural person to a CSO. Donation may be either monetary or in-kind. Often, individual donations are made at times of natural disasters or other humanitarian crises. According to the Global Philanthropy Legal Environment Index, the indicator of individual donations of rich countries significantly exceeds that of low- or medium-income countries<sup>29</sup> (CAF, 2014). According to the World Giving Index, men tend to donate to CSOs more frequently<sup>30</sup> than women (CAF, 2017); however, the picture changes when it comes to countries with high gender equality indicators: in the countries such as Sweden, Denmark, Norway, New Zealand and Australia, women donate more frequently than men (ibid.).

The international practice knows various mechanisms of regulating individual donations: in a number of countries, individual donations qualify for tax benefits. Nonetheless, according to the World Giving Index, individual donations are mainly driven by a desire to assist rather than enjoy financial or other benefits (CAF 2017). Results of a survey conducted by Indiana University also suggest that more than 73% of US citizens donate with the belief that it can make difference and for personal satisfaction; the same survey shows that a tax benefit is an incentive to donate for 34% of people<sup>31</sup> (Indiana University, 2014). Regardless of people's motivations, it must be noted that, according to a global research, there is a direct correlation between a diversity of tax benefits and the indicator of donations: the broader a tax incentive mechanism the higher the amount of individual donations<sup>32</sup> (CAF 2014).

Individual donation is not a common practice in Georgia. According to a global research, only 6% of the population donates and by the indicator of monetary donations, the country ranks 137<sup>th</sup> among 139 countries (CAF, 2017). According to a CSO survey of, conducted by CRRC in 2017, individual donations comprise 17.6% of total CSO income (CRRC, 2018). This indicator may be a result of, *inert alia*, low trust in CSOs among population: by the most recent data, only 28% of population trusts CSOs (G-PAC, 2014). In addition, in 2015, only 27% of population thought

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29 When assessing the wealth of countries, the index uses World Bank data.

30 This data reflect only monetary donations.

31 However, it is worth to note that, within this survey, to a questions whether they would decrease donations if income deductions are eliminated, 417% of respondents responded positively and 48.3% - negatively (Indiana University, 2014).

32 There is a need of one clarification here: according to the same index, the number of tax benefits for donations is higher in rich countries. Therefore, only one variable such as the availability of tax benefits may not be a determining factor of high indicator of individual donations.

that CSOs worked on important issues (USAID 2017). According to the 2018 survey, the trust of population in CSOs stands at 28%<sup>33</sup> (CRRC, 2018). No doubt that the trust towards CSO activities is an important factor stimulating giving.

## Legal framework

Giving of individual donation is regulated under the contract law of the Civil Code of Georgia. Article 524 of the Code defines the concept of gift which means transfer of property for free under a contract of gift. One of the types of such contracts is a donation;<sup>34</sup> donation is a type of contract the validity of which depends on the achievement of a particular objective (Article 528). The concept of property, under the Civil Code, includes all things and intangible property “which may be possessed, used and administered by natural and legal persons, and which may be acquired without restriction, unless this is prohibited by law or contravenes moral standard” (Article 147). A thing may be immovable, for example, land or building, or movable (Article 149); while intangible property means claims and rights that are intended to generate material benefit (Article 152).

Based on above cited provisions of the Civil Code, it may be said that natural persons may transfer money as well as movable and immovable things, securities and the right of claim<sup>35</sup> in the form of donation to CSOs. Donation specified in the Tax Code enables a natural person to demand that the donation be used for supporting a particular charity or common good.

## Tax policy

Individual donation is not a taxable income of CSOs in many countries; had it been so, either a giver or a receiver of donation would have had to seek additional sums to pay a corresponding tax to a state budget (ICNL & CSI, 2011).

According to Article 99 of the Tax Code of Georgia, which was effective until 1 January 2019, profit tax exemption applied to grants, membership dues and donations to a CSO. Donation, according to Article 8(40) of the same Code, was defined as goods, services and funds received by a CSO as gifts. This meant that individual donations to CSOs were exempted from the profit tax.

33 Almost the same level of trust is enjoyed by courts (32%) and the Parliament of Georgia (30%). See, CRRC, 2018.

34 According to civil law experts, the word used in the Civil Code to denote donation [in Georgian] is the same as donation; the difference is in term used, not content.

35 The right of claim, according to the Civil Code, includes many legal benefits. For example, a pensioner may transfer his/her right to receive and use pension to another person, for example, a CSO; a person renting immovable property may transfer the right to claim rent from renter and use rent to another person, for example, a CSO; many examples may be cited of this kind.

On 1 January 2019, the so-called Estonian model of levying profit tax entered into force, fundamentally changing the peculiarities of CSOs taxation. The provisions exempting the donations to CSOs from the profit tax were deleted from Article 99 of the Tax Code. An explanatory note on the tax amendments states that the transfer to a new model of levying profit tax means the exemption of CSOs from the profit tax because the profit is not distributed among CSO founders.

More specifically, since 1 January 2019, a taxable amount for levying the profit tax on an organization is not a type of income – be it a grant, donation or ancillary economic activity, but the conformity of spending by an organization to the organization's goals declared in its charter. Consequently, if individual donation received by a CSO is used towards charitable goals defined in the organization's charter or the Code, it is exempted from the profit tax. Article 10 of the Tax Code of Georgia lists forms and types of charitable activities which include: human rights protection, protection of environment, development of democracy, culture, art, sport, education, science, health protection, development and protection of social welfare.

It should be noted that the Tax Code of Georgia does not provide any incentive mechanism for natural persons who make individual donations. Such mechanisms can be found in abundance in legislations of various countries (ECNL, 2015).

### 3. CORPORATE DONATION AND CORPORATE VOLUNTEERING

#### Overview of the field

Corporate donation and corporate volunteering<sup>36</sup> is part of corporate social responsibility. Corporate social responsibility (CSR), as defined by the European Commission, implies business combining its financial aims with the aim to generate social and environmental benefits; this concept conflicts with a neo-classic view whereby the only goal pursued by business is profit (Steurer, 2010; Elkington, 1994). Proponents of CSR believe in its benevolent impact on not only company's financial success but also sustainable economic development of a country, as it enhances the reputation of business and contributes to tackling pressing problems in a country (CSRDG, 2012). It should be noted as well that many researchers see the weakening of state principles and economic globalization as reasons behind the popularity of CSR; according to them, with the emergence of multinational corporations the regulatory power of state has weakened, leaving the defense of public good at the good will of the business (Bakan, 2015; Caffaggi & Renda, 2012). Some even place blame on the CSR concept for strengthening and promoting the vision that social and environmental problems may be tackled through charitable activities of business, not joint efforts of the state (Thorup, 2015).

CSR is a relatively new phenomenon in Georgia (OECD 2016). However, one may already observe some activity in this area. The state has yet to develop a common strategy to promote this practice, but non-state actors have stepped up their activity. With a joint effort of UNDP and the Civil Development Agency (CiDA), a corporate social responsibility club (CSR Club) was established in Georgia, bringing together around 90 business companies, CSOs, academic institutions and public entities. The CSR Club aims at promoting and streamlining CSR in practice (OECD, 2016). In addition, the Europe Foundation<sup>37</sup> and the Center for Strategic Research and Development of Georgia (CSRDG) support the development of SCR; they take efforts to make CSR part of university education and plan other awareness raising initiatives (OECD, 2016). According to information provided by CiDA, business companies donated more than GEL 1 billion for mitigating flood results in Tbilisi on 13 June 2015. Moreover, since 2018, the Center for Strategic Research and Development of Georgia organizes an annual CSR contest "Meliora" with the aim to encourage social responsibility of busi-

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36 Corporate volunteering is discussed in this chapter inasmuch as it is a type of corporate donation.

