Public Finance Management Guidebook

October 2019

This page intentionally left blank.

TABLE OF CONTENTS

PREFACE

Dear Reader

Georgia has received a credit from the World Bank (WB) and a grant from the Swiss Development Cooperation (SDC) in order to support decentralization and Local Self-government (LSG) reforms. The project "Strengthening the Institutional Capacity of Georgian Local Self-Governments" being a part of the Second Regional and Municipal Infrastructure Development Program is supported through this funding. The Project Development Objectives are to:

A) Improve the efficiency and reliability of selected municipal services infrastructure;

B) Contribute to the establishment of an effective local self -government system.

The Second Regional and Municipal Infrastructure Development Project (SRMIDP) is an ambitious program that focuses on three different areas of need with a separate project for each:

1. Spatial Planning, Asset Management and Capital Investment Plans
2. Project Cycle Management
3. Improved Fiscal Discipline and Accounting System

The Improved Fiscal Discipline and Accounting System (IFDAS) project is being implemented by Cardno, Emerging Markets USA, Ltd. with support from its Georgian partner Centre for Training and Consultancy (CTC). The project is implemented under the supervision and coordination with the Municipal Development Fund (MDF), the Ministry of Regional Development and Infrastructure of Georgia (MRDI) and the Ministry of Finance of Georgia (MoF).

Fiscal discipline in the context of this project implies the improvement in understanding of the financial situation of the LSGs in order to render sound budget and budget execution decisions based on accurate and comprehensive accounting information.

The IFDAS project vision is to "achieve the highest possible efficiency, transparency and accountability in the allocation, management and use of public finances to meet the Local-Self Government's development and economic growth priorities remaining cognizant of its fiduciary responsibilities."

All IFDAS project activities are orientated at improving the numerical accuracy as well as upgrading Local-Self Government competencies in both "producing" financial management working products and the ability to use these in a positive, proactive manner for the betterment of the constituencies they represent.

Financial management in local government is practiced, world-wide as a part of public finance, to achieve specific objectives; to provide the desired services in the most cost-effective manner. Central to this is building a strategic core "financial management team" with skills for more effective general financial management and for undertaking financial improvement planning.

Sound financial management in any field requires proper financial reporting. No accurate analyses can be done, or decisions rendered, and results evaluated if the financial data on which the analyses are based and decisions made, were incorrect. This Public Finance Management Guidebook was created considering this, and integrates comments and issues communicated by the LSGs. Financial management starts with – sound accounting, compliance with the laws and controls.

This Guidebook is intended to build skills and capacity of local government personnel and related professionals to engage in improved financial management of local governments. Its primary purpose is to provide a user-friendly tool for implementing good practices and improving key accounting processes that are in use in the Local-Self Governments. In addition, the Guidebook provides through its design an extremely useful upgrading in financial management competencies for all LSG administrative staff and municipal officials. It achieves this by addressing financial management practices such as budgeting, internal controls and funding, in addition to incorporating a foundation of accounting regulations and practices upon which financial management exists.

It includes source documents used, reports issued, accounting procedures, and the applicable statutes and policies. It is hoped that the manual is regularly used as a reference, in addition to train staff. These activity will facilitate consistent treatment and application of the accounting policies and procedures.

Please also note that the Guidebook is accompanied by a compendium of relevant laws: "Local Self-Government Accountant's Laws and Regulations Helper". This document provides the details of the most relevant legislation and is an integral element in gaining and maintaining subject area knowledge.

To assist develop fundamental understanding of the subject area, this Public Financial Management Guidebook contains two chapters addressing budgeting - #16 – Budgeting and # 17 Linking Program Budgeting with Financial Management. Each of these chapters provides sufficient information on the subject areas to equip readers with knowledge necessary to be cognizant. Further to note is that an additional guidebook is available: "Guidebook for Effective Program and Performance-based Budgeting" This document provides users extensive information and instruction on program budgeting. Since 2014, local governments have been required to develop budgets based on program budgeting (PB) methodology. The Guidebook is intended to serve as a set of simple, user-friendly instructions and illustrative examples that will assist local governments in successfully implementing their program and performance management systems, and is aligned with MoF order No. 283, of July 27, 2018.

This Guidebook as well as all other guidance materials should not be seen or allowed to be static, but rather be a living documents which will be adapted and changed as circumstances dictate. Please be certain that the latest revision is in hand. You will note this by the issuance date on the cover. Furthermore, your comments, observations and contributions will assist in ensuring all materials are up-to-date.

Introduction

A) Financial management in relation to Local-Self Governments activities is of utmost importance. Therefore, we as public servants have to convince our stakeholders that resources like finances, human resources and opportunities made available to the LSG are utilized strictly in accordance with laws, regulations, and directives and only for the purpose for which they were intended. For that reason, every individual involved in the management of LSG resources must have a clear understanding of LSG financial management procedures. Sound Local-Self Government Financial Management can only be realized if there are clear and comprehensive guidelines. The primary objectives of the PFM Guidebook are to: Ensure that all transactions that give rise to receipts and payments of Income and Expenditure, Assets and Liabilities are accurately and properly recorded

B) Give Local Authorities timely and reliable information of the running of their day to day activities

C) Provide a sound framework for financial management and control to Local Government Authorities.

Each chapter of this guidebook starts with a section on “Relevance”. The objective of this section is to provide information to the readers in a non-technical manner. Ideally all persons associated with the management of the LSG should have knowledge of financial matters. This knowledge will better enable them to perform their fiduciary duties. With the “Relevance” paragraph, the guide book provides users an introduction to the subject matter and explains its relevance to the effective financial management of an LSG. For those persons who wish to have additional information they need only read further on into the main text of the chapter.

Also, in relation to exercising proper discharge of fiduciary duties, a separate chapter #18 “The Internal Control System and Process”, is provided. It is strongly recommended that all who access this guidebook read this chapter. Furthermore, throughout the guidebook relevant internal controls have been embedded into the text.

This page intentionally left blank.

1. Accounting and Financial Management Organization

Relevance

The Information below will help us understand how the accounting and financial management functions work at the LSGs. It gives an idea of the roles and objectives of these functions. It also describes main activities and their end objectives. Although financial accounting data is primarily historical the information it contains is also essential to manage current operations, and for planning and decision making towards the future.

The money used by the LSGs is public money and the public has both a need as well as a right to satisfy themselves either directly or through their appointed representatives that the money which they have been required to contribute for a specific purpose has been used properly for that purpose only. This is one of the objectives of the LSGs accounting system, to demonstrate proper financial stewardship. In order to achieve this objective, the accounts must achieve the following requirements:

- Conforming to statutory requirements
- Distinguishing between expenditures by their nature and type
- Relating expenditures to approved (budgeted) estimates
- Enabling the determination of proper rates of charge for goods and services provided as well as for local taxation, licenses and fees
- Providing any financial information as is necessary for the proper management of the local-self-government operations and activities
- Present a true, clear and permanent record of all financial transactions engaged in by the LSG.

To be able to work in the financial department, it is important to know how accounting and financial management is organized. This knowledge is essential for government authorities as well as for all those involved in the budgeting process. Each member of the LSG personnel will have to regularly use accounting and financial management function to withdraw numeric data and develop structure for the plan performance and achievement of pre-defined objectives.

Accounting, as an activity, enables the financial definition of property, capital, revenues, expenses and the final outcomes of the LSG operations. This is accomplished in general by financial reporting of cash-based transactions, and what is most important, the chronological accounting of economic events.

Unlike other forms of accounting (managerial, operational), Financial Accounting flow is uninterrupted, using related standards and statutes and providing relevant data to the consumers of this information. The consumer must have sufficient specific knowledge. Accounting method is a compilation of rules and measures the use of which enables obtaining, processing and transfer of information on assets, capital, liabilities, revenues and expenses of the LSG.

The LSG accounting standards are defined in Georgia by the Ministry of Finance.

These accounting standards are built on a foundation of accounting conventions. The following conventions are observed by the LSG accounting standards.

A) Conservatism Convention: This convention states that in case of any doubts about the accounting treatment (i.e. recording), the treatment which minimizes the reported profit and/or asset valuation or maximizes the reported loss figure and/or liability valuation should be used.

B) Consistency Convention: This convention states that where the is doubt, a transaction shall be treated in the same manner as other transactions reasonably considered belonging to the same class or nature. It also states that accounting policies shall not be changed arbitrarily, they must be fully justified, and all parties affected by the changes must be provided sufficient notice.

C) Materiality Convention: This convention means that the size of an amount will influence how it is treated in the accounts. Where detailed analysis or the calculation of a precisely accurate figure would involve extra-ordinary challenges, expense or significantly delay a task completion disproportionate to any advantage to be gained from such precision, a reasonable approximation shall be acceptable.

D) Substance over Form Convention: This convention requires that where there is doubt, the accounting treatment shall be adopted which exhibits the economic substance of the transaction while remaining compliant to laws.

Accounting statutes for public entities financed from the LSG budget are regulated by the Order #1321 of the Minister of Finance of Georgia dated December 28, 2007 on “Approval of Accounting Instructions for Organizations Financed from The Budget of Autonomous Republics and Local Self-Governments.” Although we also need to consider that the Georgian Legislation integrates Order #70 of the President of Georgia dated February 6, 1998 on “Approval of Resolution on Accounting and Reporting in Georgia.” It should be noted that there are some discrepancies between the above two normative acts in certain provisions. However, they have no material impact upon activities, they are a fault of the legislation

These documents provide for the following:

Organizations shall perform accounting on paper or by an electronic system in accordance with the methodology and chart of accounts defined by the Minister of Finance.

Accounting shall be performed in accordance with the approved chart of accounts, creation of additional accounts is not allowed. The LSG is entitled to introduce sub-accounts for further breakdown/detailed accounting.

In cases where they are implementing the projects within the frameworks of international agreements (including preparatory phase), entities are allowed to use international accounting standards if so, specified in the agreement.

Financial reporting shall be performed in accordance with the current Georgian legislation, which requires application of International Public Sector Accounting Standards (IPSAS) - Cash Basis.

It must be noted that the current guidebook does not cover accounting rules and methods as a whole. Entities are authorized to work out specific methodological instructions and rules and forms for internal accounting, compliant with the single methodology and current legislation, that need to be approved by the head of the LSG.

Related laws and regulations include:

- ✓ Order #1321 of the Minister of Finance of Georgia dated December 28, 2007 on “Approval of Accounting Instructions for Organizations Financed from The Budget of Autonomous Republics and Local Self-Governments.”
- ✓ Order #70 of the President of Georgia dated February 6, 1998 on “Approval of Resolution on Accounting and Reporting in Georgia.”

- ✓ Order #174 of the Minister of Justice of Georgia dated June 15, 2007 on “Rules of Entities’ Archive Operations”
- ✓ Order #72 of the Minister of Justice of Georgia dated March 31, 2010 on “Approval of The List of Typical Managerial Documents Created During Operation Process (Including Their Storage Duration).”
- ✓ Order #449 of the Minister of Finance of Georgia dated February 4, 2011 on “On Approval of Forms for Source Documents and Accounting Registries for Budgetary Organizations.”

1.1 Accounting Service Functions

Accounting is performed by the accounting service of the organization. Local Government Authorities are required by law to maintain accounting records so as to demonstrate how taxpayer’s money has been put to use. Additionally, as an information system, accounting serves individuals both inside and outside the organization.

Accounting can be defined as “the process of identifying, measuring and communicating economic information to permit informed judgements and decisions by users.” Every one of the activities undertaken in an accounting process has one or more of the below listed particular significances:

A) Analyzing: The accounts clerk or other accounting staff will determine the financial significance of each transaction or event in order to record it properly in the books of account.

B) Recording: Writing up the financial data in the books of account so that they will constitute a permanent and easily readable record.

C) Summarizing and calculating: The process of bring together and aggregating various items of financial information to determine or explain a particular result or event

D) Reporting: Communicating the results. In accounting it is usual that this is done arranged as tables – i.e. financial statements rather than as narratives. This said however, both numeric as well as clear, straightforward narratives must always be requested.

E) Interpreting: Focusing attention on the significance of various financial matters and relationships. It should be noted that this activity represents the difference between a “bookkeeper” which is occupied with items A through D above and an Accountant – who also perform A through D above – however they add additional value thru engaging in E; interpreting and bringing accountability to accounting.

With respect to presentations resulting from interpretation, best practices find accountants using percentages, footnotes, and other visualizations (graphs, charts, etc.) which assist users understand the information. This is of particular importance when presenting financial information to users with limited or no accounting background, be it members of the LSG Management, the local council, or the general public.

The accounting sub-division functions may be defined by the internal regulations of the LSG, though they should conform to the current legislation of Georgia setting out those necessary rights and obligations binding upon the accounting sub-division. These normative acts include Order #70 of the President of Georgia dated February 6, 1998 and Order #1321 of the Minister of Finance dated December 28, 2008.

Based on the Law on Normative Acts, the above listed (National) normative acts prevail over any of the local government normative acts.

Functions of accounting service are as follows:

A) Ensure correct organization of accounting in compliance with the law;
B) Control over targeted use of cash and tangible assets;
C) Control over timely registration of source documentation of economic events in compliance with the law;
D) Recording of economic events according to budget-based financing and other sources of financing as allowed by the law;
E) Timely accrual of salaries and other disbursements related to employees and control over cash outflow;
F) Complete and timely accounting of payments resulted from economic operations with legal and physical entities;
G) Integration of non-financial and financial assets (liabilities) and other accounts receivable (payable) in inventory and reflection of inventory results in accounting;
H) Financial reporting preparation with preliminary approved form in due time;
I) Storage and achieving of accounting documents, both paper and softcopies;
J) Other functions as defined by the legislation.

Performance of cash operations within the LSG is a function assigned to the accounting sub-division and is performed in accordance with the Order #49 of the Minister of Finance of Georgia dated February 4, 2011 on "Approval of Instructions for Rules for Public Entities' Cash Organization and Operation."

The order requires accounting service upon receipt of documentation (incl. softcopies) and notices with a pre-defined forms and in accordance with rules to the accounting service as a mandatory for all organizational structure and employees of organization. No accounting transactions are recorded without proper documentation

Source documents received by the accounting service are subject to mandatory checking/validation as in terms of form (complete and properly formalized, with all details filled) and contents (legality of economic operation, logical conformity of separate parts) as well as arithmetically. All documents presented are validated for accuracy, completeness, compliance and authenticity

Those persons that have prepared, and signed source documents are responsible for due and qualitative preparation as well as accuracy and reliability of the data stated in the document.

Accounting documents shall be stored at the accounting service under responsibility of designated people before sending them to archive.

Archive operation rules and storage durations are defined by the following orders of the Minister of Justice of Georgia: Order #174 dated June 15, 2007 on "Rules Of Entities' Archive Operations" and Order #72 dated March 31, 2010 on "Approval Of The List Of Typical Managerial Documents Created During Operation Process (Including Their Storage Duration)."

1.2 Rights and Obligations of the Accountant

As mentioned above, accounting is headed by the Chief Accountant or the accountant if the LSG does not have its own accounting sub-division or service.

The Chief Accountant (Accountant) is acting in compliance with the current legislation and other normative documents approved as per the rules and is responsible for compliance with general accounting methodological principles.

The Chief Accountant (Accountant) shall ensure complete recording and control of all economic operations performed by the LSG on the LSG's accounts, timely preparation and submission of operational information and accounting reports.

In case the Chief Accountant leaves (lay off, rotation, etc.), the accounting and financial reporting documents shall be transferred to a newly appointed Chief Accountant based on a delivery/acceptance act. In case of absence of such a newly appointed Chief Accountant – to an employee appointed as an acting Chief Accountant on the basis of order of the head of the LSG.

Accounting documents describing economic events of the LSG are signed by the head of the LSG (authorized person) and an accountant, or their designated substitutes. Bank cheque, payment orders and salary payment orders are signed by the head of the LSG and cashier or their designated substitute (in case the salaries are paid by wire transfer to personal bank accounts of employees, signatories are head of the LSG and an accountant), cash revenue orders are signed by chief accountant and cashier.

Work distribution between employees of the accounting sub-division and definition of their rights and responsibilities is utmost important. This shall be regulated by internal regulations. Job description of each accountant shall define the list of his/her obligations and works shall not be duplicated.

For example, distribution of work between the accountants can be done based on budget programs: Each accountant shall receive, check and register documents (agreement, delivery-acceptance act, advance payment guarantee, etc.) of economical operations performed within the frames of a certain project; ensure necessary preparations for tax payments to the treasury electronic system, including registration of agreements, liabilities and payment orders; and storage of accounting documentation.