37 The Eurasia Partnership Foundation has been renamed the Europe Foundation in 2017. It is known in Georgia as Eurasia Partnership Foundation and this name is used in all documents published before 2017.

ness.<sup>38</sup> In 2015, under the guidance of the same organization Pro Bono Network was established. The member companies take the responsibility to provide free-of-charge professional expertise to civil society organizations working on social and environmental issues; According to the official website of the network, it unites up to 20 entrepreneurs, including large banks and other financial companies<sup>39</sup>.

Despite some step-up observed in CSR area in Georgia, the results of survey conducted by CRRC in 2018 show that giving by business accounts for the smallest share in total CSO income (CRRC, 2018). Moreover, one fifth of surveyed business companies has never heard of the CSR concept whereas those, who implement social responsibility projects, decide themselves what type of public benefit project is acceptable to them and do not cooperate with CSOs in this regard. Only 8% of surveyed business companies say that they have implemented any type of project in cooperation with CSOs (CRRC, 2018).

Such a state of affairs may be caused by several reasons. Local experts cite the absence of consistent state policy encouraging business towards CSR and CSO funding, as one of the reasons. In OECD's assessment, governments play a special role in institutionalizing this approach. This means building an adequate legal framework,<sup>40</sup> introducing forms of business supervision and shaping adequate expectations to this approach<sup>41</sup> (OECD, 2016).

In addition to the absence of state policy, there is a problem of relationship between business and CSOs. On the one hand, business shuns funding CSOs because they are often perceived as politicized actors and hence, business tries to avoid tensions with the government (USAID 2017). On the other hand, donation from business is not acceptable for every CSO. According to the most recent CRRC survey, only 20 of 282 surveyed CSOs received business funding in 2016 (CRRC 2018). In recent years, one of most pressing issues in society was the neglect of environmental problems and violation of labor rights by business.<sup>42</sup>

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38 The contest is held with the support of European Union and Konrad Adenauer Stiftung. Contest categories cover all major areas of CSR. Contest is open to the companies operating in the country, "that have found responsible ways of making an enduring difference to the well-being of their workers, customers and suppliers, to the communities, and to the environment." As many as 41 companies participated in the 2018 contest. See [www.meliora.ge](http://www.meliora.ge) [last accessed on 18.03.2019].

39 See [www.probonogeorgia.ge](http://www.probonogeorgia.ge) [last seen: 18.03.2019].

40 This, among other issues, requires the introduction of different approaches to various types of enterprises. For example, the European Commission sets separate CSR recommendations for small and medium-sized enterprises (European Commission, 2013).

41 It should be noted that shaping adequate expectations with regard to CSR is one of important issues. Often expectations are too high than practicable. Clearly, all social and environmental problems cannot be tackled through good will of business; however, ethical business standards may contribute to overcoming these problems.

42 According to the UNDP survey, labor rights are the most frequently violated right in Georgia. See, UNDP 2017.

Hence, some CSOs reject donations from business as they believe that in making charitable giving they pursue corporate aims alone. In one of surveys, CSOs often assert that they pursue aims that starkly differ from those of business and declare any effective cooperation as a possibility of a very distant future (CRRC, 2018).

Based on the above overview it may be said that corporate donations and corporate volunteering depend not only on the development of policy in this area but also on CSOs and business. In discussing CSR and devising policy in this sphere, it is important to ensure a nuanced approach towards various CSOs<sup>43</sup> and business companies. In order to exclude any unlawful and corrupt deal between CSOs and business companies, CSOs must have an obligation to publicize the information on funding received from business.

The next subchapter overviews legal grounds and tax policy in regards with corporate donations and volunteering.

## Legal framework

Corporate donation is known as corporate grant in the literature. According to the Law of Georgia on Grants, grant is “earmarked means, either monetary or in-kind, allotted by the grantor to the grantee free of charge which shall be used for implementation of particular humane, educational, scientific-research, health, cultural, sports, ecological, agricultural and social projects, as well as the programs of state or public importance” (Article 2). The list of donors provided in the Law does not include entrepreneurial entities. Consequently, the Georgian legislation prohibits entrepreneurial entities to fund CSOs. Nonetheless, the Georgian legislation envisages a possibility for entrepreneurs to provide material or in-kind support to CSOs. In the following paragraphs, we will review several types of corporate donation and corresponding legislative regulation.

One should start with a concept of gift envisaged in the Civil Code of Georgia, which implies the transfer of property for free (Article 524). The Georgian civil law views donation as a type of gift; according to Article 528 of the Civil Code, the parties may determine that the validity of the contract of gift depends on the performance of certain conditions or the achievement of a particular objective (this objective, according to the same article, may be the common good). Analyzing these two articles, it may be said that the Georgian legislation allows an entrepreneurial entity to transfer a property to CSO as a gift for the implementation of a charitable, public benefit activity. One cannot qualify this institution as a grant, but these two do not differ much in essence.

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<sup>43</sup> For example, service provider, watchdog, think tank CSOs.

According to global researches, the most common form of corporate donation is in-kind business donation (BBE & EPG, 2015). According to available data, 62% of \$20 billion worth donation by 500 large companies in the world is in-kind; companies often prefer to give CSOs in-kind donations in the form of product<sup>44</sup> they manufacture, be it a computer software or construction materials (ibid). According to the same research, monetary donations comprises 24% of all donations; the share of services provided by business pro bono and corporate volunteering comprises 10%.<sup>45</sup> It is therefore important to find out whether the Georgian legislation allows the giving of various donations.

As noted above, the Georgian legislation allows business to donate property to CSO. According to the Civil Code, the concept of property implies all things and intangible property “which may be possessed, used and administered by natural and legal persons, and which may be acquired without restriction, unless this is prohibited by law or contravenes moral standard (Article 147). Thus, the Civil Code allows an entrepreneurial entity to make both material and in-kind donations (ICNL & CSI, 2011).

Yet another form that enables business to provide financial support to CSOs is the establishment of non-entrepreneurial (noncommercial) legal entity. Such a noncommercial entity, regardless of its entrepreneurial activity, may give CSOs not only a donation but also a grant which may be a more flexible and effective form of financial assistance. Several Georgian companies already apply this form.

As regards corporate volunteering, the Georgian legislation does not know this concept. Corporate volunteering means companies enabling their employees to use some of paid time to do volunteer work; in addition, corporate volunteering means business rendering services to CSOs free of charge.<sup>46</sup> In this regard, it must be said that the law which the Georgian Parliament adopted on 30 December 2016, regulates only volunteer relations with a host organization. Consequently, the provisions of this law do not apply to corporate volunteering. Nevertheless, the Georgian legislation does not prohibit business to allow its employees to use some of their paid time towards public benefit activity or become a CSO volunteer.

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44 For example, one of the largest donors, the company Oracle, gives software program for free to schools, colleges, universities in 100 countries; pharmaceutical companies in the United Kingdom, give medications for free to various medical organizations.