For accurate accounting, not only recording of budget program operations is necessary, but also all economic events that influence the LSG's assets, liabilities and net value, e.g. recording of free-of-charge received or transferred property, property realization accounting, assets revaluation, etc.

It is necessary to record flow of material supplies, fixed assets and low-cost long-term assets (by inventory card) and at least one accountant shall be responsible for this work.

Equally important is preparation of financial reporting. As a rule, financial reporting is prepared by the Chief Accountant. For preparation of financial reporting it is necessary to perform uninterrupted accounting that involves all employees of accounting sub-division; coordination of their working process must be a prerogative of the Chief Accountant.

1.3. Accounting Source Documentation

Basic accounting documents of the LSGs are those which form the basis for initiating most accounting transactions. These documents can be grouped into three categories: receipts, payments, and order forms.

Order # 1321 of the Minister of Finance of Georgia on "Approval of Accounting Instructions for Entities Financed from The Budget of Autonomous Republics and Local Self-Governments" reads that the basis for accounting entry are source documents, reflecting performance of economic events.

Operations (cash outflow, spending of inventory, write-offs, formation of accounts payable and receivable cannot be recorded in accounting without properly prepared documents. Thus, in case of performance of any economical operation, appropriate documents shall be formalized. Indeed, source documents shall be worked out during the process of the relevant economical operation, if it is not possible, then upon completion of the operation and documentation shall be submitted to the accounting sub-division not later than the next working day, if not otherwise defined by the organization.

Source documents shall be prepared with high accuracy. It shall include details as follows: name of the document, date, scope of economical operation, measure unit, name of the parties of the operation, signatures of people responsible for performance of operation and due formalization of document and other information related to the scope of operation and character of data technological processing. Authors and signatories of the document are responsible for reliability of data, quality and timeliness of it.

Cash operation documents are formalized and recorded in accordance with the Order #49 of the Minister of Finance on "approval of instructions for rules of cash organization and operations for budgetary organizations."

The head of the LSG is responsible for cash organization. Cash operations are handled by the cashier, with the main function to perform cash inflow and outflow operations on the basis of payment and cash receipt orders. Cash operations are recorded in the cash registry, a book with numbered pages and signed by the head of budgetary the LSG and the chief accountant.

Typical form of payment and cash receipt orders is defined by the Order #449 of the Minister of Finance of Georgia on "On Approval of Forms for Source Documents and Accounting Registries for Budgetary Organizations."

The term payment is used to describe an event that can be expressed in monetary terms. Payments include ledger transactions and contra-entries where no monetary transaction occurs immediately. Payments must be made by means of a payment voucher and supported by documentary evidence. The payment voucher is any document that servers as evidence of authority to pay, it is used as an "action" sheet for processing payment. Payment vouchers must contain adequate and self-understood explanations of the payment being made and the authority on which they are paid, referencing payment order or minutes of conversations as well as the files that contain relevant correspondence.

A receipt is an official acknowledgement of money received. As a matter of principle, every acceptance of public money must be acknowledged by means of an appropriate and approved receipt. The term "receipt" includes all formal receipts, licenses, tickets, stickers and any other official documents used in connection with the collection of public money and issued upon the authority of the government.

The Chief accountant is responsible for the correct functioning of the cashbook. Cash control and monitoring is performed upon decision of the head of the LSG without advanced notice. In case of cash/cash documents deficit, the loss shall be refunded by those people who are guilty for the deficit. In case of surplus, the LSG's net value will increase, and be recognized as another economic flow. Decision on directing surplus to the state treasury (financing body) accounts is made by the head of the LSG.

1.4 Preparation and Storage of Accounting Documents

Order #1321 of the Minister of Finance of Georgia on "Approval of Accounting Instructions for Entities Financed from The Budget of Autonomous Republics and Local Self-Governments" states that the documents shall be stored at accounting sub-division under responsibility of designated people before transfer to archive.

Storage of documents at LSG archives is performed in compliance with order #72 of the Minister of Justice "On Approval of List of Typical Managerial Documents Created During the LSG 's Operation Process (Including Their Storage Durations)". As per the mentioned order, source documents shall be submitted for storage. In case of absence of source documents, notarized copies are stored.

Storage duration of each document is calculated from January 1^{st} of the next year after completion of the case processing (e.g. calculation of storage deadline of a case completed in 2009 shall start from January 1, 2010). If marked "till necessary" it means that the document has only practical importance (versus legally mandated importance) and its storage deadline is defined by the LSG itself, but not less than 1 year.

Documents storage deadlines, which is "permanent" as per the list, are subject to State archiving. After expiration of temporary storage deadlines, they are transferred to the national archive of Georgia in accordance with the Order #362 of the Minister of Justice of Georgia dated November 22, 2007 "On Approval of Temporary Storage Deadlines for National Archive Fund Documents at Organizations." Temporary storage deadline for documents of government organizations of Autonomous republics of Abkhazia and Adjara, and Legal Entities of Public Law (LEPL) under their umbrella, also for documents of LSGs, before transfer to the National Archive of Georgia or its branches – local archives, is 10 years.

After archive's expert-audit commission approves annotations of permanently storable cases, the LSG is entitled to destroy temporarily stored documents of the period compliant to the approved annotations, deadlines of which are expired. Destroy of documents is formalized with an act approved by the head of the LSG. Data storage media and computer reports must be appropriately destroyed after their useful lives and expiration of retention dates.

List of typical managerial documents created during the LSG operation (including storage deadlines) are given below:

Type of Document	Storage deadline/ duration	Note
IV. Recording and reporting 10. Accounting and reporting		
Albums unified typical forms of source / original documents	Till replaced with a new one	
Accounting balances and reports; related documents (annexes of balance, explanatory notes, specialized forms):		[1]in case of absence of annual – permanent [2] in case of absence of annual and quarterly – permanent
a) Cumulative annual	permanent	
b) Annual	permanent	
c) Quarterly	5 Y.[1]	
d) Monthly	1 Y.[2]	
Transferable, dividable and liquidation balances; their annexes, explanatory notes	25 Y.	
Analytical documents of annual balances and reports (tables, notes, presentations)	25 Y.	
Correspondence regarding double-check and approval of balances and reports	6 Y.	
Documents of discussion and approval of balances and reports (protocols, acts, decisions)	permanent.[1]	[1]quarterly – 10Y.
Cost list performance reports:		

Type of Document	Storage deadline/ duration	Note
a) cumulative annual	permanent	
b) annual	permanent	
c) quarterly	5 Y.[1]	[1] in case of absence of quarterly – permanent
Synthetic, analytical and material reports of accounting	6 Y.	
Plan of accounting reports	6 Y.	
Cash transfer reports based on state and non-state insurance (retirement salary, medical, social, employment)	25 Y.	
Correspondence regarding accounting and financial reporting submission dates	1 Y.	
Documents of financial-economic activity documentary revision, monitoring-revision works, inter alia cash, tax collection accuracy check and other documents (plans, reports, protocols, acts, notices, explanatory notes, correspondence)	6 Y.[1]	[1]On condition of inspection (revision) completion. In case of dispute, opinion discrepancy, investigation and court cases – till the final decision is made.
Main criteria of economical entities' operations (system of indicators) based on which their accounting (financial) reporting is subject to compulsory annual audit:		
a) in place of preparation and approval	permanent	
b) in other organizations	Till replaced with a new one	
Agreements with auditors (Audit Firms)	6 Y.[1] "Expert-audit commission" (EAC)	[1]From the date of expiration of the agreement
Accounting registers (main journal, journal-orders, tables worked out, etc.)	6 Y.[1]	[1]On condition of completion of inspection (revision). In case of dispute, opinion discrepancy, investigation and court cases – till the final decision is made.
Approved limits, salary funds:		
a) in place of preparation and approval	permanent	
b) in other organizations	Till necessary	
Source / original documents and their annexes reflecting economic operation performance and creating basis for accounting entry (cash, bank documents, bank cheque book covers, orders, tables, bank notifications and requirements to send, acts of property and materials delivery, acceptance, write offs; receipts, their covers, VAT documents, bills of lading, advance accounts, etc.)	6 Y.[1]	[1]On condition of inspection (revision) completion. In case of disputes, opinion discrepancies, investigations and court cases – till the final decision is made.
Entities' reconciliation and recalculation documents (acts, notices, correspondence)	6 Y.	
Correspondence regarding financial and economic activities (funds accounting, levy penalties, payments enforcement; receipt, delivery or write off of inventory, etc.)	6 Y.	
Personal accounts of employees	75 Y. (EAC)	
Resolution on bonuses of employees	6 Y.[1] (EAC)	[1]after replaced with a new one
Documents of receipt of salaries and other staff benefits (cumulative payment orders of salaries, benefits, royalty, material support and other payments cumulative reports (table grams);1 PoAs (incl. annulled) related to acceptance of cash or inventory.	6 Y.[2]	[1]In case of nascence of personal accounts – 75Y. [2]On condition of inspection (revision) completion. In case of disputes, opinion discrepancy,

Type of Document	Storage deadline/ duration	Note
		investigations and court cases – till the final decision is made
Correspondence regarding salary payments	6 Y.	
Data on annual collective incomes of employees and payments of taxes (income, tax and property declarations)	6 Y.[1]	[1]of public authorities 50 წ.
Warranty letters	6 Y.	
Notices on funds, salary limit accounting, distribution control, salary overspending and indebtedness recalculation; detention from salary, social security funds; on payment of vacation salary	6 Y.	
Correspondence regarding obtaining and paying back of credits.	6 Y.[1]	[1]after covering the credit
Charity payments, sick leave remuneration documents (copies of accounts, announcements, lists of employees, extracts from protocols, resolutions)	6 Y.	
Execution papers	Till necessary[1]	[1]not less than 10 years
Documents of accounts receivable and accounts payable, deficit, misappropriation of funds, peculation (notices, acts, obligations, correspondence)	6 Y. (EAC)	
List of authorized signatories of source / original documents.	Till replaced with a new one	
Study leave remuneration documents (announcements, resolutions, notices, correspondence)	Till necessary[1]	[1]not less than 10 years
The LSG 's main funds revaluation, fixed assets depreciation definition and property evaluation documents (protocols, acts, calculations, decisions)	50 Y. (EAC)	
Amortization transfer documentation (acts, bank statements, reports, calculations, correspondence)	6 Y.	
Trial balance	6 Y.[1]	[1]On condition of inspection(revision) completion in case of disputes, opinion discrepancy, investigations and court cases – till the final decision is made
Notifications (certificates) regarding tax registration	6 Y.[1]	[1]After registration is cancelled
Reports as per taxes: a) Annual b) Quarterly c) Monthly	Permanent 5 Y. [1] 1 Y.[2]	[1] In case of absence of annual - permanent [2] In case of absence of quarterly – 5Y.
Documents of accrued and paid taxes for all budget levels (calculations, notices, tables)	6 Y. (EAC)	
Correspondence regarding discrepancies on levying taxes, excise and other collection issues	6 Y. (EAC)	
Exemption from taxes, tax benefits, issued credits, taxes, excise and other payments installment or rejection documents (calculations, notices, announcements, decisions, lists, statements, correspondence)	6 Y. (EAC)	
Tax revenue payments and their indebtedness documents in different budget levels and non-budget funds (notice, notifications, correspondence)	6 Y.	

Type of Document	Storage deadline/ duration	Note
Correspondence regarding working capital formation, distribution, collection and calculation.	6 Y.	
Documents of costs incurred on purchase of equipment, operational and living funds (announcements, notices, limits, calculations)	6 Y.	
Documents of payment of taxes born out of tax set-off bonds, provision of products and goods, performance of works, provision of services. Acts of acceptance, notices)	6 Y.	
Acts - notices of covering taxes (indebtedness) by bill of exchange (BOE)	6 Y.[1]	[1]After paying the taxes
BOE remuneration, exchange, delivery-acceptance documents (applications, resolutions, notices, graphics, acts)	6 Y.	
Documents on currency issues (announcements, acts, notices, correspondence)	6 Y. (EAC)	
Currency and conversional, grant financed operations implementation documentation (reports, notices)	50 Y. (EAC)	
Operational reports for international accounts of foreign currency	50 Y. (EAC)	
Operational reports on foreign currency spending during business trips abroad	6 Y.	
List of payments, on which insurance disbursements to state social funds are not accrued.		
a) in place of preparation and approval	50 Y. (EAC)	
b) in other entities	Till replaced with a new one	
Personal accounts of the shareholders	6 Y.[1]	[1]After shift to ownership right shares. On condition of inspection(revision)completion
Contracts, agreements (credit, economical, operational)	6 Y.[1] (EAC)	[1]After expiration of the contract, agreement
Passports of deals	permanent	
Delivery-Acceptance acts of performed works (acts, notices, reports)	6 Y.[1]	1In case of absence of personal accounts – 75Y.
Agreements on material responsibility	6 Y.[1]	[1]After lay off of the materially responsible person
Samples of signatures of materially responsible people	Till necessary	
inventory insurance agreements	6 Y.[1]	[1]After agreement expiration
Documents of inventory of fixed assets, property, buildings and facility, inventory. (inventory commissions protocols, inventory annotations, acts, reports)	6 Y.[1]	[1] On condition of inspection (revision) completion. In case of disputes, opinion discrepancy, investigations and court cases – till the final decision is made
Accounting books, journals, cards of:		[1]After expiration of the last agreement, contract, arrangement. [2]After liquidation of the fixed asset, on condition of inspection (revision)completion [3]On condition of inspection (revision) completion. In case of
a) Bonds	50 Y. (EAC)	
b) Agreements, contracts, arrangements (credit, economical, operational)	6 Y.[1] (EAC)	
c) Fixed assets (buildings, facilities)	6 Y.[2]	
d) payments with other entities	6 Y.[3]	

Type of Document	Storage deadline/ duration	Note
e) cash documents of revenues/costs (accounts, payment orders)	6 Y.[3]	disputes, opinion discrepancy, investigations and court cases – till the final decision is made. [4]After covering tax indebtedness on condition of inspection (revision) completion [5]After the date of the last recording on condition of inspection (revision) completion
f) closed BOE for tax payments	6 Y.[4]	
g) realization of taxed and VAT exempted goods, works, services	6 Y.[5]	
h) inventory	6Y.[3]	
i) supplementary, controlling (transportation, weight, etc.)	6 Y.[3]	
j) accountable people	6 Y.	
k) execution papers	6 Y.	
l) employees revenues and total income tax	6 Y.	
m) deposited salary	6 Y.[3]	
n) as per deponents deposit amounts	6 Y.	
o) power of attorneys	6 Y.[3]	
Program for organization and implementation of accounting and reporting automated systems, manuals	Till replaced with a new one	
Correspondence regarding organization and implementation of accounting and reporting automated systems.	6 Y.	
Orders of accounting and reporting forms/blanks	1 Y.	
Financial documents of charity activities (reports, notices, correspondence, etc.)	6 Y. (EAC)	

EAC ("Expert Audit Commission") means that these kinds of documents may be of scientific-historical importance and they shall be transferred to archive institutions in compliance with the defined rules or be stored at the LSG. This note is applicable to all those entities that serve as a source of archive institutions, also might be used by LEPLs permanently storing their documents.

1.5 Electronic Documents

Increasing use of electronic systems resulted in necessity of creation of electronic documents. Various state entities (National Agency of Public Registry, Revenue Service, Purchasing Agency, etc.) perform operations through electronic systems.

Electronic documents are textual, sound, visual or audiovisual information and/or aggregated data stored in electronic format, while material documents are group of information or/and data represented on paper or any other material form.

Electronic document, to have legal power must be compliant with the requirements of law on electronic documents and electronic reliable services.

Backup is mandatory for computer data files, programs and system software. Each entity must identify data files to be retained for compliance with regulatory or statutory requirements. A fail-safe system to record and track backup data files and other off-line media for recovery and retention purposes must be maintained and tested.

Disaster recovery plans must include the following:

A). An analysis of the most effective alternative processing method for relevant and non- critical applications.

Alternatives include:

- an alternative computer site; or
- not processing applications until restored

B). A plan detailing IT and user personnel requirements and specialized skills

C). Off-site storage

To confirm that recovery can be accomplished, all disaster plans must be 100% tested at least annually. Where testing is found to be impractical due to operating conditions or costs, alternative methods must be developed and implemented

1.6 Synthetic and Analytical Accounting

There are two methods used in accounting: Synthetic and Analytical. They differ by the quality of generalization and breakdown.

Synthetic accounts are a group of accounts similar in scope, reflecting the object of accounting in a cash form. “Fixed assets”, “accounts payable”, “accounts receivable”, and “inventory”, are examples of synthetic accounts.

Analytical reports are the part of synthetic reports and serve to describe the object in detail. During analytical accounting, quantitative and value characteristics of assets are recorded, thus analytical accounting is given a big importance as it provides exhaustive information regarding financial-economical activities of the LSG.

We would like to draw your attention to Off-Balance Accounts – off balance sheet items that are used for defining the events not ranked among balance articles, but it is necessary to record them, as they represent important financial information for the LSG.

Off-balance accounts are fixed assets under operational rent, inventory received under storage responsibility, written-off debts of insolvent debtors, expensed inventory in operation, contingent requirements, contingent liabilities, depreciated fixed assets, overdue indebtedness, long-term low-cost expensed assets in operation, bank guarantees.

With the aim to control accuracy of synthetic and analytical accounting entries, trial balances for each group of analytical accounts are prepared monthly; turnovers and balances on analytical accounts of trial balance are compared to the balances of relevant accounts of the “main book.”

Materially responsible people are responsible for acceptance, storage and distribution of non-financial assets in compliance with the agreement conditions signed as per the legislation. The responsible people make inventory list of fixed assets, long-term low-cost assets and values.

When receiving non-financial asset, materially responsible person shall sign the delivery-acceptance act or the supplier’s document to approve acceptance of the non-financial asset.

With the aim to organize accounting and ensure control over maintenance, fixed assets, long-term low-cost assets and values are given the inventory numbers when received, maintaining it till their useful life within the organization. Based on each inventory number an inventory card is created as defined by the relevant order (normative act) of the Minister of Finance, indicating requisites (in case of existence) envisaged by the card. In addition to this, a short individual description of the object (goods) is included. In case the fixed assets, long-term low-cost assets and values contain precious metals, the list of those details containing precious metals shall be worked out specifying names of details and volumes of metals contained, as shown on passport. In case of rotation of assets within the organization, a relative record shall be made.

Accounting service is responsible for chronological and timely reflection of non financial assets acceptance and distribution in accounting and reporting.

2. ACCOUNTING METHODOLOGY

Relevance

In order to find out how the system works; it is necessary to understand its components. The accounting basics are described below. Along with the principles of double entry accounting, the top-level international accountability is also discussed. It is explained where the individual transactions recorded at LSG level are gathered, how they are compiled at the state level and what's their impact on the status of Georgia in the international community.

It is important that all the parties - accountants, budget specialists and leaders (appointed and elected officials) know, analyze and understand the final outcomes of their financial activities.

The discussed laws and regulations include the following:

- ✓ Order #1321 of the Minister of Finance of Georgia dated December 28, 2007 on "Approval of Accounting Instructions for Organizations Financed from The Budget of Autonomous Republics and Local Self-Governments."
- ✓ Order #70 of the President of Georgia dated February 6, 1998 on "Approval of Resolution on Accounting and Reporting in Georgia."
- ✓ Order #672 of the Minister of Finance of Georgia dated August 25, 2010 on "Approval of Budget Classification of Georgia."
- ✓ State Finance Statistics Manual 2001 (GFSM 2001)

2.1 Economic Events

In practical use of accounting, it is necessary to look into the essence of the economic phenomenon.

The action taken by the organization, that reflects the creation, exchange, transfer, or abolishment of the value, is the economic event.

The meaning of the above-mentioned definition will be discussed in detail:

Creation of value: Property acquisition free of charge by the municipality, production of assets with own resources, etc.

Exchange: Selling the property by market rules, as the sold property, for instance, a car, is exchanged in an asset again, which is translated into money or in other words, instead of one asset - car, we get another asset- money.

Transfer: Within the limits of our authority, we transfer the property under our ownership to the state unit, in such a case, no asset of equal equivalence is obtained.

Abolishment: As a result of inventory taking, a useless computer technology was identified, written off and destroyed according to the applicable law.

Economic events in turn divide into economic operations (transactions) and other events.

Economic operation (transaction) is an action taken on mutual agreement between entities, which is associated with the changes in amounts, composition and value of assets, liabilities and capital.

Other events are divided into operating and non-operating costs. They are reviewed as volumetric or value changes of assets or liabilities, which do not represent the operation outcome.

Volumetric changes of assets or liabilities are demonstrated in three groups, the first group includes the events, which envisage the addition or removal of existing assets/liabilities to/from the balance without any quantitative and qualitative changes. The second group involves events, that change the quantity or quality of assets, and the third group is comprised of changes made in asset classification.

Value changes are generated as a result of price changes of assets/liabilities without their transformation, such as revaluation of assets/liabilities, exchange rate impact, etc.

2.2 Double Entry

Economic events highly affect economic resources and the resources of their formation; they are double natured. Each economic event has two aspects: increase and decrease, formation and loss, purchase and transfer.

Accounting is performed by means of double entry. At this time, changes caused by economic events are registered with the same amount in the debit of one account and in the credit of another.

Linking the accounts by means of double entry is also called correspondence of accounts or accounting entry.

Based on the content, economic events can be simple, when the debit of one account is linked to the credit of other account, or complex, when the debit of one account is linked to several credits of the other account or vice versa.

Comprehensive knowledge of double entry or accounting entry and their use in practice is a precondition for accurate accounting and financial reporting.

In order to properly perform accounting entries, we need to know what is written on debit account and what is written on credit account.

Debit	Credit
Increase of assets	Decrease of assets
Reduction of liabilities	Increase of liabilities
Increase of costs	Reduction of costs
Reduction of revenue	Increase of revenue
Reduction of equity	Increase of equity

Example 2.2-1

We have bought a computer from a supplier, which costs 700 GEL, we should pay this amount to the supplier, within ten days after delivery of goods. In this case, there are two aspects: the organization's assets increase in the form of computers and at the same time, the organization's indebtedness is also increased.

Debit - Asset (Natural Account # 2122 other machinery and inventory): 700

Credit - Liability (Natural Account # 3220 liabilities accrued as a result of assets delivery): 700

2.3 Accrual and Cash Methods of Accounting

Transactions and other events are registered in accounting forms/registries with the receipt date of source documents and belong to that reporting month, they are registered through both accrual and cash-based accounting methods.

Application of the accrual method of accounting requires that economic events are recognized as soon as they occur and not at the time of receipt and payment of cash and cash equivalents. Correspondingly, accounting entries are made at the time when economic events occur and not at the time of funds receipt or payments. Accrual method enables to get information about both the future receivable assets as well as the payable liabilities. Revenues and expenditures are reflected when revenues are received, and actual disbursements are made.

Example 2.2-2

Based on Agreement terms, we transferred 15,000 GEL as an advance payment (as an advance) to the supplier for office maintenance works. In this case, our financial assets are increased as requirements and at the same time, our funds are decreased.

Debit - Financial assets (Natural Account # 1431 requirements for goods and service delivery based on advance payments):	*15,000*
Credit - Funds (Natural Account # 1100 thru 1200):	*15,000*

The supplier has performed maintenance works at 15,000 GEL, which became the basis of signing the act of acceptance. The office maintenance is the cost, while at the same time, demand for the supplier has been diminished since he/she did his job well and the client has no claim, which is confirmed by the act of acceptance.

Debit - Costs (Natural Account # 7230 office expenses):	*15,000*
Credit - Financial assets (Natural Account # 1431 requirements on goods and service delivery based on advance payments):	*15,000*

Application of the cash method of accounting requires that revenues and costs are recognized at the time of receipt and payment. During the cancellation or coverage of financial liability, the moment of cancellation or coverage is considered to be the moment of disbursements.

As mentioned above, the instructions envisage application of both accrual and cash-based methods of accounting.

For accounting the revenues, spending operations, assets and liability transactions of the organization, defined by the budget classification, only accrual method is used.

Transactions of non-financial assets are recorded at the moment of transfer of ownership rights. If it is impossible to accurately determine this moment, the transaction is captured at the moment of physical change of the owner or transferring the supervision rights.

Transactions according to various financial assets (securities, loans, currency and deposits), are reflected in the accounts after acquisition of ownership rights on assets.

Service operations are registered at the time of service delivery.

Funding received through allocations defined by the budget, is accounted by organizations through cash-based method.

When selling goods and services through non-market rules and the funds are received at the same time, it is permissible to use cash-based method of accounting.

Example 2.3-1

We have paid the supplier 50,000 GEL, the amount envisaged by the act of acceptance. Accounting entry will be as follows:

The funds are received from the budget

Debit - Natural Account # 1250 - Account for budget funds for organization's cash expenses:	*50,000*
Credit - Natural Account # 4100 - Funds received from the budget:	*50,000*

The amount is paid to the supplier

Debit - Natural Account # 3220 - Liabilities, accrued as a result of asset delivery:	*50,000*
Credit - Natural Account # 1250 - Account for budget funds for organization's cash expenses:	*50,000*

2.4 Budget Classification of Georgia (Economic Classification of Costs, Classification of Non-Financial Assets, Classification of Financial Assets)

One of the basic principles of the budgetary system of Georgia is unity which implies that the central, autonomous republic and local governments of Georgia will be guided by common ground, unified budget classification, unified accounting system and single principles of state financial control.

Budget classification includes economic classification of revenues and costs, functional classification of costs and non-financial asset operations, classification of non-financial assets and their operations, classification of financial assets and liabilities and operations related to them, as well as program classifications.

Budget classification is approved by the Order N672, 2010, of the Minister of Finance of Georgia. Compliance with this order is mandatory for all budget organizations.

<u>Revenue Classification</u>

Revenue classification is the revenue grouping according to their content. Revenues are divided into the following four main groups:

- ✓ Taxes
- ✓ Social contributions
- ✓ Grants
- ✓ Other revenues

Taxes are mandatory, unconditional cash contribution set by the Tax Code, which is paid by the taxpayer, based on necessary, unequal and gratuitous nature of the payment.

Types of taxes are the following: income tax, profit tax, value added tax, excise taxes, property tax.

Property tax and income tax paid by physical entities within individual activity goes to the LSG units: These are surplus amounts from entrepreneurial activities, sales of inventory, lease of property, and property donation.

Social contributions are not envisaged by Georgian legislation.

Grant is an optional transfer, received by a state unit from another state unit, from other government or international organizations.

Other revenues include incomes from property, from the sales of goods and services, and other mixed revenues not indicated in the above categories.

<u>Classification of costs</u>

Economic classification of costs is a clustering of financial transactions of budget expenditures based on economic content and is divided into eight main groups, namely, labor remuneration, goods and services, basic capital consumption, interest, subsidies, grants, social security and other expenses.

Labor remuneration implies the compensations in the form of money or commodity, issued by the employer to the employee for the value of work performed during the reporting period.

According to budget classification, Labor Remuneration does not include the remuneration of persons employed by service agreements. They are classified as Goods and Services in economic classification. Labor remuneration includes a basic salary, pay by position, by rank, bonus, supplement, royalty and compensation.

Goods and services include expenses incurred for the organization needs, such as:

- ✓ *Compensation paid for freelancers* - cash or commodity compensation for contracted freelancers.
- ✓ *Business trip* - expenses incurred during the departure of an employee outside the permanent workplace for the purpose of carrying out official tasks (travel expenses, accommodation, and expenses incurred for obtaining a visa, as well as the expenses prescribed for other specific positions by the Resolution No 211 of the Government of Georgia, dated April 25th, 2017).
- ✓ *Office expenses* include low-cost office equipment, stationary goods, one-year-of-use computer software, maintenance of buildings and adjacent territories, communication, utility and other office expenditures.
- ✓ *Representative expenses* imply both representative costs incurred for Georgian citizens and costs incurred for foreign guests within the same events.
- ✓ *Costs for meals* include expenses related to food.
- ✓ *Medical expenses* include medicines, medical disinfection, medical care materials and general healthcare costs.
- ✓ The cost category related to purchase of a *soft inventory, uniforms and personal hygiene*, include the costs for clothing, shoes, mattress, blankets, sports uniforms, carpets, curtains and other similar costs.
- ✓ *Operating and maintenance costs of vehicles and equipment* include expenses related to operation and maintenance of vehicle, equipment and instruments/tools, such as purchase of fuel/lubricant materials, operating, maintenance and spare parts, car renting (transportation), purchase/storage of low price tools and devices, etc. non-classified expenses related to operation and maintenance of vehicle, equipment and tools/instruments.

- ✓ The costs of purchase of *military equipment and bullets* involve the expenses paid by military agencies for armament, armored vehicles, bullets, low-price accessories and other similar costs, capital repair costs of technical means.
- ✓ Any other goods and services integrate expenses not indicated in above categories, such as: *expertise and inspection costs, advertising costs, auditing service costs, archiving costs, expenses related to cultural, sport, educational and exhibition events, etc.*

Basic Capital Consumption implies reduction of the value of fixed assets existing in the ownership of and used by the state unit, as a result of physical depreciation, moral depreciation and casual accidental damage during the reporting period. This article only applies to accrual method of accounting.

Interest is a payable amount, deriving from certain types of financial requirements, namely, deposits, securities (except shares) loans and accounts payables.

Subsidies represent transfers to enterprises and organizations free of charge and irreversible for current purposes by state units. The amounts transferred to legal entities/non-entrepreneurial (noncommercial) legal entities and other state nonfinancial enterprises for funding current and operating costs, are registered under this article.

Grants constitute current or capital transfers from one state unit to the other state unit, international organization or government of another country. The content of the grant for classification purposes does not coincide with the definition given in the Law of Georgia "regarding the grants" and the term "grant" used in the classification of expenditure is used only for the purposes of this classification.

Social security is a transfer of cash or commodity, which is carried out in order to protect the entire population or some part of it against social risks. Social security integrates:

- Social aid including state pensions, state compensations and state academic scholarships, pensions of disabled persons, assistance for unemployment, refugees and IDPs;
- Compensation for victims of violence and affected people, social assistance for households in vulnerable conditions, assistance to the population below the poverty line;
- Assistance provided by the monetization program, assistance for pregnancy, childbearing and childcare, as well as adoption of newborns, health care costs, etc.

The **social assistance provided by the employer** includes the following:

- Compensation for dismissal
- Full or partial salary paid for sickness or accidental damage inflicted not on work, and in case of death or mutilation of the employee when performing official duties
- Social assistance provided by the state for pregnancy, childbirth and childcare, as well as for adoption of newborns. Also, the social transfers that are included in the Social Assistance category that may be paid by the employer.

Miscellaneous costs include several types of transfers executed for various purposes and also the spending operations, which are not classified elsewhere, and is divided into the following:

- Various current expenses which include enforcement expenses imposed by the courts and other quasi-judicial authorities, insurance costs for premises, transportation means, costs for compensating damages caused by natural calamities, fees and taxes (excluding income tax and VAT within the cost of goods), fines and other unclassified expenses.

- Miscellaneous capital costs include monetary/commodity capital transfers issued for households, monetary/commodity capital transfers issued for households or their market-based enterprises, cash/commodity capital transfer issued for Non-Profit Organizations, payments made by the state unit for the purpose of capital formation by enterprises, compensation for damage to non-financial assets of enterprises and organizations and various unclassified capital expenditures.

Classification of nonfinancial assets

Classification of non-financial assets and operations are divided into 4 main groups, namely: basic assets; material supplies; values; non-manufactured assets

Basic assets are manufactured assets that have been used over multiple years or are continuously used in the production or service process, and the cost of which is 500 GEL and more. Items which have a long-life cycle but are not intended for multiple use cannot be classified as the basic assets (e.g. coal used for burning).

Significant improvement of existing assets, which increases their production capacity, prolongs life cycle or both, is a capital repair and is registered as a purchase of basic assets. Capital repair implies the renewal, reconstruction and expansion of an asset that is an analyzed investment decision and increases the operational characteristics, capacity of the asset, or prolongs the period of pre-specified useful life of the asset. Moreover, storage and maintenance costs of basic assets, which do not affect their production capacity and life cycle, are registered as "Goods and Services"

Fixed assets include buildings and structures; machinery and inventory; other basic assets.

Buildings and facilities include residential buildings, non-dwelling buildings, roadways, streets, roads, bridges, tunnels, sewage and water supply systems, electric transmission lines, pipelines.

Machinery and inventory combine means of transportation and other machinery and inventory.

Other major assets include cultivated assets, non-material assets, other non-material assets.