45 Data varies in different countries of the world. According to a survey, commissioned by UNESCO, each of 132 surveyed US companies spends, on average, \$78 million; each of 94 surveyed Chinese companies spends, on average, \$5 million; each of 14 surveyed Swiss companies - \$38 million; each of 29 surveyed German companies - \$18 million (BBE & EPG, 2015).

46 That's why we discuss corporate volunteering in this chapter and not in the chapter on volunteering.

## Tax policy

In many countries various types of corporate donation are not considered a taxable income of CSOs. Had it not been so, a giver or a receiver of such donation would have to seek additional sums to pay a corresponding tax to a state budget (ICNL & CSI, 2011; CEPR, 2012). The Georgian tax policy is not uniform in this regard and requires a consistent analysis.

According to Article 99 of the Tax Code of Georgia, which was effective before 1 January 2019, profit tax exemption applied to grants, membership dues and donations to CSOs. Donation, according to Article 8(4) of the same Code, was defined as goods, services and funds received by a CSO as gifts. This meant that individual donations to CSOs were exempted from the profit tax.

On 1 January 2019, the so-called Estonian model of levying profit tax entered into force, fundamentally changing the peculiarities of CSOs taxation. The Parliament of Georgia deleted those provisions from Article 99 of the Tax Code, which exempted grants and donations to CSOs from the profit tax. An explanatory note on the tax amendments states that the transfer to a new model of levying profit tax means the exemption of CSOs from the profit tax because the profit is not distributed among CSO founders.

More specifically, since 1 January 2019, a taxable amount for levying the profit tax on an organization is not a type of income – be it a grant, donation or ancillary economic activity, but the conformity of spending by an organization to the organization's goals declared in its charter. Consequently, if corporate donation received by a CSO is used towards charitable goals defined in the organization's charter or the Code, it is exempted from the profit tax. Article 10 of the Tax Code of Georgia lists forms and types of charitable activities which include: human rights protection, protection of environment, development of democracy, culture, art, sport, education, science, health protection, development and protection of social welfare.

The Tax Code of Georgia also provides an incentive mechanism for business companies to make corporate donations.<sup>47</sup> Article 117 of the Code enables business to deduct from taxable income the amount donated to a charitable organization, also the market price of goods<sup>48</sup>/services supplied free of charge, but “not more than 10% of the amount remaining after deductions under this Code from

47 Similar mechanism is practiced in many countries across the world and is aimed at encouraging corporate charity (BTD, 2013).

48 Other than immovable property; the Tax Code does not apply the procedure specified in Article 117 to immovable property donated by business to a charity organization.

gross income.” A similar rule has applied to entrepreneurial subjects under the so-called Estonian tax model enforced since 2017: a donation made to a charity organization during a calendar year not exceeding 10 % of the net profit gained by the organization during a previous calendar year shall not be subject to profit taxation (Article 98<sup>3</sup>).

It must be stressed that incentive mechanisms provided in Articles 117 and 98<sup>3</sup> apply only in case if business donates to a charity organization and not all CSOs (non-entrepreneurial legal persons). The rule of granting a status of a charitable organization is defined in Article 32 of the Tax Code; according to official data, there are only up to 150 organizations in Georgia with the status of charitable organization<sup>49</sup> against over 20,000 organizations registered as SCOs.<sup>50</sup> Therefore, these mechanisms cannot have any significant impact on CSO funding.

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49 In the assessment of many CSOs, the status of charity organization does not ensure them with many tax benefits; consequently, they do not see any sense in obtaining this status. Moreover, charity organizations are required to submit annual activity reports and financial statements certified by an independent auditor to the Revenue Service (Article 32 of the Tax Code).

50 Official data of the Public Registry.

## 4. SOCIAL AND IMPACT-ORIENTED INVESTMENTS

### Overview of the field

In the past few years, social and impact-oriented investing has often attracted attention of state, business and CSO. It is an investment strategy that aims to combine financial profit with social impact benefit and generate their simultaneous and balanced growth (Oliver Wyman, 2016). Under this concept, the aim of investors to gain profits is combined with social, environmental and ethnical goals; social and impact-oriented investment may be understood as corporate social responsibility translated and materialized in investment decisions; thus, it means streamlining social issues in capital investments implemented for the aim of generating profits (CSR DG, 2012).

There is no universal definition of social and impact-oriented investment: it is an evolving concept with its essence, like terms denoting it, constantly changing. According to the approach of the Global Impact Investing Network (GIIN),<sup>51</sup> social investment may be made by business companies and individual investors as well as CSOs and the state (for example, state pension fund's social investing<sup>52</sup>).

In parallel to state efforts to stimulate social and impact-oriented investing, international incentives mechanisms have been devised. The most important international instrument is the Principles for Responsible Investment adopted by the UN in 2006 (UN, 2006). These principles rest on the idea that objectives of social, environmental and corporate management will, over time, increasingly affect investment activity and combining them will, in the long run, lead to better financial results, on the one hand, and on the other, satisfaction of public demands. As of today, the principles have 1,853 signatories;<sup>53</sup> each signatory is required to submit an annual report on responsible investments (UNEP, 2016). Other instruments stimulating social investment include the OECD Guidelines for Multinational Enterprises (OECD, 2014) and the IFC's Environmental and Social Performance Standards (IFC, 2012).

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51 GIIN was founded in 2009 and aims at raising awareness of social investment on the international arena.

52 In 2000, in Sweden, based on the consensus of five political parties, the Parliament adopted the law obligating the state pension fund management body to annually prepare a report; the report shall contain information as to what extent the management body considers requirements of social impact investment when investing social funds.

53 A signatory to the UN Principles for Responsible Investment may be a shareholder, investment manager and service providers in investing sphere.

CSOs view the concept of social and impact-oriented investing as a mechanism of social changes (Evenett & Richter, 2011). CSOs have important knowledge of those social spheres which are not well known to business and consequently, viewed as attractive for economic activity. However, social cooperation of state, CSOs and business enables to exchange information and identify those social spheres where investments and ethical business activity may be carried out (World Economic Forum, 2013).

The concept of social and impact-oriented investments is not widely known in Georgia. Discussions around CSR are more focused encouraging companies to observe ethical norms in their ongoing activities and engage in various charity activities; less attention is paid to identifying possibilities of social investing and mainstreaming CSR in decision making process. The Europe Foundation ran special program for several years, which, inter alia, aimed at introducing the topic of social and impact investing in business schools of local universities.

## Legal framework

The Georgian legislation does not contain special provisions regulating social and impact investments. In such cases relevant persons apply those legal acts<sup>54</sup> that concern starting and running a business, or partnership between business and CSOs. Moreover, there is no strategy which would identify those spheres that require social investments and would determine a legislative regime encouraging such activity. State programs for funding startups do not envisage incentives for impact investments.

## Tax policy

Tax benefits are one of incentives for social and impact investments. Many countries have financial incentive and tax benefit schemes in place, which facilitate socially responsible companies to conduct their activities. The tax legislation of Georgia does not provide benefits for such type of activity. However, the government of Georgia, sometimes, exempts various investments of state importance from tax.

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<sup>54</sup> This mainly implies the Law of Georgia on Entrepreneurship, Civil Code, Tax Code and other sectoral laws.