Material supplies include goods that are stored for further sale, used in the production process or future utilization, these are strategic supplies and other material supplies (raw materials and materials. unfinished production, finished products, goods purchased for further sales). Hereby it should be noted that the material supplies mentioned by the budget classification is recorded in economic articles of expenses, and for accounting purposes, they are registered as non-financial assets. Monetary instruments, spare parts and other material supplies are in the chart of accounts.

Valuables are tangible, manufactured goods that have a significant value. They are acquired and stored primarily as a means of accumulation and are not used for production or consumption. It is expected that their real value will increase over time, at the worst, will not decrease, and the quality will not deteriorate when stored in appropriate conditions. Values include precious stones, metals, paintings, sculptures and other works of art.

Non-manufactured assets include assets, generated naturally or created through legal or accounting operations, protection of ownership rights of which can be ensured. These include land, minerals and other natural assets (radio frequency spectrum license, uncultivated biological resources, water resources, etc.)

Classification of financial assets and liabilities

Classification of financial assets and liabilities is a clustering of purchase and expenditure operations of financial assets, receipt and coverage of liabilities, as well as grouping of financial assets and liabilities according to their types.

The following table gives a clear picture of financial assets and liabilities:

Financial assets	Liabilities
Internal	Internal
Currency and Deposits	Currency and Deposits
Securities, except shares	Securities, except shares
Loans	Loans
Shares and other capital	Shares and other capital (only state enterprises and organizations)
Insurance technical reserves	Insurance technical reserves
Derivative financial instruments	Derivative financial instruments
Other accounts receivable	Other accounts payable
External	External
Currency and Deposits	Currency and Deposits
Securities, except shares	Securities, except shares
Loans	Loans
Shares and other capital	Shares and other capital (only state enterprises and organizations)
Insurance technical reserves	Insurance technical reserves
Derivative financial instruments	Derivative financial instruments
Other accounts receivable	Other accounts payable
Monetary gold and special drawing rights	

As we see, financial assets and liabilities have similar names (excluding the Gold and the Special Drawing Rights). This can be explained by the fact that one and the same thing can be an asset for one party and the liability for the other party, for example, when the organization issues a loan, it registers the loan into financial assets as a loan, and when it borrows, then registers the loan in liabilities, as a loan.

Currency and Deposits. Currency consists of banknotes and coins in circulation, which are widely used during payments. The majority of state units are accounted for as assets of various deposits, including foreign currency deposits. It is also possible that the state unit takes the liability as a deposit. For example, a court or a tax authority may arrest a deposit as a collateral before the dispute settlement.

Securities, except of shares, include circulating financial instruments certifying liabilities/requirements of institutional entities; such as: bills, bonds, circulating deposit certificates and other securities.

Loans. This is a financial instrument when the creditor directly gives money to the debtor.

Stocks and other capital. This is an enterprise shareholding by the state organization.

Technical insurance reserves consist of net value of the means invested by households in pension funds and life insurance reserves, of means which are derived from pre-paid bonuses as well as from the claims of outstanding insurance payments.

Other accounts receivables/payables are made up of trade credits as well as all other types of accounts payable (including debts arising from previous years) that are not classified in other articles.

Derivative financial instruments are the financial instruments that are developed on the basis of other financial tools. There are two basic classes of derivative financial instruments: forward-type contracts, including swapping, and optional contracts. Within the forward-type contract, the two contracting parties agree to exchange the determined number of basic objects which may be both real and financial, with agreed price at the time specified. Swap is a sale agreement with further redemption. The option is the contract that gives the buyer the option (but does not impose any obligation) to buy ("call" option) or sell ("put" option) a specific financial instrument or goods at a predefined price in the given time period or within a specified deadline.

Monetary gold and Special Drawing Rights - monetary gold includes gold coins, molded and cut gold bars of at least 995/1000 tests, which are owned by monetary/credit regulatory units and are included in state official reserve assets. **Special Drawing Rights** are the international reserve assets, created by the International Monetary Fund, which are distributed to its member countries, to fill the existing reserve assets.

2.5 Economic Operations

Economic Operation is an action taken on mutual agreement between entities, which is related to the changes in volume, composition or value of assets, liabilities and equity, and it is noteworthy that mutual agreement does not involve necessity of voluntary participation of the both entities in the operation. Obligatory actions, that are necessary for (judicial or administrative) decision execution, regardless of whether they are voluntary or not, are considered as operation. In turn, the economic operations are divided into exchange and non-exchange transactions.

An economic operation is an exchange when a unit receives an asset/service or covers its liability and transfers the approximate value of the goods/services in the form of usage rights of goods/services to the other side in exchange for this asset/service.

In non-exchange operation, the unit either does not receive the equivalent approximate value from the other entity or transfers the exchange value to the other party without receiving the value.

Operations are also divided into monetary and non-monetary operations.

During monetary operations, there are expected cash inflows or outflows in the organization, and on the contrary, during non-monetary operation, instead of cash, there take place inflows or outflows of goods/services.

Types of non-monetary operations are barter, commodity payments etc.

The operation is barter, if two units change the goods/services or assets of equal value, except for cash.

Commodity payments are the payments in a form of goods/service or assets (except cash) delivery for liability coverage.

Although most operations are carried out between two entities, there are cases where the same unit operates in two different aspects and in analytical terms the action is considered as an internal operation. For example, transfer of goods and raw materials from inventory to production; internal consumption of material supplies.

2.6 "Government Finance Statistic Manual" (GFSM) 2001 Worked Out by International Monetary Fund

Background

The International Monetary Fund uses data dissemination standards to guide IMF member countries when disseminating their economic and financial data to the public. These standards are created by the International Monetary and Financial Committee (IMFC) and are split into two tiers: The General Data Dissemination System (GDDS) and the Special Data Dissemination Standard (SDDS). The primary objective of the GDDS is to encourage member countries to build a framework to improve data quality and statistical capacity building to evaluate statistical needs, set priorities in improving the timeliness, transparency, reliability and accessibility of financial and economic data. The SDDS is a global benchmark for data dissemination and provides information about economic and financial data (macroeconomic statistics) to the public. Compliance with the SDDS indicates that a country meets the test of "good statistical citizenship." Countries that adhere to the SDDS agree to follow good practices in four areas: the coverage, periodicity, and timeliness of data; public access to those data; data integrity; and data quality.

Georgia as a member country is committed to observe the SDDS standards and to provide information about data and data dissemination practices – metadata - to the Dissemination Standards Bulletin Board (DSBB).

Specific

Starting from FY2008 Georgian government finance statistics are compiled according to the IMF GFSM 2001 methodology. For analytical purposes, an accomplishment survey is prepared quarterly and monthly in the Ministry of Finance of Georgia and presented to the Parliament of Georgia. The mentioned information is publicly available. Consolidated data are compiled for government authorities as a whole, including data on operations of local authorities. Expenditures and revenues are recorded on cash basis. For central government budgetary revenue, grants and domestic financing data are available from the NBG Treasury Account records. Monthly expenditure data are available at the Treasury system. After compilation, all GFS data are compared with the previous period to identify unusual trends, for which explanations are then obtained and documented internally.

Georgian budget revenue and expenditure classification system consists of:

- Classification of Budgets Revenue by origins of it
- Economic Classification of Budget Expenditure by types of expenditure,
- Functional Classification of Budget Expenditure by similarities of expenditure targets;
- Organizational Classification of Budget Expenditure by spending agencies;

General government finance statistics are compiled according to the IMF GFSM 2001:

- Cash receipts from operating activities
- Cash payments for operating activities

- Net cash inflow from operating activities
- Net cash outflow from investments in nonfinancial assets
- Cash surplus (+)/deficit (-)
- Net acquisition of financial assets, excluding cash
- Net incurrence of liabilities
- Net cash inflow, financing activities
- Net change in the stock of cash
- Statistical discrepancy
- Memorandum items

GFSM 2001 methodology

The IMF Statistics Department's Government Finance Statistics Manual 2001 (GFSM 2001) updated the 1986 edition of A Manual on Government Finance Statistics (GFSM 1986). There is a newer version - GFSM 2014, which supports the balance sheet approach for analyzing economic policy by bringing together stocks and flows in a transparent and consistent framework.

The GFSM 2001 is intended to be a reference volume describing the GFS system. It covers concepts, definitions, classifications, and accounting rules. The GFS system is a specialized macroeconomic statistical system designed to support fiscal analysis. Fiscal analysis is any analysis that has to do with budgets, finances, and cash related issues over time. Fiscal analysis studies are usually concerned with how money was delegated and whether certain groups or entities received disproportionate payouts. Fiscal analysis helps to shape fiscal policy. Fiscal policy is the government's stance on using spending, revenue collection, and financial incentives to influence the economy. The GFS system is applicable to all types of economies regardless of the institutional or legal structure of a country's government, the sophistication of its statistical development, the system of government financial accounting, or the extent of public ownership of for-profit entities. The GFS system pertains to the general government and public sectors.

Two types of flows are recorded in the GFS system: transactions and other economic flows. Flows reflect the creation, transformation, exchange, transfer, or extinction of economic value. In most cases transactions are interactions between two institutional units that take place by mutual agreement.

The core of the analytic framework is a set of four financial statements. These are (1) the Statement of Government Operations; (2) the Statement of Other Economic Flows; and (3) the Balance Sheet. In addition, the framework includes a Statement of Sources and Uses of Cash to provide key information on liquidity.

#1 The "**Statement of Government Operations**" records the results of all transactions during an accounting period. They are classified as revenue, expense, net acquisitions of nonfinancial assets and effect the creation, transformation, exchange, transfer, or extinction of economic value.

#2 The "**Statement of Other Economic Flows**" summarizes price changes and a variety of other economic events that affect the holdings, such as debt write-offs and catastrophic losses in assets, liabilities, and net worth. It presents influences on the government's net worth that are not the result of government transactions.

#3 The "**Balance Sheet**" is the statement for the general government or public sector regarding the stocks of financial and nonfinancial assets owned, the stock of claims of other units against the owners of those assets in the form of liabilities, and the sector's net worth, equal to the total value of all assets less the total value of all liabilities. In many cases, it may be difficult to attach market values to some government nonfinancial assets, and therefore many analyses are focused only on the financial assets of the general government sector rather than its total assets.

#4 The "**Statement of Sources and Uses of Cash**" records cash inflows and outflows using a classification similar to that of the Statement of Government Operations. However, it shows the total amount of cash generated or absorbed by (1) current operations, (2) transactions in nonfinancial assets, and (3) transactions involving financial assets and liabilities other than cash itself. The net change in the government's cash position is the sum of the net cash received from these three sources.

Analytical measures for fiscal policy

Macroeconomics is a branch of the economics field that studies how the aggregate economy behaves. In macroeconomics, a variety of economy-wide phenomena is thoroughly examined such as, inflation, price levels, rate of growth, national income, gross domestic product and changes in unemployment.

For macroeconomic analysis, fiscal policy measures include the three core balances in the GFS system, other balances used by various institutions (including the IMF), and other important macroeconomic measures of flows and stocks. These variables could apply to the different levels of government, the general government sector or to the public sector.

Core GFS balances

Net/gross operating balance: The net operating balance equals revenue minus expense. The gross operating balance equals revenue minus expense other than consumption of fixed capital.

Net lending /borrowing: Net operating balance minus the net acquisition of nonfinancial assets (or the gross operating balance minus the net acquisition of nonfinancial assets that also excludes consumption of fixed capital). Net lending/borrowing is also equal to the net acquisition of financial assets minus the net incurrence of liabilities

Cash surplus/deficit: Net cash inflow from operating activities minus the net cash outflow from investments in nonfinancial assets

Total expenditure composition

Total expenditure composition: Disaggregation of total expenditure through applying functional classification **-** Classification of Functions of Government (COFOG)

Classification of Functions of Government (COFOG)

The Classification of the Functions of Government (COFOG) was developed by the Organization for Economic Co-operation and Development and published by the United Nations Statistical Division.

COFOG provides a classification pertaining to outlays by governments on functions allowing wide variety of analytic applications. Statistics on health, education, social protection, and environmental protection, for example, can be used to study the effectiveness of government programs in those areas. The classification codes of COFOG are somewhat different from the structure of other GFS classification codes.

The functions are classified using a three-level scheme. There are 10 first-level, or two- digit, categories, referred to as “Divisions”. Within each division, there are several “Groups”, or three-digit categories. Within each group, there are one or more “Classes”, or four-digit categories. All outlays for a particular function are collected in one category of COFOG regardless of how the outlays are implemented. COFOG permits trends in government outlays on particular functions or purposes to be examined over time. In summary Divisions could be seen as the broad objectives of government, while the Groups and Classes detail the means by which these broad objectives are achieved.

Comprehensive information is available in English by down loading: https://www.imf.org/external/pubs/ft/gfs/manual/

3. Accounting

Relevance

The technical part of the guidebook starts with this chapter. The chapter provides specific and detailed rules of accounting. It will be more useful for accountants, however some parts might as well be interesting for others, to develop an understanding of accounting requirements. In addition to accountants, the knowledge of aforementioned information will help other specialty staff to work better within the system.

The reviewed laws and regulations include the following:

- ✓ Order #1321 of the Minister of Finance of Georgia dated December 28, 2007 on "Approval of Accounting Instruction for Organizations Funded from the Budget of Autonomous Republics and Local Self-Government Bodies".
- ✓ Order #70 of the President of Georgia dated February 6, 1998 on "Approval of Resolution on Accounting and Reporting in Georgia."
- ✓ Order #672 of the Minister of Finance of Georgia dated August 25, 2010 on "Approval of Budget Classification of Georgia."
- ✓ State Finance Statistics Manual 2001 (GFSM 2001)
- ✓ Order #439 of the Minister of Finance of Georgia dated December 31, 2002 on approval of "Instructions on Physical Depreciation Norms for Fixed Assets of Budgetary Organizations and Their Accounting"

3.1 Valuation

We are all aware, that the accounting is the field of bookkeeping, where economic transactions are translated into monetary value. Accordingly, the monetary valuation of economic events is a top issue on the agenda.

In general, as a result of economic events, the assets are valued at their original or purchase value, which is adjusted considering all the changes that have taken place after their purchase, free transfer (donation) or production/rendering of services. These changes are the following: substantial improvement, depreciation/basic capital consumption, profit or loss from ownership, depletion, destruction, quality deterioration, unforeseen aging, losses caused by accidental damage and other losses.

The value of receipt or disbursement of financial assets is their exchange value. Accounts receivable generated upon goods or service delivery, is the value of delivered goods or services.

The value of inventory includes the costs related to their purchase, production and processing.

Inventory purchase costs contain purchase costs plus all payments including nonrefundable taxes, transportation, production and all other costs, directly related to the purchase of inventory.

Cost price of material supplies can be determined using one of the following methods:

By means of:

- Assessment method based on individual expenditures
- (FIFO) method – First in, first out.
- Method of weighted average value.

Selection and use of these methods is dependent on accounting policy of the organization.

Example 3.1-1

On July 1, 50 pieces of office paper were purchased. Unit price is 6 GEL

On August 1, 100 pieces of office paper were purchased. Unit price is 6,5 GEL

On August 15, 120 pieces of office paper is spent.

Balance: 30 pieces

The value of the 120 pieces of office paper will be 755 GEL

From the purchase on July 1, 50X6=300 GEL

From the purchase of July 2, 70X6,5=455 GEL

While applying the method of weighted average value, assets are valued according to weighted average value.

Let's first calculate the cost price of unit (weighted average): 755 GEL/130 units =5.81 GEL/unit

The value of the inventory is 30 X 5.81= 174.3 GEL.

In applying assessment method per individual expenditure, the cost price of inventory is determined individually for a given time period.

With the FIFO method, the value of inventory is determined by the sequence of their acquisition and expenditure.

The acquisition of fixed assets is assigned a monetary value, which includes acquisition, production, construction, installation and set up costs, other direct costs necessary for asset's activation, as well as nonrefundable taxes, fees, other taxes and all the expenses related to transfer of property rights.

Fixed assets are recorded in the balance sheet at Gross Value excluding depreciation.

Expenditures incurred for fixed assets' storage, maintenance and repair to keep them in working condition, which does not effect on their capacity, quality, service potential and life cycle, are recognized as expenses

Expenses that result in the substantial improvement of assets are recorded as increases in the value of fixed assets. These are added to the book value of assets.

The costs incurred on substantial improvement may include the following:

- Modification of components of buildings and structures with the purpose of extending their useful life, as well as their capacity;
- Upgrading the parts of vehicle/machinery for improvement of product/service quality;
- Introduction of new production processes for the purpose of significant reduction of operational costs.