## 5. CROSS-SECTOR COOPERATION

### Overview of the field

Cross-sector cooperation implies voluntary and partner relations among various sectors. All participants in this cooperation pursue common aim and share risks, responsibilities, knowledge and benefits. Parties to cross-sector cooperation, usually, include the state,<sup>55</sup> entrepreneurial and non-entrepreneurial entities and civil society associations. The cooperation of these three sectors is known as a flexible and effective instrument for tackling important global and national problems; it is believed that such cooperation brings together resources, knowledge and interests of each party, thereby facilitating the resolution of such social and public problems which one sector would fail to solve (CSDRG, 2012). Cross-sector cooperation is also known as Public-Private Partnership, PPP.<sup>56</sup>

There is no universal definition of cross-sector cooperation. According to the definition of European Commission, it implies cooperation between business and state for the funding, improving and managing infrastructure and public services; the IMF views cross-sector cooperation as an alternative to privatization; OECD describes it as a contractual relationship between public and private actors, where the state interest to provide public services coincides with the interest of private partners (TUAC, 2010). According to the UN, Public-Private Partnership must be a long-standing relationship where economic risks are, typically, assumed by business. Cross-sector cooperation differs from relationship arising during public procurement by its length and continuity (UN, 2008).

Governments across the world broadly apply the model of cross-sector cooperation. This approach is especially popular in Canada, India, Australia and the United Kingdom. Many countries support the development of cross-sector cooperation: for example, in 2010, the government of France allocated 10 billion euros towards this goal, while the Portuguese government allocated 7 billion euros; the government of South Korea earmarks 15% of its fiscal incentive budget for this cause; some governments have special state departments set up to promote public-private partnership (Hawkesworth, 2010).

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55 The state implies entities of central government as well as of autonomous republics and local self-governments.

56 The public-private partnership dates back to the Roman Empire. There may be recalled a number of initiatives from history when state, business and society worked jointly on this or that issues. However, PPP as a concept of consolidation and its promotion started in the 1970s.

Cross-sector cooperation also enables the implementation of development-oriented initiatives pursuing social and public benefit especially when one of the parties to the cooperation is a CSO. Such a cooperation may be either long- or short-term while the participation of business be limited to one-off financial assistance. Business engages in this type of public benefit projects not for profits, but as its CSR.<sup>57</sup> Such cooperation is especially intensive in healthcare sector.

The idea of PPP has attracted justified criticism too. In researchers' view, the majority of PPP-related decisions has served the aim of business gains to the detriment of public interest. PPP was often employed in privatization of public property and handing this or that public service to private sector, which, despite possible positive results in the short run, led to the increase in citizens' spending and decrease in the access of society to privatized services (Horvat, 2019). In response to this criticism, a new model of cross-sector partnership – Public-Civil Partnership has been developing, which envisages addressing public and social problems through cooperation and partnership between public entities and civic associations. Although this concept is in its nascent stage, examples can already be seen in the municipal governments of Barcelona, Zagreb, Vienna, Bologna, Hamburg (Horvat, 2019). The idea of Public-Civil Partnership places a special emphasis on the participation of citizens and views state and municipal budgets as well as citizen and civil association donations as sources of funding.

Cross-sector cooperation is not developed in Georgia, save some exceptions when non-entrepreneurial persons, with the state funding, render public services in various social areas<sup>58</sup> (for example, management of houses for elderly people) and grant financing of CSOs by the state.<sup>59</sup> According to a CRRC survey, out of 282 surveyed CSOs 44 named the state funding as a source of income, which comprises 40% of their income.

Apart from the above mechanisms there is no document which would determine areas or cooperation between public, private and civil sectors and the role of state in promoting it. Probability of spontaneous, un-concerted cooperation on the part of the state is not high: on the one hand, business shuns cooperation with CSOs as perceives them as politicized actors and hence, tries to avoid a possible deterioration of relation with the government (USAID, 2017) while on the other hand,

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57 For example, in 2003, upon the initiative of Federal Government of Germany, a program of PWD employment began, within the scope of which private companies and CSOs, along with state programs, provided PWDs with opportunities to develop vocational skills. Another example of this is the international initiative of AIDS vaccination which was established by public and private entities in 1996 with the aim to develop HIV/AIDS vaccine.

58 These mechanisms which, typically, rely on voucher funding, are among state funding forms and consequently, not discussed in this research.

59 This mechanism as well is viewed as a state funding and not cross-sector cooperation.

business sector does not enjoy a high level of trust in society and therefore, CSOs shun cooperation with it (CRRC, 2018).

Nevertheless, a few examples of successful cross-sector cooperation can still be cited in Georgia. The most outstanding, among them, is the construction of children's hospice when the author of the idea, Open Society Georgia Foundation,<sup>60</sup> succeeded in raising GEL 1.5 million in donation. The land for the hospice was purchased by the EVEX Medical Corporation while the largest monetary donation, GEL 220,000 was made by the Administration of President of Georgia. According to the author of the idea, in addition to citizens' donations, companies involved in the construction of the hospice, provided their services free of charge. Today, the hospice is run by a cross-sector council comprising representatives of business, CSO and arts and culture sector. So far, costs of running the hospice have been covered, along with financing from the fund, by individual donations.<sup>61</sup>

The following subchapters provide the analysis of legal framework and tax environments for cross-sector cooperation.

## Legal framework

Georgian legislation does not contain provisions regulating cross-sector cooperation; nor does it define the term “public-private partnership.” Nonetheless, by applying various legal institutions, the legislative framework allows both short- and long-term cooperation.

According to the Civil Code of Georgia, legal persons may regulate their relations and determine rights and responsibilities in agreement unless it is not prohibited by law or does not conflict with the established order. The institution of donation envisaged in Article 528 of the Civil Code enables CSOs to receive donations from business for the achievement of particular objectives. Donors may determine an objective and give financial means and other property for its achievement;<sup>62</sup> this objective may be the “common good” (Article 528).

As noted above, the state must be one of the parties to public-private partnership. According to Georgian legislation the state may be a party to contractual relationship; moreover, in specified cases, it may assume contractual obligations and demand the fulfillment of contractual terms from other parties to agreement. More-

60 Open Society Georgia Foundation is a CSO in Georgia; the author and implementer of the idea of children's hospice was Nino Kiknadze, an employee of Open Society Georgia Foundation.

61 Interview with Nino Kiknadze.

62 According to Article 147 of the Civil Code, property is all things (movable and immovable) and intangible property (e.g. right of claim), which may be possessed or does not contravenes moral standards.

over, according to the Law of Georgia on Grants, ministries, office of state ministers and legal persons in public law<sup>63</sup> may give grants (Article 3) which may become a ground for cross-sector cooperation. A state organ<sup>64</sup> may itself be a grantee (Article 4 of the Law on Grants) to implement an initiative. A different regulation is applied to self-government bodies: according to the Law of Georgia on Grants and the Local Self-Government Code, local self-government may be a grantee but municipal bodies have no grant-making power.

According to the Law of Georgia on State Property, the state has the right to transfer property to legal persons of private law, including CSOs, into their ownership, or for use without charge, for a definite or indefinite period. This right is a crucial issue for cross-sector cooperation. In addition, in accordance with the established procedure, a local self-government has the right to transfer to a CSO or business company the municipality's movable and immovable property by direct transfer, without auction, with the right to use without charge, conditionally or unconditionally. A decision on the transfer of municipality's property with the right to use without charge is made by the executive body of self-government (Mayor) with the approval of representative body of self-government (Sakrebulo) (Article 54 of the Local Self-Government Code).

It must be noted that public-private partnership may require the establishment of a new legal entity. Georgian legislation is very flexible in this regard. The state, entrepreneurial persons specified in the Law of Georgia on Entrepreneurship as well as non-entrepreneurial persons specified in the Civil Code may, in accordance with procedure stipulated in law, establish a legal entity, no matter entrepreneurial or non-entrepreneurial (Chapter II of Section I of the Civil Code of Georgia; Law of Georgia on Legal Entities under Public Law). In addition, enterprises established by the state where 50% or more of the equity is owned by the state, may even receive immovable property, that law prohibits to privatize, with the right to use without charge (Paragraph 3 of Article 36 of the Law of Georgia on State Property).

## Tax policy

The Tax Code of Georgia does not contain special provisions concerning cross-sector cooperation. Operations within the scope of such cooperation are subject to the tax regime similar to the regime applied to other entrepreneurial and social activities.

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63 Except for local self-government which has no power of grant-making.

64 According to Article 4 of the Law of Georgia on Grants, the grantee may be: the state of Georgia as the organ authorized by the Prime Minister of Georgia, the government of Georgia as the organ authorized by the government of Georgia, organ of state authority and local self-government, legal person in public law of Georgia.

The so-called Estonian model of levying profit tax, which entered into force on 1 January 2019, exempts an organization's income, including grants and donations, from the profit tax if it is used towards charitable activities defined in the organization's charter or the Code. Article 10 of the Tax Code of Georgia lists forms and types of charitable activities which include: human rights protection, protection of environment, development of democracy, culture, art, sport, education, science, health protection, development and protection of social welfare.

Furthermore, the Tax Code enables business to deduct from taxable income the value of donations.<sup>65</sup> This incentive mechanism applies only in case when business donates to a charity organization and not all CSOs (non-entrepreneurial legal persons). The rule of granting a status of a charitable organization is defined in Article 32 of the Tax Code; according to official data, there are only up to 150 organizations in Georgia with the status of charitable organization against over 20,000 organizations registered as SCOs.

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65 "not more than 10% of the amount remaining after deductions under this Code from gross income" (Article 117 of the Tax Code). A similar rule applies in case of so-called Estonian tax model which entered into force in 2017 a donation made to a charity organization during a calendar year not exceeding 10 % of the net profit gained by the organization during a previous calendar year shall not be subject to profit taxation (Article 98<sup>3</sup>).

## 6. SOCIAL ENTREPRENEURSHIP

### Overview of the field

Social entrepreneurship has been attracting a growing interest over the past few years. It implies the use of entrepreneurial methods and approaches for attaining social objectives. In other words, social entrepreneurship is a business pursuing not only the goal to generate profit or personal financial gains but also the mission to generate public benefit. Social entrepreneurship normally means the implementation of economic activity by social, non-entrepreneurial entities. A dual nature of social entrepreneurship – an underlying social objective, on the one hand, and on the other, entrepreneurial means and methods for achieving it, makes this concept somewhat difficult to handle.

Although the signs of such type of activity can be traced back to the 19<sup>th</sup> century US and European countries, the concept of “social entrepreneurship” appeared in the 1970s while its intensive development started in the 1990s (OSGF, 2017). That coincided with the period when the formation of a new world order began: the idea of great power was experiencing crisis in the US and Europe while entrepreneurial and individual initiatives were declared as a key solution to it. Today, social entrepreneurship takes on different forms and directions in various countries. Though lacking a universal definition,<sup>66</sup> social enterprise has several characteristic features (ICNL, 2015):

(1) *Governance*. Social enterprise is a voluntarily established organization that is independent in its activity and not directly subordinated to any public entity. A social enterprise may be a provider of public service but the state is not involved in its management either directly or indirectly. A social enterprise is usually established by non-entrepreneurial legal entities or, act as social enterprises within the scope of their economic activity. In exceptional cases, a legal person existing in the form of enterprise may also be considered a social enterprise. However, in such a case, it is central for this enterprise to give preference to social objective over the objective of profit.

(2) *Economic activity*. A social enterprise is engaged in a production process - producing goods and/or selling services.<sup>67</sup> In contrast to traditional CSOs and state bodies, the viability of social enterprise depends on the efforts of its employees. It

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66 According to the definition of Social Enterprise Alliance, social enterprise is an organization or an enterprise that implements social mission through an entrepreneurial approach.

67 By definition, a sphere of activity of social enterprise cannot be so-called unethical fields of economy, for example, tobacco or arms business. No other restrictions are specified in the literature.

is believed that a social enterprise cannot rely on volunteer work alone, it must use the work of at least one paid employee.

(3) *Social purpose.* A social enterprise has an explicit, identified social purpose towards which it employs production methods. Profit of a social enterprise is not distributed among its founders, but used for the achievement of social objectives. A social enterprise may allow a limited distribution of profits among its founders/shareholders, but it is prohibited to distribute the entire profit – the use of production methods to further social goals must remain underlying principles.

One in every four newly established enterprises in the EU is a social enterprise (European Commission, 2014). Each EU country went through its unique path of first, recognizing and then, promoting social entrepreneurship. However, in almost every case, social entrepreneurship was linked to ideas of social economy (ECNL, 2012). In parallel to its growing popularity, the concept of social entrepreneurship is being gradually institutionalized and politically recognized, including, in terms of new organizational-legal forms of private law entities. Several countries have a specific legal form of social enterprises; some countries apply several corresponding legal forms and social enterprises have a possibility to choose among them. In discussions about a concept of social enterprise we are recommended not to limit ourselves to one or several particular legal forms, not to confine it to organizational-legal forms but leave an open space for the implementation of such activities.

Social entrepreneurship is a relatively new concept to Georgia. Georgian CSOs are not, usually, engaged in entrepreneurial activities. The CSRDG database of social enterprises lists only 40 such enterprises. This is often explained by the lack of knowledge of entrepreneurial activity and methods.<sup>68</sup> According to a CRRRC survey, in 2016, only 56 among the surveyed 282 CSOs (20% of surveyed organizations) were engaged in economic activity, including only 23 CSOs (8% of surveyed organizations) in social entrepreneurship. The share of social entrepreneurship income in the revenues of these organizations is small, at 8%, on average (CRRRC, 2018).

The legal framework, instead of encouraging, restricts the establishment of social enterprises in many aspects. For example, state programs designed to support start-ups,<sup>69</sup> do not mention social enterprises or identify social enterprise as a priority. In the following subchapters we will discuss legal regulations and tax regime concerning social enterprises.

68 It is noteworthy that Georgian CSOs have access to international assistance in contrast to European countries where international donor assistance is restricted.

69 For example, LEPL Enterprise Georgia of the Ministry of Economy and Sustainable Development; see, <http://enterprisegeorgia.gov.ge/> [last accessed on 18.03.2019]. Also, Startup Georgia, founded by the state investment fund/joint stock company partnership fund; see, <http://startup.gov.ge> [last accessed on 18.03.2019]. None of these programs prioritize social enterprise.

## Legal framework

The Georgian legislation does not provide a specific legal form of social enterprise. Nonetheless, CSOs are not deprived of a possibility to implement such activity.