The assets received free of charge should be evaluated by a qualified specialist.

The value of the exchange or repayment of financial liabilities is their exchange value.

The value of accounts receivable generated from the purchase of goods or services is the value of received goods or services.

The value of operations translated in foreign currency shall be converted to the national currency at the official rate at the date when these operations were conducted, and the asset/liability value is converted according to the official exchange rate set for the reporting date.

Example 3.1-2

An automobile is purchased at a price of 10,000 USD on December 15, the exchange rate 1$=2, 4 GEL. Payment shall be made in January of the next year.

Debit) Natural Account 2121 - Transportation means:	*24,000*
Credit) Natural Account 3220 - Liabilities accrued through assets delivery:	*24,000*

GEL exchange rate was changed by December 31, the end of reporting period 1$=2, 5 GEL

Since the dollar rate has increased by 0.1 units, the liability will be increased accordingly. If on December 15, 10,000 USD were worth 24,000 GEL, on December 31, 10,000 dollars became 25,000 GEL, which means that our liability increased by 1,000 GEL.

Debit) Natural Account 8200 - Non-operational costs:	*1,000*
Credit) Natural Account 3220 - Liabilities accrued through asset delivery:	*1,000*

3.2 Contingent/Conditional Instruments

It is important to describe an event that may influence on organization's assets, liabilities, revenues, and expenditures in the future, such events are called conditional/contingent instruments.

Conditional/contingent instruments are of two types: conditional/contingent requirements and conditional/contingent liabilities.

Conditional/contingent instruments depend on the future events, on the factors that cannot be fully predicted, such as a lawsuit of a citizen, and therefore the dispute in court for the claim of damages. In this case, the court may take the citizen's demand into consideration and impose refunding obligation on the organization that will result in liability creation, or a guarantor letter issued by the LSG on treatment costs compensation. These kind of cases constitute a conditional obligation.

No contingent instrument is an unconditional requirement or liability and shall not be considered as a financial asset or liability.

Contingent requirements and contingent liabilities are recorded in off balance sheet items, so that the organization is able to precisely determine the risks in the future and objectively evaluate the situation.

3.3 Accounting of Financial Assets and Requirements

Financial assets include funds, financial requirements, demands for goods and services.

Financial assets are funds, contractual right to request financial assets; or other financial instruments, contractual right on profitable exchange of financial instrument with other subject or equity instrument.

Contractual rights that do not foresee receipt of financial assets, do not constitute a financial instrument.

The demand is an asset if it is used as the means of value accumulation ensuring economic gain for its owner.

Financial assets and requirements are arranged according to maturity: short-term and long-term.

Financial assets are short-term assets if they are expected to be used (spent)/covered within one year after the reporting date.

Financial assets are long-term assets if they are expected to be used (spent)/covered in the period after one year since the reporting date.

The chart of accounts defines the groups of financial assets according to content and maturity:

Name of account	Account №
Financial assets and requirements	1100-1500
Short-term financial assets	1100-1300
Funds	1100-1200
Cash on hand in national currency	1110
Cash on hand in foreign currency	1120
Current account in bank	1210
Current account in bank in national currency	1211
Current account in bank in foreign currency	1212
Other accounts in bank	1220
Current account for non-budget funds in the treasury	1230
Account for target grants and funds	1240
Account of budget funds for organization’s cash expenses	1250
Deposits in treasury in national currency	1260
Deposits in treasury in foreign currency	1270
Treasury currency account	1280
Other accounts in treasury	1290
Other short-term financial assets	1300
Securities excluding shares	1310
Short-term loans	1320
Short-term budget funds	1321
Short-term loans with non-budget funds	1322
Shares and other equity	1330
Derivative financial instruments	1340
Other short-term accounts receivable	1350
Interests charged on budget loans	1351
Interests charged on non-budget loans	1352
Interests charged on deposits and other financial assets	1353
Requirements charged by fines, sanctions and other property-related revenues	1354
Requirements on funds and their equivalents by assets/service delivery	1355

Name of account	Account №
Paid VAT	1356
Pre-paid profit tax	1357
Other tax asset	1358
Requests by deficit of funds and their equivalents	1359
Other short-term financial assets	1360
Other short-term requirements	1400
Requirements by barter	1410
Requirements against insurance companies	1420
Requirements by advance payments	1430
Requirements by advance payments for goods and service delivery	1431
Requirements by advance payment for assets delivery	1432
Requirements by deficit of non-financial assets	1440
Requirements against accountable entities	1450
Requirements against accountable entities by advance payments	1451
Requirements against accountable entities by other funds	1452
Requirements against employees	1460
Requirements by business trips within the country	1461
Requirements by business trips abroad	1462
Other short-term requirements against employees	1463
Requirements by pre-paid taxes	1470
Other short-term requirements	
Long-term financial assets and requirements	1500
Long-term loans	1510
Long-term budget loans	1511
Long-term loans with non-budget funds	1512
Shares and other equity	1520
Other long-term financial assets	1530
Other long-term requirements	1540

The increase of financial assets is recorded in the debit of corresponding account and the decrease – in the credit.

Funds received for financing the taxes determined by the budget, are recorded in account 1250.

Example 3.3-1

5,000 GEL is paid to the supplier for service delivery.

Since the funds received from budget are accounted using the cash-based method, the accounting entry will be as follows:

Debit) Natural Account 1250 - Budget funds for organization's cash expenses:	*5,000*
Credit) Natural Account 4100 - Funds received from budget:	*5,000*
Debit) Natural Account 3210 - Liabilities charged through goods and service delivery:	*5,000*
Credit) Natural Account 1250 - Budget funds for organization's cash expenses:	*5,000*

Loan issuance by budgetary organization is captured in the debit of accounts of budget loans/loans by non-budget funds (1321/1322/1511/1512) with the correspondence to the credit of fund related accounts (1100-1200)

Example 3.3-2

The municipality has issued a loan with the amount of 6,000 GEL to homeowners' partnership for upgrading the elevators with the term of 3 years.

Debit) Natural Account 1250 - Budget funds for organization's cash expenses:	*6,000*
Credit) Natural Account 4100 - Funds received from budget:	*6,000*
Debit) Natural Account 1511 - Long-term budget loans:	*6,000*
Credit) Natural Account 1250 - Budget funds for organization's cash expenses:	*6,000*

At the year of loan issuance, the loan payment is recorded in the debit of the account corresponding to funds and in the credit of the loan account.

From the above-mentioned example, homeowners' partnership has repaid 1,000 GEL.

Debit) Natural Account 1250 - Budget funds for organization's cash expenses:	*1,000*
Credit) Natural Account 1511 - Long-term budgetary loans:	*1,000*
Debit) Natural Account 4100 - Funding received from budget :	*6,000*
Credit) Natural Account 1250 - budget funds for organization's cash expenses:	*6,000*

In case of loan repayment within next budgetary year, the returned loan amount is reflected on the account of the organization, in the debit of funds account (Natural Account 1100-1200) and in the credit of loan accounts (Natural Account 1320/1511). In addition, the operation of creating liabilities by loan amounts to the budget is recorded in the debit of net present value account (Natural Account 5100), with correspondence to the credit of accrued liability (Natural Account 3245) against the budget, and the decrease of liabilities is captured in the credit of accounts relevant to funds (Natural Account 1100-1200) or financial assets (Natural Account 1320/1511) and in the debit of liability account against the budget.

Advance payments to the suppliers are recorded in the accounts of receivable by advance payments.

In case of sending the employee on business trip, when business trip costs are reimbursed in advance, the liability by business trip is created.

Example 3.3-3

According to contractual terms, 10,000 GEL is transferred to the supplier for office construction as an advance payment based on bank guarantee.

Debit) Natural Account 1250 – Account of budget funds for organization's cash expenses:	*10,000*
Credit) Natural Account 4100 – Funds received from the Budget:	*10,000*
Debit) Natural Account 1432 - Receivable for receipt of assets through advance payments:	*10,000*
Credit) Natural Account 1250 – Account of budget funds for organization's cash expenses:	*10,000*

Example 3.3-4

The employee travels abroad for business purpose, before the trip, we have transferred the amount for business trip– 4,500GEL to their account

Debit) Natural Account 1250 - Budget funds for organization's cash expenses:	*4,500*
Credit) Natural Account 4100 – Funds received from the Budget:	*4,500*
Debit) Natural Account 1462 -Advance for business trips abroad:	*4,500*
Credit) Natural Account 1250 - Budget funds for organization's cash expenses:	*4,500*

3.4 Accounting of Inventory

Inventory is non-financial assets envisaged for production, for future transfer or service delivery.

The exit of material supplies is captured when goods are sold or used for production or movement to another category.

Inventory 1600	Account
Strategic inventory	1610
Another inventory	1620
Raw materials and materials	1621
Unfinished production/service	1622
Finished product	1623
Goods purchased for future sales	1624
Cash items	1625
Spare parts	1626
Other material supplies	1627

Strategic inventory comprises the following: goods, stored for strategic purposes and emergency situations; goods stored by market regulatory bodies; and goods, having special significance for the country (for example, wheat and oil)

Raw material and materials consist of all-natural resource and materials, stored as resource to be used in production process.

Unfinished products include products that are partially processed or produced by the producer and their production will be finished soon by the same producer, but generally, they are not subject to sales, delivery or transfer to the other party without further processing.

Ready-made (finished product) include the goods, which are the outcome of the production process, still stored by the producer and before delivery to other units, are not subject to further processing. State units can have the finished products only if they produce goods for sale or transfer to other units.

Goods for future sales include goods purchased for future sales or for transfer to other units, the physical forms of which do not change sharply, as the product already has a finished shape during procurement process. The mentioned category also consists of goods purchased for the purpose of future transfer from state unit to other unit free of charge or at economically insignificant price.

"Cash items"/ Negotiable Instruments consist of cash documents at organization's disposal. Including, strict accounting blanks (ID blanks, VAT documents, etc.), fuel coupons, oil, food; postal stamps, excise marks, etc.

Spare parts include (regardless of their value) items designated for repair or replacement of worn out parts of vehicles (medical, electrical computing, etc.), equipment, and transport means (engines, tires, etc.). High-cost (expensive) auxiliary parts (with the value of 500 and more), that are intended to be used by the organization for more than one year and which can be consumed only together with any specific object of fixed assets and is used on non-regular basis, is recognized and recorded as a fixed asset. The basis for its recognition as an asset is the receipt of future economic benefits or service potential from other assets, which might not be possible without these assets.

Other inventory includes economic materials, stationary items, fuel for business needs, fuel and oil for machinery and equipment, food products and other inventory that are not registered in accounts corresponding to another inventory.

Receipt of inventory is reflected in value, which includes all expenses related to their purchase, production and processing.

Inventory can be received through purchase, free of charge or own production.

Example 3.4-1

Spare parts of automobile, specifically 15 pieces of tires, are received from the state free of charge. Unit price is 200 GEL.

Debit) Natural Account 1626 – Spare parts (15X200):	*3,000*
Credit) Natural Account 6321 - Current grants in commodity form:	*3,000*

When writing off the assets, useful service or value materials should be registered on balance.

Example 3.4-2

We have written off the machinery, which was not functional any more. As a result of dismantling the machinery, we got one ton of scrap iron and other spare parts. The scrap iron is envisaged for sale, and spare parts will remain in the organization and will be used in operation for other machinery. The scrap iron and spare parts were evaluated by the specialist of relevant qualification at 430 GEL one-ton scrap iron and spare parts – at 300 GEL.

Debit) 1 Natural Account 624 - Goods purchased for future sale (scrap):	*430*
Debit) Natural Account 1626 - Spare parts:	*300*
Credit) Natural Account 6450 - Other non-classified revenues:	*730*

The sale of inventory (except for strategic inventory) are recorded in debit of accounts equivalent to cash (1100-1200), requirements for barter (Natural Account 1410), requirements for cash and cash equivalents through asset delivery (Natural Account 1355) or other revenues received in advance (Natural Account 3282) and in relevant credit accounts of revenues, and is recorded in debit of goods and service account (Natural Account 7200) and in credit of other relevant inventory accounts (1620) with the cost price of sold materials.

Example 3.4-3

We sold one ton of scrap metal at a price of 500 GEL. Self-cost of scrap metal was GEL 430. The purchaser fully transferred the cost of scrap metal - 500 GEL on the corresponding treasury code of the budget revenues. Afterwards we transfer goods to the Purchaser

Debit) Natural Account 3282 - Other revenues received in advance:	*500*
Credit) Natural Account 6421 - Goods and services sold by market rules:	*500*

On the next stage we will write off the scrap material with its cost price:

Debit) Natural Account 1624 - Goods (scrap metal) purchased for further sales	*430*
Credit) Natural Account 7290 – Other goods and service:	*430*

The sale of strategic inventory is captured as the exit of fixed assets.

Own consumption of inventory is recorded in the debit of goods and services account (7200) and in credit of relevant inventory accounts – during the transfer to commission; while inventory in commission, if necessary (if determined by the organization's internal accounting rules), are reflected in off balance sheet items.

We would like to draw attention to the fact that for accounting purposes, inventory is reflected in costs upon their commissioning (if the internal accounting rule does not regulate their recognition as costs during their actual usage), not upon their purchase.

Inventory is reflected in costs at the moment of purchase only in treasury operations envisaged by budget according to budgetary classification.

Valuation of inventory is performed through the following methods: the method of valuation according to individual expenses; (FIFO) method- First in, First- out; the weighted average value method (the above-mentioned methods are reviewed in the chapter of valuation 3.1.)

Example 3.4-4

On July 1st we purchased stationary (300 packs of office paper. Unit price – 6 GEL)

Debit) Natural Account 1627 - Other inventory (300X6):	*3,600*
Credit) Natural Account 3210 - Liabilities accrued through supply of goods and services:	*3,600*

20 packs of office paper were handed over to financial service on July 15 for daily use.

Debit) Natural Account 7230 - Office expenses	*120*
Credit) Natural Account 1627- Other inventory (20X6)	*120*

3.5 Accounting of Fixed Assets

Property, plant and equipment (also called tangible fixed assets) is a class of assets which have physical existence, which are held for internal use and which are expected to generate economic benefits for the government over more than one year.

Fixed assets accounting is regulated by the order N 1321 of the Minister of Finance of Georgia on “Approval of Accounting Instructions for Organizations Financed from the Budget of Autonomous Republics and Local Self-Governments”. According to instruction, the fixed asset:

- ✓ constitutes a manufactured asset
- ✓ is used in the production and service process over more than one year repeatedly or continuously
- ✓ The value is 500 GEL and above
- ✓ Meets the requirements determined for asset recognition.

Items, which have long life-cycle, but are not intended for multiple use, do not constitute fixed assets.

Fixed assets are recorded in the account 2100 and are classified as long-term nonfinancial assets.

Fixed assets acceptance procedures are the following: purchase, receipt free of charge and production with own resources or based on agreement.

Receipt of fixed assets are recorded at value, implying the paid funds or their equivalents for production or purchase and includes the following: purchase price, import duty, nonrefundable taxes, as well as other direct costs needed for activating the asset and all the expenses related to transfer of property rights.

Direct costs related to asset purchase are the following:

a) Costs of preparing location for an asset

b) Costs of delivery and loading-unloading of the asset;

c) Installation and dismantling costs

Costs related to transfer of property rights are the following:

a) Remuneration of services provided by valuators, civil engineers, architects, lawyers and real estate sales agents;

b) Taxes, paid during transfer of property rights

Administrative and other total overhead costs do not belong to the value of assets, except for the case when they are directly related to the purchase or the activation of an asset.

Costs related to testing of machinery and equipment do not belong to their value, if this is not necessary for asset's activation.

Borrowing costs directly related to asset's purchase, production or construction are recognized as costs by self-government units as soon as they are incurred.

Organizations may capitalize direct borrowing costs related to purchase, production or construction of assets, in case of proper necessary conditions.

Capitalization of costs related to use of loans as a value part of the assets begins when:

a) Direct costs are incurred for the asset

b) Primary costs related to the use of loan is incurred

c) Primary works are begun for the use of or ensuring sale condition of the asset.

The cost of the asset created by the organization is determined similarly to the acquired asset. In the event of an asset's performance, unusually high (over normative) expenses of raw materials and materials, labor and other resources are not included in the carrying amount of the asset

If the value of the fixed asset derived by barter is greater than the carrying amount of the sold asset, and the recipient organization does not have a liability on the surplus amount, the value of the asset with surplus amount is recognized by the recipient organization as an income received in a form of commodity derived from a capital grant or other income.