Any civil, non-entrepreneurial legal person may perform any activity which is not prohibited under the Georgian legislation. In addition, according to the Civil Code of Georgia, non-entrepreneurial person may engage in an auxiliary entrepreneurial activity<sup>70</sup> the profit from which shall be used for achieving public benefit objectives of the non-entrepreneurial legal person. In other words, according to Article 25(5) of the Civil Code, profit from auxiliary entrepreneurial activity cannot be distributed among founders, members, donors, management and persons with representative powers of the legal entity,<sup>71</sup> but used for the achievement of objectives that benefit public.

According to Organic Law of Georgia on the Suspension and Prohibition of Activities of Public Associations, a court may suspend, and in cases stipulated in law, ban the activities of those CSOs which “has substantially engaged itself in entrepreneurial activities” (Article 3). Although neither the Civil Code nor the Organic Law defines the concept of auxiliary entrepreneurial activity, it is widely accepted that “auxiliary entrepreneurship” always serves social objectives of non-entrepreneurial legal entities – the major objective of a non-entrepreneurial legal person is to make benevolent social impact while entrepreneurial activity is declared as a means to achieve this end.<sup>72</sup> Consequently, a public non-entrepreneurial legal entity has the right to perform entrepreneurial activity on any scale provided the profit for this activity is spent for attaining social goals, not distributed among founders, members and leadership. Organization distributing its profits from auxiliary economic activity among these persons instead of using towards a social goal, risks being suspended the status or even banned.

In this regard, it must be noted that CSOs find it difficult to separate income, profit and expenditure of entrepreneurial activity from those of non-entrepreneurial ac-

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70 The Civil Code does not define social entrepreneurship. According to the Law of Georgia on Entrepreneurship, entrepreneurial activity is “legitimate and repeated activity carried out independently and in an organized manner to gain profit” (Article 1).

71 Even in case of liquidation of a non-entrepreneurial legal entity, the property remaining after the liquidation is not transferred to founders, members, donors or managers. According to Article 38 of the Civil Code, the property remaining after the liquidation is transferred to another non-entrepreneurial legal person pursuing similar objectives, or the state, in accordance with the rule stipulated in the law.

72 According to the decision #3k/939-01 of the Supreme Court of Georgia, “registration may only be abolished when this organization materially moves to commercial activity [...]. This will occur only when it becomes established that the profit generated by economic activity is distributed among members of the association.”

tivity. With two types of revenue – taxable and non-taxable, CSOs find it difficult, for example, to exactly identify when separate resources were used for entrepreneurial and non-entrepreneurial activities. To eradicate this and similar problems, the Georgian legislation allows a non-entrepreneurial legal entity to establish an entrepreneurial legal entity. Such entrepreneurial legal entity will be able to engage in economic activity without any limitation while the sole beneficiary of the profit will be the founding non-entrepreneurial entity which shall sue the profits for furthering social objectives. An enterprise established in this form is a social enterprise as it channels all its profit towards attaining a social goal.

Along with the regulatory legislation, we should mention the access of social enterprises to finances. According to the Law of Georgia on Grants, entities specified in the Law on Entrepreneurship,<sup>73</sup> are not eligible for grants. Moreover, means obtained by CSOs engaged in economic activity for entrepreneurial aims shall not be regarded as grants<sup>74</sup> (Article 2). Thus, the Georgian legislation does not qualify the means used for entrepreneurial purposes as grants regardless of legal status of a giver or receiver of these means.

It is worth to note that the Parliament of Georgia is now in the process of considering the draft legislative amendments prepared by the Center for Strategic Research and Development of Georgia,<sup>75</sup> which aim to regulate social entrepreneurship and determine the state policy framework for its development. According to the proposed amendments, a social enterprise shall be defined as a legal person<sup>76</sup> duly registered under the Georgian legislation, which (a) is established to promote social equality, employ vulnerable groups, also achieve social aims in the fields of education, culture, health care, sport and environmental protection; (b) carries out entrepreneurial activity and a large part of its income is made up of proceeds from entrepreneurial activity; (c) reinvests at least 70% of its profit into activity carried out towards the achievement of social goals declared in its charter; (d) is run by democratic principles and can make changes to its charter and the goals declared in its charter by at least 80% of the votes; (e) is not linked or subordinated, either directly or indirectly, to central or local government bodies. According to the package of amendments, decision making in a social enterprise does not depend on the amount of share or stocks of founders, but on the principles of free will, democratic management, social responsibility, justice, equality, transparency and sustainability.

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73 Entities specified in the Law on Entrepreneurship are: a limited liability company, joint-stock company, cooperative, general partnership, limited partnership, individual entrepreneur.

74 The exception to this rule under the law is means received by an entity having the status of agricultural cooperative and amount received to attain political aims.

75 The draft legislative amendments, relevant conclusions, explanatory notes and other material are available at the website of the Parliament. See <https://info.parliament.ge/#law-drafting/12813> [last accessed on 18.03.2019]

76 According to draft legislative amendments, a social enterprise may register as a limited liability company, a joint stock company and a cooperative.

In the event of adoption of the draft law, the state will assume an obligation to support the development of social entrepreneurship and enhance possibilities for social enterprises to obtain soft loan resources and grants. Furthermore, according to the draft law, the state will assume an obligation to give, in the event of equal conditions, preference to goods and services of social enterprises in public procurements.

## Tax policy

the Georgian legislation does not specify a special status of social enterprises. Consequently, the Tax Code of Georgia does not contain provisions which would set a different tax regime for social enterprises. The taxation of a Georgian social enterprise depends on its legal form.

Let's first discuss a social enterprise with a legal status of non-entrepreneurial (non-commercial) legal entity and is engaged in ancillary economic activity. Article 9 of the Tax Code defines economic activity as any activity undertaken to gain profit, income or compensation, irrespective of the results of such activity; while according Article 32(3) of the Tax Code, ancillary economic activity that serves the main purposes of an organization shall not change the organization's charitable character. Hence, an organization is entitled to carry out an economic activity – an *ancillary* nature of this activity only means that the profit and income received shall serve the main purposes of the organization. The Georgian legislation prohibits the distribution of profit from such activity among management and persons with representative power.

On 1 January 2019, the so-called Estonian model of levying profit tax entered into force, fundamentally changing the peculiarities of CSOs taxation. According to the amendments, a taxable amount for levying the profit tax on an organization is not a type of income – be it a grant, donation or ancillary economic activity, but the conformity of spending by an organization to the organization's purposes declared in its charter. According to a new wording of Article 97 of the Tax Code, an organization engaged in an ancillary economic activity will be subject to the profit tax if it has: (1) made the spending that is not related to economic activity; (2) made the spending that is not related to purposes of its activity or charitable activity specified in the Tax Code;<sup>77</sup> (3) made the spending that is not related to the aim of grant agreement; (4) provided goods/services free of charge, that is not related to purposes of its activity; (5) made a representative spending that exceeds the limit set in the Tax Code.

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<sup>77</sup> Article 10 of the Tax Code of Georgia lists forms and types of charitable activities which include: human rights protection, protection of environment, development of democracy, culture, art, sport, education, science, health protection, development and protection of social welfare.