Example 3.5-1

The organization has acquired equipment for 20,000 GEL. 30% of purchase amount was paid in advance. The residual 70% will be paid within a month. The organization paid 2,000 GEL for transportation, 1,000 Gel for installation and the administrative costs, after service, amounted to 5,000 GEL.

The cost of the equipment will include 20,000+2,000+1,000=23,000 GEL

Advance Payment:

*Debit) Natural Account 1432 – Requirements for receipt of assets through advance payments (20,000*30%): 6,000*

Credit) Natural Account 1250 - Account of budget funds for organization's cash expenses: 6,000

Purchase of equipment:

Debit) Natural Account 2122 - Other machinery and equipment and inventory: 20,000

Credit) Natural Account 1432 – Requirements for receipt of assets through advance payments 6,000

Credit) Natural Account 3220 - Liabilities accrued through asset delivery: 14,000

Transportation of the equipment:

Credit) Natural Account 3220 - Liabilities accrued through asset delivery: 14,000

Installation of the equipment:

Debit) Natural Account 2122 - Other machinery and equipment and inventory 1,000

Credit) Natural Account 3220 - Liabilities accrued through asset delivery 1,000

Example 3.5-2

Organization "A" exchanged a vehicle in a machine with organization "B". The cost of the equipment is 10,000 GEL and the cost of the vehicle is 8,000 GEL. Organization "A" will not be obliged to pay extra money. The organization's accounting records will have the following form:

Debit) Natural Account 2122 - Other machinery and equipment: 10,000

Credit) Natural Account 2121 - Means of transport: 8,000

Credit) Natural Account 6322 - Capital grants in commodity form: 2,000

or

Credit) Natural Account 6400 – Other income 2,000

Receipt of fixed assets free of charge is recorded as follows:

Debit) Natural Account 2100 – fixed assets

Credit) Natural Account 6300- grants

or

Credit) Natural Account 6400 – other income

Acquisition of fixed assets (construction, other forms of creation, etc.) shall be reflected in the form of an unfinished fixed asset according to partial payments (before acquiring ownership rights) or by own funds of capital (till completion):

Debit) Natural Account 2141 – unfinished fixed assets

Credit) Natural Account 3220 – liabilities accrued through assets delivery

Completion and receipt of the asset will be reflected as:

Debit) Natural Account 2100 – fixed assets

Credit) Natural Account 2141 – unfinished fixed assets

The fixed assets acquired through financial leasing are registered as assets acquired and owned by the consumer or lessor (not by their legal owner or lessor). Purchase is recorded as:

Debit) Natural Account 2100 – fixed assets

Credit) Natural Account 3310/3130 – liabilities by loans

In case of normal (operating) lease, fixed assets remain on the balance of the lessee, and the lease payable levies and costs incurred will be reflected as expenditure:

Debit) Natural Account 7200-goods and services

Credit) Natural Account 3210-liabilities accrued through goods and service delivery

Costs on the substantial improvement of the assets of the ordinary (operating) lease are capitalized and reflected as the fixed asset of the organization:

Debit) Natural Account 2142 - substantial improvement of the property received under lease

Credit) Natural Account 3220 – liabilities accrued through assets delivery

Fixed assets taken under usual (operational) lease are reflected in the off-balance sheet item - Fixed Assets under Operating Lease - 01.

Exit transactions of fixed assets are the sale and transfer free of charge.

In case of difference between balance sheet value while selling the fixed asset and selling cost, excess/reduction is reflected in debit/credit of relevant accounts of non-financial assets and in credit/debit of non-operating income/non-operating costs account. Assets with selling value are reflected in credit of relevant non-financial assets accounts and in debit of relevant accounts of financial assets and requirements. If the liability against budget is generated through the sale of assets, the payable amount is recorded in the credit of relevant account of accrued liabilities against the budget (3245), and in the debit of the account of net value/profit loss (5100/5210)

Example 3.5-3

An organization sold equipment with the carrying cost of 8,000 GEL. The sale resulted in 10,000 GEL cash inflows. The organization's accounting records will have the following form:

Debit) Natural Account 1100-1500 - Financial assets and requirements:	*10,000*
Credit) Natural Account 2122 - Other machinery and inventory:	*8,000*
Credit) Natural Account 8100 - non-operating revenues:	*2,000*

After the initial registration of the asset, the fixed asset is accounted with its carrying value, taking into consideration all the changes that may have occurred after their receipt (including the principal capital consumption).

Example 3.5-4

An organization handed over a machinery with carrying amount of 2,000 GEL to a limited liability company. The organization's accounting records will have the following form:

Debit) Natural Account 7822 - Miscellaneous capital costs:	*2,000*
Credit) Natural Account 2122 - Other machinery and inventory:	*2,000*

The inventory commission shall submit a reasoned assertion on the necessity of writing off amortized or unused fixed assets along with the documents required for writing off the property to the Governor of the Municipality. The Governor/Mayor will forward the submitted documents to the Sakrebulo (city council) of self-governing unit for relevant decision. The decision on writing off the movable property registered in the ownership of the self-governing unit shall be made by the Chairman of Sakrebulo of the self-governing unit which issues the individual administrative-legal act with this purpose. The decision on writing off the self-governing unit is made by Sakrebulo of the self-governing unit.

The fixed assets shall be deemed written off on the basis of an administrative-legal act issued in conformity with the report of the Inventory Commission.

Write off of fixed assets with residual value are recorded as follows:

Debit) Natural Account 8200 – non operating costs of assets

Credit) Natural Account 2100 -fixed assets

3.6 Accounting of Long-Term Low-Cost Assets

Accounting of long-term low-price assets are regulated by the order N1321 of the Minister of Finance of Georgia on “Approval of Accounting Instructions for Organizations Financed from the Budget of Autonomous Republics and Local Self-Governments”. According to the instruction, the low- price assets are equipment, inventory and appliances, with the value of less than 500 GEL and intended for multiple use within more than one year. Long-term low-cost assets are registered on account 2200 and are classified as long-term non-financial assets.

Acquisition of long-term low-price assets are reflected by value that includes all the expenses related to acquisition, production and processing. The purchase costs includes purchase price, including all taxes including nonrefundable, transport and manufacturing expenses, and all expenses directly related to the acquisition of long-term low-cost assets.

Example 3.6-1

An organization has purchased a printer at a price of 200 GEL, which should be paid within a month. The organization paid for transportation 20 GEL and for installation 10 GEL.

Cost cost will include 200+20+10=230 GEL

Debit) Natural Account 2200 - Long-term low-cost assets: 230

Credit) Natural Account 3210- Liabilities accrued through supply of goods and services: 230

Receipt of long-term low-price assets free of charge are accounted in the following manner:

Debit) Natural Account 2200 - Long-term low-cost assets

Credit) Natural Account 6300 – grants or

Credit) Natural Account 6440 - voluntary transfers except grants

Own consumption of long-term low-cost assets when transfer into operation, is recorded as follows:

Debit) Natural Account 7200-goods and services

Credit) Natural Account 2200 - Long-term low-cost assets,

Expensed long-term low-cost assets in commission are registered in off balance sheet item "long-term low-cost assets in commission."

3.7 Accounting of Valuables

Accounting of values is regulated by order N1321 of the Minister of Finance of Georgia on "approval of accounting instructions for organizations financed from the budget of Autonomous Republics and Local Self-Governments". According to the instruction, the value is a manufactured asset of significant value, stored as the means of value accumulation (mainly, not used in production/service process, as well as for consumption). The valuable include precious stones and metals, as well as pieces of art. The valuables are accounted on corresponding sub-accounts of the account 2300 and are classified as long-term non-financial assets.

Name accountability of valuable assets must be established.

Receipt of valuables includes both the value of these assets and any expenditure related to property transfer, and in case of exit, the expenditures related to property transfer are recorded as goods and service expenses.

With the existence of an organized market of valuables their valuation may be performed according to the current market prices, including all types of agent service fees or commission payments. In other cases, valuation shall be performed at a price they are insured from fire, stealing and other risks.

Receipt or disbursement of valuables are reflected in the debits/credits of the relevant value account, in correspondence with credits/debit of other accounts.

Example 3.7-1

An organization has purchased precious metals at 20,000 GEL. It paid 500 GEL for the sales agent's service, and 1,000 for valuation expert.

Debit) Natural Account 2310 - Precious stones and metals: 21,500

Credit) Natural Account 1100-1500 - Financial assets and requirements: 21,500

3.8 Accounting of Non-Manufactured Assets

Non-manufactured assets include the assets generated naturally or created by legal or accounting operation for which the property protection can be ensured. Otherwise, the above mentioned does not constitute economic assets and are not reviewed as non-financial assets.

Name of the account	Account №
Non-manufactured assets	2400
land	2410
natural resources	2420
other natural assets	2430
non manufactured intangible assets	2440

The land naturally is the ground, with soil cover and surface waters related to it including the improvements (grading, roads, etc.), which are impossible to physically separate from land.

The natural resources include proven reserves of minerals such as oil, natural gas, coal (including anthracite, bitumen and coal), metal shells (including black, colored and precious metals) and useful non-metallic minerals (including deposits of quarries, clay and sand quarries, chemicals and fertilizers, salt, quartz, gypsum, natural gemstones, bitumen, peat, etc.). Shafts, boreholes and other facilities necessary for abstraction of natural resources constitute the fixed assets.

Radio frequency spectrum license, non-cultivated biological resources, water resources and electromagnetic spectrum belong to other natural assets.

Non-cultivated biological resources include animals and plants, on which it is possible to establish property rights and protection. However, their natural regeneration is not subject to direct control, responsibility and management of any state unit. For instance: virgin forests and fish stock, which can be commercially exploited. These categories cover only the natural resources having economic value and not included in the value of the land related to it.

Non manufactured intangible assets include products intended for public welfare, which are based on legal or accounting actions. Some assets of this type give the right to the owner to conduct this or that specific activity or produce specific type of good or service and in addition, forbid other entities to conduct the like activity without the proprietor's permit. Nonproduction intangible assets cover patent facilities, leasing agreements and other contracts, as well as purchased goodwill.

Non manufactured assets, as naturally generated or the assets created by legal or accounting actions, are recognized as economic assets and are reflected in accounting as other events and recorded in debit of relevant accounts of non-manufactured assets (Natural Account 2400) and in the credit of non-operating income account (Natural Account 8100), except for the case, when the state unit purchases non manufactured asset.

Example 3.8-1

A self-government unit has registered 5,000m2 non-agricultural land existing on the territory of the municipality in public registry. Normative price of the land determined by the municipality is 80 GEL/m2.

Debit) Natural Account 2410 - Land (5000 m2 X 80 GEL):	*400,000*
Credit) Natural Account 8100 – Non-operation income:	*400,000*

Some non-manufactured/intangible assets experience depletion and are exhausted, accordingly their value decreases. Reduction of non-cultivated biological resources or water resources are reflected in debit of account of non-operating costs of assets (natural 8200) and in credit of relevant account of non-manufactured/intangible assets (natural 2400).

3.9 Accounting of Liabilities

Liability is an obligation created as a result of past event, the payment (coverage) of which will cause the outflow of unit resources in the forms of economic benefit or service potential.

The liability (accounts payable) function must be:

Example 3.8-2

We have purchased land at a cost of 15,000 GEL from a private entity. The payable amounts related to registration (notary, registration in public registry, etc.) amounted to 350 GEL. In this case, the value of the land will be assessed at the cost of 15,350 (15,000+350) GEL.

a. Separate from procurement and receiving activities.

b. Independent from any general ledger recording tasks

Accounts Payable personnel must review debit balance accounts at least quarterly and request remittance on debit amounts outstanding more than 90 days.

In case of generating liability, an obligation and corresponding responsibility is imposed on organization, fulfillment of which is subject to certain norms. Payment of liability is related to the exit of an economic resource from the organization in favor of the debtor. This can be executed in several ways: by payment of money, transfer of other assets, service provision.

Liability can also be covered by the debtor declining the liability (disclaim).

Liabilities are recorded in the following accounts:

Name of the account	Account №
Liabilities	3000
Short-term financial liabilities	3100
Liabilities through deposits	3110
Liabilities through securities, excluding shares	3120
Liabilities through short-term loans	3130
Short-term liabilities through budget loans	3131
Short-term loan liabilities through non-budget funds	3132
Liabilities with shares and other equity	3140
Derivative financial instruments	3150
Other short-term accounts payable	3200
Liabilities imposed as a result of delivery of goods and services	3210
Liabilities accrued by assets delivery	3220
Liabilities through barter	3230
Other tax liabilities and liabilities against budget	3240
Payable profit tax	3241
Payable VAT	3242
Payable income tax	3243
Other taxes	3244
Liabilities accrued against the budget	3245
Liabilities against employees and scholarship holders	3250
Accrued salaries for staff members	3251
Accrued salaries for freelancers	3252
Liabilities for business trips within the country	3253
Liabilities for business trips abroad	3254
Liabilities accrued through social assistance in a cash form provided by the employer	3255
Liabilities accrued through social assistance in a commodity form provided by the employer	3256
Liabilities through salary detentions of the organization's employees	3257
Payable scholarships	3258
Social Insurance charges	3259
Liabilities against deponents	3260
Liabilities accrued through social assistance	3270
Liabilities accrued through social assistance provided in a cash form	3271
Liabilities accrued through social assistance provided in a commodity form	3272
Other short-term accounts payable	3280
Lease amount received in advance	3281
Other revenues received in advance	3282
Accrued payable rent	3283

Name of the account	Account №
Accrued payable interests	3284
Payable dividends	3285
Other accrued short-term liabilities	3286
Long-term financial liabilities and accounts payable	3300
Long-term liabilities through loans	3310
Long-term liabilities through budget funds	3311
Long-term loan liabilities through non budget funds	3312
Other long-term financial liabilities	3320
Long-term accounts payable	3330
Long-term Accounts payable accrued through service delivery	3331
Long term accounts payable accrued through asset delivery	3332
Other long-term accounts payable	3333

Operations are recorded as liabilities, when the cash amount of financial liability increases or decreases.

When the operation comprises generation or payment of existing financial liability, comes when the agreement is signed, or the debtor pays the amount or transfers any other financial asset to the creditor.

The value of generation or payment of financial liability is their fair market value at the time of creation.

When purchasing goods or services, the value of generated accounts payable is the value of received goods or services.

Generation/payment of financial liabilities and other accounts payable is reflected in the credit/debit of relevant accounts of financial liabilities/other accounts payable, in correspondence with debits/credits of the other accounts.

Example 3.9-1

As per the agreed conditions, a supplier provided the organization with 10 office desks at a price of 400 GEL each on February 10. Payment shall be done in 10 days from the date of supply.

Debit) Natural Account 2220 – Inventory (10X400): 4,000

Credit) Natural Account 3210 – Liabilities accrued through supply of goods and services: 4000

Payment was done on February 15 with the amount of 4,000 GEL. First, we record financing received from the budget and then reduction of liability.

Debit) Natural Account 1250 – Budget funds for organization's cash expenses: 4,000

Credit) Natural Account 4100 – Funding received from the budget: 4,000

Debit) Natural Account 3210 - Liabilities accrued through supply of goods and services: 4000

Credit) Natural Account 1250 - Budget funds for organization's cash expenses: 4,000

Accrual of salaries generates liabilities to the employees. In general, basis for salary accrual are organization's orders on appointment, layoff and rotation of employees, corresponding with the approved staff list and salaries, monthly register of use of working time in a form set by the organization (workplace entrance register or/and specific admission control equipment) and other documents defined by the employment agreement or internal regulation (if any).

Salary accrual and payment rules shall be regulated by the internal regulation of the organization.

Example 3.9-2

On May 29, accrued salary for employees made up 80,000 GEL and for freelancers – 5,000 GEL.

Debit) Natural Account 7111 – Salaries in a cash form:	*80,000*
Credit) Natural Account 3251 – Salaries accrued for employees:	*80,000*
Debit) Natural Account 7210 – Freelancers' salaries:	*5,000*
Credit) Natural Account 3252 – Salaries accrued for freelancers:	*5,000*

Some portion of the amount may be retained from the salaries of employees (insurance, trade unions, execution, etc.). In parallel with salary accrual we shall record these amounts on relevant accounts. Let's say we need to retain from the salaries of employees' insurance fee totaling to 1,500 GEL and 300 GEL for execution.

Retention of insurance amount:

Debit) Natural Account 3251 – Salaries accrued for employees:	*1,500*
Credit) Natural Account 3257 – Liabilities arising out of retention of certain amounts from the salaries of the organization employees:	*1,500*

Retention of execution amounts:

Debit) Natural Account 3251 - Salaries accrued for employees:	*500*
Credit) Natural Account 3257 - Liabilities born out of detention of certain amounts from the salaries of the organization employees	*500*

As per the tax code, tax agent is obliged to retain income tax at the tax source. Therefore, whenever we make payment of salaries, we shall retain income tax and transfer it to the budget.

Debit) Natural Account 3251 – Accrues salaries for employees:	*16,000*
Credit) Natural Account 3243 – Payable income tax:	*16,000*

3.10 Accounting of Funding

Funding received by the organization from the budget is subject to cash-based accounting meaning that funding sources received from the budget shall be recorded the same time as the budget payments are performed.

Funding is recorded into two accounts as per the chart of accounts: funding received from the budget – (natural account 4100) and funding received from the budget for pensions and benefits – (natural account 4200)

Sources received by the organization that are denoted for payments to budget (budgetary sources, credits and grants) are recorded on account (natural account 4100) “financing received from the budget.” Financing received from the budget is recorded in debit of 1250 account and in credit of natural account 4100 account.

Example 3.10-1

We made advance payment of 13,000 GEL to the supplier.

Debit) Natural Account 1250 – Budget funds for organization’s cash expenses:	*13,000*
Credit) Natural Account 4100 – Financing received from the budget:	*13,000*
Debit) Natural Account 1432 – Requirement for supply of assets with advance payment:	*13,000*
Credit) Natural Account 1250 - Budget funds for organization’s cash expenses:	*13,000*

Returned amounts paid during the current year are reflected in debit of 4100 account in correspondence with credit of 1250 account, i.e. we are performing reverse entry.

Example 3.10-2

The supplier paid back a part of advance payment with the amount of 4,300 GEL.

Debit) Natural Account 4100 – Financing received from the budget:	*4,300*
Credit) Natural Account 1250 – Budget funds for organization’s cash expenses:	*4,300*

The above example demonstrates return of the advance payment of the current year. As to the return of advance payment of previous year, there are two different ways of doing it:

1. Debtor makes transfer of returnable amount on a budget treasury account

Debit) Natural Account 5100 – Net value:	*4,300*
Credit) Natural Account 3245 –Liabilities accrued against the budget:	*4,300*
Debit) Natural Account 3245 - Liabilities accrued against the budget:	*4,300*
Credit) Natural Account 1432 - Requirements on supply of assets w/ advance payment:	*4300*

2. Debtor makes transfer of returnable amount on a bank account of the organization

Debit) Natural Account 1211 – Current account in a bank for national currency:	*4,300*
Credit) Natural Account 1432 - Requirements on supply of assets w/advance payment:	*4,300*
Debit) Natural Account 5100 – Net value:	*4,300*
Credit) Natural Account 3245 - Liabilities accrued against the budget:	*4,300*
Debit) Natural Account 3245 - Liabilities accrued against the budget:	*4,300*
Credit) Natural Account 1211 - Current account in a bank for national currency:	*4,300*

3.11 Equity Accounting

In general, equity is the part which remains after all liabilities are covered and is governed by the well-known balance equation: **Equity = Assets - Liabilities**.

For the accounts of budgetary organizations, equity is represented by the net value and share capital. Net value is the difference between all assets formed by the budget resources and all liabilities envisaged by the budget. Thus, net value is a balance article formed only through the operations of budget resources.

As to the share capital, it is represented as the difference between assets formed through non-budgetary resources (including economic activity) and liabilities formed through non-budgetary resources (including economic activity).

Municipalities have net value as their activities are only financed through the budget, as to the budgetary organizations, they have equity and net value as they are authorized to perform economic activities and obtain other resources. These type of budgetary organizations comprise LEPLs and non-entrepreneurial (noncommercial) Legal Entities.

Own equity comprises profit/loss, retained earnings and uncovered loss of the reporting period.

Profit/loss account shows a difference between (operational and non-operational) revenues and (operational and non-operational) costs from non-budgetary activity during the reporting period.

By the end of reporting year, balance of profit/loss account shall be transferred to the account of retained earnings or uncovered loss respectively.

Retained earnings account keeps record of undistributed profits of previous years, as well as profit of reporting year that remained undistributed.

Uncovered loss account shows the losses of the previous and reporting year.

Net value (5100) shall be closed at the end of the reporting year in correspondence with debit accounts of funding, revenues and non-operational revenues.

Debit) Natural Account 4100 - funding

Credit) Natural Account 5100 – net value

In case of costs and operational costs net value shall be closed in correspondence with credit accounts.

Debit) Natural Account 5100 – net value

Credit) Natural Account 7000 – expenses account

3.12 Accounting of Revenues

Revenue is an increase of capital as a result of operations.

There are 4 main revenue sources for state authorities: # 1 taxes and other mandatory transfers imposed by the state authorities; # 2 property related revenues through asset ownership; # 3 sale of goods and services; and # 4 voluntary transfers from other entities.

Billing of taxes and services must be performed promptly and in proper amounts. Self-assessed taxpayers need to be actively monitored. Exemptions or adjustments can only be provided by way of independent authorizations.

In addition to this, cash-based method may be used for accounting revenues from monetary operations for those cases defined in this guidebook.

Name of account	Account number
Revenues	6000
Taxes	6100
Social payments	6200
Grants	6300
Grants in a cash form	6310
Current grants in a cash form	6311
Capital grants in a cash form	6312
Grants in a form of inventory	6320
Current grants in a form of inventory	6321
Capital grants in a form of inventory	6322
Other incomes Roads Bridges Tunnels	6400
Property related revenues	6410
Interests	6411
Dividends	6412
Cash from the revenues of quasi corporations	6413
Property related revenues applied to the owners of insurance policy	6414
Rent/lease	6415
Sales of goods and services	6420
Market rule-based sales of goods and services	6421
Administrative taxes	6422
Nonmarket rule-based sales of goods and services	6423
Conditional sales of goods and services	6424
Sanctions, penalties and fines	6430
Voluntary transfers, excluding grants	6440
Current	6441
Capital	6442
Other non-classified revenue	6450

Revenue formation is reflected in accounting entries in debit accounts of relevant financial and non-financial assets, in correspondence with relevant revenue (natural account 6000) credit accounts.

It is noteworthy that current order on “approval of accounting instruction for entities financed through the budgets of Autonomous Republics and Local Self-Governments” doesn’t provide complete and exhaustive list of revenue accounting methods, resulting in discrepancy between the opinions of various specialists.

Types of revenues like taxes, grants, fees, etc. are not accounted. They are only accounted based on cash method in budget performance report. Though types of revenue defined by the budget classification absolutely coincide with the revenue accounts, moreover, with the aim of accurate accounting, accounts of capital grants and transfers are added.

Example 3.12-1

We received 5 laptops from the state. Cost of each laptop is 700 GEL. We also received 10 cartridges for printers, cost of each is 25 GEL. As laptop is an asset, it shall be classified as a capital grant; cartridges, which are materials, being inventory are classified as current grants.

Debit) Natural Account 2122 – Other machinery and equipment and inventory (5X700):	*3,500*
Credit) Natural Account 6321 – Current grants in a form of inventory:	*3,500*
Debit) Natural Account 1627 – Other inventory (10X25):	*250*
Credit) Natural Account 6322 – Capital grants in a form of inventory:	*250*

As per the Budget Code, all receipts of the state budget, or budgets of Autonomous Republics and LSGs, also LEPLs and Non-Entrepreneurial (Non-Commercial) Legal Entities defined by this Code are immediately directed to the relevant budget. Thereafter, municipality is obliged to transfer the received interest to the single account of the budget (TSA).

Example 3.12-2

Municipalities may put their free resources in a commercial bank with the aim to earn interest. Over time the municipality is accumulating resources on a current account in a commercial bank. The bank accrues interest to the amount by the end of each month and makes capitalization (transfer of interest amount on the client’s account). Respectively, interest accrued, and amount transferred to the client’s account made up 120,000 GEL in August.

Debit) Natural Account 1220 – Other accounts in a bank:	*120,000*
Credit) Natural Account 6411 – Interest:	*120,000*

Budgetary organizations shall ensure accrual of administrative and other penalties and fines and monitor their collection.

Example 3.12-3

Due to violation of agreement conditions a supplier has to pay penalty of 3,000 GEL.

Debit) Natural Account 1480 – Other short-term requirements:	*3,000*
Credit) Natural Account 6430 – Sanctions, penalties, fines:	*3,000*

Voluntary transfers (also known as gifts or donations) are revenues from physical entities, private noncommercial organizations, non-governmental funds and organizations, enterprises and corporations (excl. government and international organizations). This category comprises monetary benefits (in case of accrual method, non-monetary gifts/benefits) and other voluntary transfers.

Example 3.12-4

A Legal Entities of Private Law transferred construction design of water retaining structure to municipality free of charge. Cost of design is 4,500 GEL

Debit) Natural Account 2141 – Uncompleted fixed assets:	*4,500 GEL*
Credit) Natural Account 6442 – Capital voluntary transfers, except of grants:	*4,500 GEL*

3.13 Accounting of Expenses

Expense is a reduction of equity as a result of operations.

Governmental organizations have two basic economic responsibilities of provision of special goods and services to population on non-market conditions and through payments by transfer.

Purchase of financial and non-financial assets are not classified as spending operations, these are operations, when one type of asset is exchanged into another type of asset.

Lists of all proposed payments must be validated, signed and dated before the payments are made. All discrepancies between the information must be independently resolved before payment is made.

The disbursement function must have the following segregation of duties:

A) Separation of payment preparation from cheque signing
B) Accounts payable tasks must be separate from procurement and receiving activities
C) Separation of payment preparation, printing, signing and distribution activity from supplier validation and set-up and from invoice input activity
D) Vendor validation and set-up must be separated from invoice input activity and payment preparation and distribution

Economic classification of expenses enables identification of expenses according to the types of economy through grouping them based on their economic scope and represents a basis for structure of chart of accounts.

Name of account	Account number
Expenses	7000
Salaries of employees	7100
Salaries	7110
Salaries in a form of cash	7111
Salaries in a form of commodity	7112
Social benefits	7120
Goods and services	7200
Salaries of freelancers	7210
Business trip	7220
Office expenses	7230
Representative costs	7240
Food and medical costs	7250
Food costs	7251
Medical costs	7252
Purchase of soft inventory and uniforms, personal hygiene related costs	7260
Maintenance and operation costs of transport, equipment and instruments	7270
Military equipment and bullets purchase costs	7280
Other goods and services	7290
Basic capital consumption	7300
Physical depreciation of fixed assets	7310
Moral depreciation and loss due to accidental damage	
Interest	7400
Subsidies	7500
Grants	7600
Grants in a cash form	7610
Current grants in a cash form	7611
Capital grants in a cash form	7612
Grants in a form of inventory	7620
Current grants in a form of inventory	7621
Capital Grants in a form of inventory	7622
Social security	7700
Social insurance	7710
Social aid	7720
Social aid provided by the employer	7730
Other costs	7800
Property related costs excluding interest	7810

Salary payment means financial compensation paid by employer to employee for the works performed within the reporting period.

According to the chart of accounts, salary is defined by a single account, though for the purposes of analytical accounting, adding sub-accounts would be advisable.

Example 3.13-1 "Salaries and Bonus"

Salaries of 25,000 GEL and bonus of 10,000 GEL is accrued.

Debit) Natural Account 7111 – Salaries:	*25,000*
Credit) Natural Account 3251 – Accrued salaries for regular employees:	*25,000*
Debit) Natural Account 7111 – Bonus:	*10,000*
Credit) Natural Account 3215 – Accrued salaries for regular employees:	*10,000*

Basic salary accrual statement shall be prepared when salary is accrued. Basis for salary accrual are orders of the organization on appointment, lay off and rotation of employee, corresponding with the approved staff list and salaries, monthly register of use of working time in a form set by the organization (workplace entrance register or/and specific admission control equipment), and other documents defined by the employment agreement or internal regulation (if any). All should be set out in the internal regulation of the organization.

As to the accrual of independent contractors wages, it is done in a similar way with the only difference in account numbers.

Example 3.13-2 "Accrual of Independent Contractors"

Wages for Independent Contractors of 5,000 GEL

Debit) Natural Account 7220 – Wages of freelancers:	*5,000*
Credit) Natural Account 3252 – Accrued wages for freelancers:	*5,000*

Office expenses category comprises costs for low cost and multi-use subjects. Office renovations, purchase of stationery, communication, utilities, office hygiene and other costs as necessary for office maintenance.

Example 3.13-3 "Office Expenses"

Floor renovation works were performed at the lobby of an administrative building. Cost of renovation made up 1,300 GEL. As floor replacement doesn't increase productivity of the organization or its useful life, it is classified as a spending operation and expense

Debit) Natural Account 7230 – Office expenses:	*1,300*
Credit) Natural Account 3210 - Liabilities accrued through supply of goods and service:	*1,300*

Representative expenses imply both representative costs incurred for Georgian citizens and costs incurred for foreign guests within the frames of the same events. It includes representative costs of reception and official dinner, party and other events, excursions and cultural-sightseeing events, souvenirs purchase or production, transfers from/to airport (VIP lounge service), transportation, accommodation (rooms reservations, cost of accommodation, etc.) consulate service (obtain/prolong visa) and other representative costs.

Physical depreciation of fixed assets is reduction of the asset value as per the norms defined by the Order #439 of the Minister of Finance of Georgia dated December 31, 2002.

Depreciation of fixed asset is accrued at the end of reporting year despite the month of the year in which they were purchased or produced, whether they are in operation or not.

Depreciation is accrued at the end of year and is calculated by multiplying their historical value by the annual rate envisaged by the Order #439.

Example 3.13-4 "Depreciation of Fixed Assets"

A laptop was purchased in September at a price of 700 GEL. Annual rate of depreciation of hardware is 20%. By the end of year value of depreciation will be 700X20%=140 GEL. Value of asset is reduced in proportion with the depreciation value.

Debit) Natural Account 7310 – Physical depreciation of fixed assets: 140

Credit) Natural Account 2122 – Other machinery and equipment and inventory: 140

Depreciation of intangible assets is accrued in proportion of their useful life if possible, otherwise the applied rate is 10% annually.

Example 3.13-5 "Depreciation of Intangible Asset"

A service provider created an informational webpage for tourist guidebook of the municipality, the webpage expected operational period is anticipated to be 5 years. Cost of webpage development is 20,000 GEL. Municipality will benefit from the use of this intangible asset for 5-year, depreciation will be proportionally distributed over this period 20,000 /5=4000, i.e. annual depreciation made up 4,000 GEL.

Debit) Natural Account 7310 – Physical depreciation of fixed assets: 4000

Credit) Natural Account 2132 – Intangible assets: 4000

3.14 Accounting of Non-Operational Incomes and Costs

Changes of volume or value of assets or liabilities, not resulted by the organization operations are classified as non-operational incomes and non-operational costs.

Non-operational incomes/costs are born out as a result of:

- ✓ change of cash value of the asset or liability due to change of price level and structure, on condition that quality or quantity of the asset or liability has not changed;
- ✓ exchange rate – in case of assets and liabilities evaluated in foreign currency;
- ✓ recognition/derecognition of existing sites as economic assets;
- ✓ other quantitative or qualitative changes in assets resulted from other events;
  a) events that change quantity of existing economic assets;

b) events that result in recognition or derecognition of those assets being discovered, created, canceled or destroyed.

- ✓ Reclassification of assets/liabilities that may be resulted from change of purpose of use of the asset.

Example 3.14-1

During the "taking of inventory", a qualified specialist evaluated a vehicle at a market price of 12,000 GEL. Balance amount of the vehicle was 3,500 GEL. In this case, value of the vehicle increased by 8,500 GEL due to reasons above control of the organization and without any designated operational activity. Thus, increase in value is not a result of the operation. It is recognized as a change of value and classified as a non-operational income.

Debit) Natural Account 2121 – Transportation means: *8,500*

Credit) Natural Account 8100 – Non-operational incomes: *8,500*

Example 3.14-2 "Write Off of Inventory"

As the result of an inventory check it was demonstrated that the organization possesses useless inventory and should be subjected to write off. Balance value of inventory amounts to 7,000 GEL.

In this case, we deal with volumetric change of assets and is classified as non-operational cost.