As regards social enterprises with entrepreneurial status, they do not enjoy tax benefits of other type. Much like legal entities specified in the Law of Georgia on Entrepreneurship, they are exempt from profit tax except in cases when obtained profit is distributed in the form of dividend or envisages such distribution that is not related to the business activity of the entity. Thus, the new model envisages taxation not upon the receipt of profit but upon the distribution thereof.

Apart from profit tax, benefits are established for organizations on property tax too: property tax is not levied on the property<sup>78</sup> of an organization if it is not used for economic activity whereas the property which is used for economic activity is subject to the property tax. Consequently, a CSO that carries out ancillary entrepreneurial activity is not exempt from the property tax.

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<sup>78</sup> This does not apply to the property of organization in the form of the land.

## 7. COMMUNITY FOUNDATION

### Overview of the field

Community foundation is a charity community organization which works to improve the quality of life of population in a defined geographic territory. Activity of community foundation, usually, implies pooling financial means to support charity and public benefit activities. The main source of income of community foundation is donation from citizens, families and business in a defined geographic territory. However, community foundations are not prohibited to receive state grants and international assistance. It is worth noting that community foundations finance not only charity initiatives but business start-ups and social enterprises pursuing the goal of empowerment of local population (Garson, 2013; Sacks, 2014).

The first community foundation was created in the United States, Cleveland (Ohio) in 1914 and then spread to other US cities and towns. According to the data of Community Foundation Atlas,<sup>79</sup> 1,863 community organizations exist across the world.<sup>80</sup> The total budget of community foundations exceeds \$5 billion. Community foundations largely support education of community members, social services, development of arts and culture and health care<sup>81</sup> (CFA, 2014).

Community foundation is viewed as a mechanism for dealing with problems of a community in a particular territory - a region, city, village or neighborhood. Apart from pooling financial resources to tackle community problems, community foundations contribute to the development of social trust among citizens by enhancing a shared sense of community and focusing on common problems (Graddy & Wang, 2009). In this context it is important that when planning its activity, a foundation conducts a poll of citizens and also reports on the performance to the population of the community. While recognizing benefits of community foundations it is important to note that it cannot replace the responsibility of a local government and the state to solve complex problems such as, for example, poverty, social exclusion or homelessness. In researchers' view, community foundation may facilitate the solu-

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79 Community Foundation Atlas is a project of Cleveland community foundation, which was created in 2014 to mark the 100<sup>th</sup> anniversary of the foundation. The project aims at gathering information about community foundations worldwide and promoting them. For additional information see, [communityfoundationatlas.org](http://communityfoundationatlas.org) [last accessed on 18.03.2019].

80 According to the same data, community foundations operate in North America – 1032, Europe – 678, Asia – 62, Oceania – 56, Africa – 31 and South America – 11.

81 Other priority areas are: environmental protection (9.6%), child support (8.7%), economic development of community (5.9%), housing issues (3.3%). For additional information, see [communityfoundationatlas.org](http://communityfoundationatlas.org) [last accessed on 18.03.2019].

tion of social problems, but cannot take efforts which must be undertaken by the state (Harrow & Jung, 2016).

As many as 70% of current community foundations have been created over the past 25 years. According to a global research, the establishment of community foundations is, more frequently, the result of efforts of community leaders and community activism. Among important factors encouraging the creation of a community foundation is the desire of community to make change in their economic situation and a preferential legal and tax environment ensured by the state (CFA, 2014). The key area in the activity of community foundation is grant-making in prioritized areas. A grantee may be a natural as well as a legal person. Community foundations often cooperate with schools, universities CSOs and enterprises operating in their defined territory. A community foundation is, typically, governed by a council comprising representatives of various interest groups (Hoyt, 1996).

Community foundation is not a common practice in Georgia; nor is a state concept developed on the creation of such foundations. Nevertheless, with the assistance of Taso Foundation,<sup>82</sup> for example, several community foundations were established in various regions of Georgia. According to official information, with intellectual and technical assistance from Taso, 14 community foundations operate in various regions of Georgia;<sup>83</sup> 11 of them are registered organizations, eight organizations already has some grant-making experience and five are unregistered. The registered foundations are non-entrepreneurial entities. According to information provided by Taso, several community foundations operate only within the territory of one village, though there are foundations that cover several villages. It is also worth noting that some community foundations have identified priority areas, for example, domestic violence and women's rights, while others do not define such thematic limits and work on all problems of relevant communities. Over the period between 2013 and 2016, Taso-supported community foundation financed 90 small grant projects with the total value reaching GEL 84,778. Projects financed by them include improvement works on roads, squares, village library, kindergarten as well as empowerment of women and protection of their rights, development of computer skills among population, initiatives of citizen participation in local self-government.<sup>84</sup> In the following paragraphs we will discuss legal and tax environment related to community foundations.

82 Taso foundation is a Georgian CSO, affiliate of Open Society Georgia Foundation, which works on women's right and supports philanthropic activities. Taso Foundations defines a community foundation as "such conscious activity of community, which helps perceive common work as personal work; this is a responsibility not only for personal but also shared property, interests, environment and people. This is a will to make change in joint effort, to facilitate social changes and to live a decent life."

83 According to information provided by Taso Foundation, community foundations operate in Kakheti, Shida Kartli, Mtskheta-Mtianeti, Samtskhe-Javakheti, Samegrelo and Imereti.

84 Interview with Marina Tabukashvili, the manager of Taso Foundation.

## Legal framework

The Georgian legislation does provide a special legal status of community foundation. However, the existing legislative framework allows the establishment and operation of community foundation.

A community foundation may be established in Georgia as a non-entrepreneurial legal entity defined in the Civil Code. According to the Civil Code of Georgia a non-entrepreneurial legal entity may perform any activity which is not prohibited under the Georgian legislation. Such activities include pooling assets for the support of charitable, social, cultural, scientific-research and educational activities and then, giving it for these reasons. Besides, a non-entrepreneurial legal person may determine an acceptable form of governance and set a corresponding governing body. It should be noted that the Civil Code allows a non-entrepreneurial legal person to perform its activities in a defined geographic area – region, city, village and community (Book I, Section I, Chapter II of the Civil Code). As noted above, such a power is vital for the concept of community foundation.

The Civil Code allows a non-entrepreneurial legal entity to receive membership fees and donations.<sup>85</sup> According to the Law on Grants, a non-entrepreneurial legal entity may get and give grants as well as get a state grant. Several ministries<sup>86</sup> of Georgia already give state grants (Articles 2-4 of the Law on Grants).

One of important issues seen as a problem by community foundations is that the absence of grant-making power of self-governments.<sup>87</sup> The Law of Georgia on Grants, much like the Local Self-Government Code, does not authorize local self-governments to issue grants to community foundations. Given that community foundations have no access to international financing and do not receive large individual and corporate donations either, grants from local self-governments would significantly enhance their viability.

It should also be noted that at the end of 2016, the Parliament of Georgia adopted the Law on Volunteering which enables non-entrepreneurial legal persons, including community foundations, to use work of volunteers.<sup>88</sup>

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85 Donations include all movable and immovable property, intangible assets and financial means (Civil Code of Georgia, Articles 528 and 147).

86 It should be noted that procedures for awarding grants, approved by ministries of Georgia, are not uniform.

87 The manager of Taso Foundation regards prohibiting local self-governments to award grants as one of most important shortfalls of the legislation.

88 A volunteer is a person who voluntarily and gratuitously helps a CSO in attaining its objectives. A volunteer may be a natural person who has attained the age of 16. See, the Law of Georgia on Volunteering.

## Tax policy

The Tax Code of Georgia does not set a special taxation regime for community foundations. Consequently, they are taxed as other non-entrepreneurial legal persons. In the following paragraphs we will review those provisions of the Tax Code, which have a special meaning for community foundations.

According to the Tax Code of Georgia, effective before 1 January 2019, profit tax exemption applied to grants,<sup>89</sup> membership dues and donations to community foundations. Donation, was defined in Article 8(40) of the Code as funds, goods and services provided as gifts. According to the wording enforced on 1 January 2019, a community foundation having the status of non-entrepreneurial legal entity is exempted from profit tax in accordance with the procedure specified in Article 97(3) of the Tax Code.

There is another important issue that concerns the taxation of community foundations. Although volunteers do not receive salaries, activities performed by them for community foundations involve some costs, for example, transportation and communications costs. Such expenses, according to the Law on Grants, shall be compensated by host organizations (Article 5). It is noteworthy that the Tax Code qualifies such compensation to a volunteer as a taxable income and accordingly, levies income tax.<sup>90</sup> As a result, the cost of the use of volunteer work increases for community foundations, as they have to “top up” a compensation intended for volunteer with the income tax. Such approach is known as “volunteer tax” in literature.

Donors to community foundations may be both natural and legal persons.<sup>91</sup> According to the Tax Code, if individual donations to an organization are used for charitable purposes declared in a charter of the organization or defined in the tax Code, the organization is exempted from the profit tax.

89 A grantee who buys goods provided in the grant agreement and/or receives services under the same agreement in compliance with the legislation of Georgia, may obtain a deduction or refund under this article of the value added tax paid for such goods/services (Article 63(5) of the Tax Code). Moreover, the import of goods under the grant agreement is exempted from the tax (Paragraph 3, Article 63 of the Tax Code).

90 According to Article 100(3) of the Tax Code, gross income is income earned in any form and/or through any activity, namely: a) salary income; b) income earned from economic activity, which is not related to employment; c) other income not related to employment and economic activity. Thus, compensation given to a volunteer is income and a host organization, as a tax agent, shall deduct income tax (save the exceptions stipulated in the Tax Code).

91 See, Articles 98<sup>3</sup> and 117 of the Tax Code of Georgia which specifies incentive mechanism for business donations.

The Tax Code of Georgia also provides an incentive mechanism of corporate donations for business companies.<sup>92</sup> Article 117 of the Code enables business to deduct from taxable income the amount donated to a charitable organization, also the market price of goods<sup>93</sup>/services supplied free of charge, but “not more than 10% of the amount remaining after deductions under this Code from gross income.” A similar rule has applied to entrepreneurial subjects under the so-called Estonian tax model enforced since 2017: a donation made to a charity organization during a calendar year not exceeding 10 % of the net profit gained by the organization during a previous calendar year shall not be subject to profit taxation (Article 98<sup>3</sup>). This rule may be applied by entrepreneurial subject to community foundations having a status of charitable organization. The rule of granting a status of a charitable organization is defined in Article 32 of the Tax Code.

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92 Similar mechanism is practiced in many countries across the world and is aimed at encouraging corporate charity (BTD, 2013).

93 Other than immovable property; the Tax Code does not apply the procedure specified in Article 117 to immovable property donated by business to a charity organization.

## 8. CROWDFUNDING

### Overview of the field

Crowdfunding is a relatively new form of non-state funding of CSOs. It means raising money on a large scale through various campaigns by CSOs.<sup>94</sup> In such cases, CSOs call on citizens to donate money for a particular public benefit activity.<sup>95</sup> In applying this funding mechanism, CSOs pursue the objective of reaching as many people as possible as because citizens, typically, make small donations. In 2014, the European Commission held public consultations on potential benefits of crowdfunding and established that with this mechanism CSOs may alleviate their dependence on traditional sources of income and stir up interest among citizens towards tackling common community problems (European Commission, 2014).

Crowdfunding is typically carried out via electronic platforms. There are international as well as regional and national platforms<sup>96</sup> that connect CSOs with citizens and offer them online modules of money transfer. According to the European Center for Not-for-Profit Law (ECNL), national platforms are more effective as citizens of a relevant country better understand the context of a particular activity and also, are not charged a high banking fee on the transfer of donation (ECNL, 2014).

According to the CSO Sustainability Index of the US State Department, crowdfunding has been gaining in popularity as a source of funding in Eastern Europe and Eurasian region. While, in the past, used mainly for raising funds for social, humanitarian and environmental issues, crowdfunding is already applied for financing initiatives such as same-sex marriages, exposing corruption of high officials, et cetera (USAID, 2017). Besides, according to the Index, this non-state funding mechanism has been taking on a new dimension in countries where governments restricted the access to international financing. For example, in 2015, in Belarus, CSOs raised \$160,000 through this mechanism and almost doubled the indicator in 2016. In parallel to emphasizing the benefit of crowdfunding, CSOs also note an

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94 Crowdfunding mechanism is used by business too when, for example, reis to raise funds for a business initiative through public offer of shares. Such relations in Georgia is regulated by the Law of Georgia on Securities Market. This issue is not addressed in this research.

95 There are various models of crowdfunding. One of them is citizens' donation to CSOs and this form is applied by CSOs. Other forms, for example, when small investors get share in equity instead of funding, is not virtually used by CSOs.

96 Examples of international platforms are: Causes.com, Kickstarter.com, Crowdrise.com. As regards national platforms, the Czech Republic has darujme.sz, Slovakia - Darujme.sk and startlab.sk, Poland - Dobroczynosc.com [last accessed on 18.03.2019].

instable nature of this mechanism which makes it only an auxiliary mechanism of raising funds (USAID, 2017).

Crowdfunding is not much practiced in Georgia. According to CRRC survey, only 11 of 282 surveyed CSOs (CRRC, 2018) applied this mechanism. Although electronic donation modules have appeared on webpages of CSOs, organizations do not take much effort in this direction. It should be noted as well that a few organizations used this mechanism to raise funding for separate initiatives in the past few years. An example of this is the organization, Soviet Past Research Laboratory, which implemented several research projects with the donations from citizens and published books about Soviet and pre-Soviet past of Georgia. According to the manager of the organizations, they intend to use this model for preparation of new publications in future too.<sup>97</sup> The following subchapters offer a review of legal and tax environment of crowdfunding.

## Legal framework

Crowdfunding is a legal activity under the Georgian legislation. CSOs are allowed to perform any activity not prohibited by law. True, the legislation does not mention the concept of crowdfunding, but the institution of gift and donation enables such legal relationship. According to Articles 524 and 528 of the Civil Code, CSOs may receive gifts and donations from natural and legal persons. The Civil Code does not differentiate between an individual donation and a donation through crowdfunding.

## Tax policy

The Tax Code of Georgia does not contain any special provisions for regulating crowdfunding campaigns. However, any donation from a natural person to a CSO is exempt from profit tax regardless of the amount of donation (see the chapter on individual donations). Tax regulation of corporate donations in case of crowdfunding was discussed in the subchapter on corporate donation.

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<sup>97</sup> Interview with Irakli Khvadagiani, a researcher at Soviet Past Research Laboratory.

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