Debit) Natural Account 8200 – Non-operational costs: *7,000*

Credit) Natural Account 2122 – Other machinery and equipment and inventory: *7,000*

3.15 Accounting of Off -Balance Sheet Items

To ensure additional information on articles which are part of the balance, but not accounted as balance sheet items the recording of information as off balance sheet items is suggested.

Off-balance sheet items are analytical accounting. They are not used for double entries, though in a technical point of view we may correspond them with virtual accounts.

Fixed assets under operational lease	01
Inventory received under responsible storage	02
Written off debts of insolvent debtors	03
Expensed inventory in operation	04
Contingent requirements	05
Contingent liabilities	06
Equity formation through own resources	07
Amortized fixed assets	08
Overdue indebtedness	09
Long term low cost expensed assets in operation	10
Movable property transferable for disposal	11

Bank guarantees	12

Complete supporting documentation of fixed assets register must be maintained and include information regarding asset description, location, asset tag number, status and condition. Verification of fixed assets must be completed at least bi-annually. Verification must consider the present state and usefulness against the current value. Any differences must be recorded promptly.

Fixed assets under operational lease are the assets received through lease from another organization at a cost defined by the lease agreement. Analytical accounting of leased fixed assets is performed according to lessors and subject of lease itself.

The off-balance sheet account “Inventory received under responsible storage” keeps records on inventory received by the organization for temporary responsible storage.

Off-balance sheet account “Written off debts of insolvent debtors” keeps records on written off debts of insolvent debtors (excluding the debts written off on the basis of the court decision), with the aim of possible removal of indebtedness in case of change of supervisor or the property condition of the debtors within 5 years from the date of their write off. Resources received for covering this indebtedness shall be written off from the given article and is subject to recording to the relevant account.

Off-balance sheet account “Contingent Assets/ Requirements/ Receivables ” keeps record of those Assets/Requirements/Receivables that enter into force only in case of existence of previously agreed condition(s); by defining rights, that can influence future decisions, including requirements for remuneration of loss or requirements/demands/receivables related to the court cases being processed, etc.

Off balance sheet account “Contingent liabilities” keeps record of liabilities that enter into force only in case of existence of previously agreed condition(s); by defining liabilities, that can influence future decisions, including payment guarantee to the third party – letter of credits, credit lines, payment guarantees of unexpected tax liabilities born out of agreements with the government or other entities or otherwise and other liabilities.

Off-balance sheet item “Equity formation through own resource” keeps record of expenses incurred for equity formation with own resource, including salaries, inventory and service, etc.

Off-balance sheet account “Amortized fixed assets” keeps record of completely worn out (amortized) fixed assets, indicating primary (historic) value, revaluated value, till the ultimate disposal of the asset in accordance with the current legislation.

Off-balance sheet account “overdue indebtedness” keeps account of all accounts payable born out within the previous period of the reporting year.

Off-balance sheet account “Long term low cost expensed assets in operation” keeps account of long-term low-cost assets that were placed into operation and expensed.

Off-balance sheet item “Bank guarantees” keeps account of guarantees (when advance payments are made by the organization) envisaged by the law on state procurement.

4. ACCOUNTING OF DEPRECIATION

Relevance

Knowledge of depreciation and amortization is important for every person working at self-governments. It is necessary that accountants are aware of technical aspects of amortization and depreciation calculation, as required by the legislation. Management of the organization – heads of departments and other officials, as well as employees being involved in budgeting process, shall also be aware of the mentioned technical aspects. It will enable them to assess financial effects of purchase and ownership of assets, e.g. effect of self-government owned vehicle. This chapter also describes the facts and aspects that we need to consider keeping the assets in sound condition – repair, maintenance and renovation.

Laws and regulations discussed:

- ✓ Order #439 of the Minister of Finance of Georgia dated December 31, 2002 on approval of “Instructions for physical depreciation norms of fixed assets and their accounting for budget organizations”.
- ✓ Order #1321 of the Minister of Finance of Georgia dated December 28, 2007 on “Approval of Accounting Instructions for Organizations Financed from The Budget of Autonomous Republics and Local Self-Governments.”

There should be segregation of duties between initiation, acquisition, authorization, approval and recording, access and disposal of assets.

4.1. General Rules for Accrual of Depreciation

After the initial recording of an item as an asset, the fixed asset is accounted for with its residual (balance) value- the “net” book value. This net book value is calculated based on all those changes which take place after activation of the asset (including depreciation/consumption of basic capital).

Consumption of basic capital is reduction of value of the fixed asset owned by the LSG, as a result of physical/natural/technological depreciation or accidental damage within the reporting period.

For the purpose of accounting, preliminary defined annual rates of physical depreciation of fixed assets are provided by the Order #439 of the Minister of Finance of Georgia on approval of “Instructions On Physical Depreciation Norms For Fixed Assets Of Budgetary Organizations And Their Accounting”, while depreciation of intangible fixed assets is accrued proportionally with their useful life, if possible, otherwise annual 10% depreciation rate is applied.

Depreciation is not accrued on cultivated assets (excluding draught animals and perennial crop of useful life), uncompleted fixed assets (works in progress) and library stock.

For fixed assets, despite which month of the reporting year they were purchased or produced, or whether they are in operation or not, depreciation is accrued by the end on the year for the whole calendar year and is calculated by multiplying their primary (historical) value with annual rate set out by this # 439 instruction. In case of significant improvement or revaluation, depreciation of the revaluated value shall be added to this amount.

By the end of reporting year physical depreciation of fixed asset shall be recognized as an expense and be recorded as follows:

Debit) Natural Account 7310 – physical depreciation of fixed assets

Credit) Natural Account 2100 – fixed assets

Completely worn out (depreciated) fixed assets shall be accounted in the off-balance sheet account "amortized fixed assets (08)" before being written off. They shall be recorded at their primary (historical) value and substantial improvement (revaluation) value.

4.2. Depreciation Norms

Physical depreciation norms for fixed assets of budgetary organizations are defined by the Order #439 of the Minister of Finance of Georgia on approval of "Instructions on Physical Depreciation Norms for Fixed Assets of Budgetary Organizations and Their Accounting", Annex 1.

Fixed assets are divided into 8 basic groups, each being divided into sub-groups as per the types of assets:

01	Buildings
02	Facilities
03	Transmittion Equipment
04	Machinery And Equipment
05	Transportation Means
06	Tools and Instruments
07	Inventory and Equipment Used in Manufacture
08	Draught Animal

Depreciation rates are defined for each sub-group separately, e.g.

Code	Types and groups of fixed assets	Annual depreciation rate %
01 Buildings: Manufacturing and non-manufacturing facilities		
1000	Multistory buildings (more than two), excluding special technological purpose facilities; One-story buildings with RC and metal frame, stone walls, thick blocks and panels, RC, metal and other steady roofing	1.0
1001	Two-story buildings of any purpose (except of wooden ones)	1.2
1002	Special technological purpose multistory buildings; One-story buildings without frame and with stone walls, thick blocks and panels, RC, metal wooden and other roofing.	1.7
1003	Wooden buildings with posts or logs, one-story and above.	2.5
1004	Buildings made of multi-layer material (airproof, pneumo-framed, etc.), dismantling and assembling container type structures, wooden, frame type, frame-panel and panel type, wooden and other light structures.	10.0
1005	Structures with frame-panel and panel materials with metal and wooden frame structures.	5.0

Accrual of depreciation on fixed asset specifically listed in approved list of rates is performed in correspondence with the rates of similar (analogical) fixed assets.

In cases where the use of single rates is impossible or there is a new type of fixed assets created, organizations will develop proposed depreciation rates along with justification and submit these for approval to the Ministry of Finance of Georgia.

If separate components of fixed asset have different useful life and related economic benefits are not received at the same time, for the purposes of accrual of depreciation it is necessary to account them separately (if they satisfy fixed assets recognition criteria), distribute common expenses across components and use different depreciation rates.

Example 4.2-1

*An organization purchased a two-story wooden building on September 23, 2016 at a price of 15,000 GEL. Depreciation cost of Y2016 will be 15,000*2.5%=375 Gel.*

Debit) Natural Account 7310 – Physical depreciation of fixed assets:	*375 Gel*
Credit) Natural Account 2100 – Fixed assets:	*375 Gel*

4.3. Accounting of Reconstruction, Maintenance and Repair Expenses of Assets

Substantial improvement of existing assets – renovation, reconstruction or expansion, that increases capacity or quality or useful life of the existing fixed asset, despite the fact that they physically perform as a part of an existing fixed asset, is considered as receipt of a fixed asset.

Expenses incurred for substantial improvement can be:

a) Modification of elements of buildings and facilities aimed at extension of their useful life and increase of capacity;
b) Repair of parts of machinery and equipment aimed at improved quality of production /service;
c) Implementation of new production processes aimed at substantial decrease of operation costs.

Example 4.3-1 "Replacement of a Part of Equipment"

An organization replaced a part of equipment with a new improved one that resulted in increased capacity of the equipment. Cost of the part was 10,000 GEL.

Debit) Natural Account 2100 – Fixed assets:	*10,000*
Credit) Natural Account 1100 – 1500 – Financial assets and liabilities:	*10,000*

Expenses incurred for maintenance and regular repair of fixed assets which do not influence the capacity, quality, service potential or useful life are recognized as costs in debit account of goods and services (Natural Account 7200).

Existing assets maintenance and regular repair characteristics are:

a) They are regular activities that are obligatory for owners or users of the fixed asset to keep it useful till the end of its pre-defined useful life.
b) They do not change fixed assets or their operational characteristics, keep them in operational condition or in case of damage, restore their primary condition.

Example 4.3-2

An organization changes tyres of a vehicle at a cost of 800 GEL.

Debit) Natural Account 7200 – Goods and services:	*800*
Credit) Natural Account 1100-1500 - Financial assets and requirements:	*800*

5 Inventory

Relevance

Inventory used by the LSG is important. Self-governments shall possess accurate information on quantity of property and their actual condition. This chapter describes the related issues, considering the fact that each subject purchased with public resources is valuable and this value shall be accounted. Knowledge of technical aspects of inventory is necessary for people engaged in accounting and materially responsible employees, as well as for consumers of inventory and budgeting specialists. Inventory consumers and budgeting specialists – administrative personnel and elected officials shall be aware what is the cost of purchase and storage of inventory. Accountants and materially responsible people shall know what is necessary to reflect the correct value of inventory in accounting recordings.

Laws and regulations discussed:

- ✓ Order #605 of the Minister of Finance of Georgia dated July 23, 2010 on approval of "rules of inventory of property, requirements and liabilities of public organizations."
- ✓ Order #449 of the Minister of Finance of Georgia dated December 31, 2013 on approval of "accounting forms of source documents and accounting registries for budgetary organizations."

The stores inward department must be physically segregated from the ordering department. Access to the stores inward department must be restricted to authorized personnel only. All incoming items and supplies must be processed by the designated stores inward location. The stores inward location must accept only those goods for which an approved purchase order has been prepared. All other receipts must be returned to the supplier or investigated for propriety promptly. Each designated stores inward location must account for and provide evidence of a receiving transaction for all items, services or supplies accepted. Incoming goods must be secured and safeguarded upon receipt. Valuable commodities must be protected during the stores inward process. Corrections of errors in receiving transactions may only be undertaken by authorized personnel and require co-signatures.

5.1 Purpose of Inventory

In the process of operation of an organization there are activities which result in changes of financial and non-financial assets and liabilities. These changes can be physical damage to non-financial assets in usual operation process, destroy, casual use that results in loss, etc.

With the aim of ensuring reliability and accuracy of accounting and reporting data and facilitate effective use of economic resources, organization perform on a regular basis a physical inventory of its property, requirements and liabilities.

Purpose of a physical inventory of assets and liabilities is to:

a) Control over protection/safety of financial and non-financial assets;
b) Identify actual balance of inventory as reflected in assets and labilities and off-balance sheet items;
c) Identify unused/useless assets;
d) Check rules and conditions of storage of financial and non-financial assets;

e) Check if operation rules of non-financial assets are observed;
f) Check actuality of requirements and liabilities demonstrated in balance of the organization;
g) Comparison of actual balance of assets and liabilities with accounting data of the organization.

First and foremost, the purpose of the physical inventory is effective use of economic resources of the organization. In cases where physical inventory is not performed on a regular basis and in correspondence with the current legislation, there is a high risk of wasteful use of property.

Quite often the physical inventory is perceived as inventory of only material assets – those which have a physical presence like furniture, equipment, etc., but in fact physical inventory shall comprise material property as well as financial assets and liabilities.

Inventory of financial assets implies documentary check of cash resources and accounts receivable; measures for covering indebtedness shall be defined, also irrecoverable accounts receivable (if term of limitation is exhausted, debtor is removed from the entrepreneurial registry, physical person passed away and has no heir, etc.) shall be recorded and written off the balance. The same applies to the inventory of liabilities.

Taking a physical inventory of real estate is also necessary this includes buildings and facilities and uncompleted constructions – work-in-progress. This inventory shall identify the condition of the site, reasons for non-completion of construction (work-in-progress, work stopped), whether components of these sites are damaged. Often some sites are significantly damaged and destroyed due to lack of proper attention or maintenance (e.g. minor damage of a roofing may result damage of the whole building).

Rules of inventory for public organizations is approved by the Order #605 of the Minister of Finance of Georgia dated July 23, 2010 on “approval of rules of inventory of property, requirements and liabilities of public organizations”.

5.2 Timing of Mandatory and Advisable Inventory

Inventory shall be performed on a regular basis, there are both mandatory and recommended periods of inventory.

Mandatory inventory terms are as follows:

- ✓ Annually – by the end of budget year (excluding real estate, library stocks and those assets inventory of which was performed after October 1.);
- ✓ Real estate – once in 3 years;
- ✓ Library stocks – once in 5 years;
- ✓ At the moment of lease or redemption of assets – at the moment of transfer or redemption, a physical inventory of leased/redemption asset is performed, also other cases of transfer of property in use/disposal (e.g. usufruct, lease/rent, borrowing, transfer of assets through agreement to the program implementer, etc.);
- ✓ Assets which may be out of organization during a scheduled inventory should be inventoried before they leave organization;
- ✓ During liquidation of the organization – before preparing liquidation balance;
- ✓ When legal form of budgetary organizations is changed – at the moment of change of legal form;

- ✓ In case of change of those persons assigned responsible within the organization - at the moment of their change and only for assets under their responsibility;
- ✓ Misappropriation or misuse of assets, violation of storage rules – at the moment of identification of the fact of misappropriation, misuse or violation of storage rules of the asset;
- ✓ Fire or natural disaster – after fire or natural disaster;
- ✓ In case of revaluation of assets or liabilities – at the moment of revaluation of assets and liabilities subject to revaluation.

Also, during the periods of mandatory inventory, upon decision of the head of organization, a selective or complete inventory of assets and liabilities may be performed. This is called a special interim inventory

If the assets are under the responsibility of a group, a hand over physical inventory shall be performed at the moment of change of a group leader or one of the members of the group.

Recommended dates for inventory are as follows:

- ✓ Fixed assets – by the end of budget year, but not earlier than October 1;
- ✓ Strategic stock/inventory – by the end of budget year, but not earlier than October 1;
- ✓ Raw materials and materials – minimum twice a year;
- ✓ Work-in-Process/Uncompeted production/service – by the end of budget year, not earlier than October 1;
- ✓ Finished Goods/Ready products, commodity purchased with the aim of further processing, spare parts, other inventory - at least once a year, but not earlier than October 1;
- ✓ Cash accounts and cash documents – at least once a quarter;
- ✓ Fuel - monthly;
- ✓ Financial requirements and liabilities – minimum twice a year.

5.3 Inventory Rules and Procedures

For the purpose of taking inventory an inventory commission is created on the basis of individual administrative-legal act issued by the head of the LSG. The commission is headed by the chairman.

For mandatory inventory the commission shall consist of minimum 5 members. In case sufficient number employees is not available, composition of the commission is approved depending on the maximum number of employees, but not less than 3.

If the member of inventory commission cannot participate in the inventory process due to legitimate excuse, the head of the LSG is authorized to replace him/her based on an individual administrative-legal act.

Should need arise, a qualified specialist (certified audit/expert) might be invited to participate in working process of inventory commission.

Inventory commission shall perform the following:

- ✓ Physical inventory of non-financial and financial assets, material values reflected in off balance sheet items grouped by responsible people. In cases of where the materially responsible person, it shall be stated in the Act of Inventory as a violation of current legislation and inventory shall be done according to their location;

- ✓ Defines the results of inventory together with the accounting service and other authorized services;
- ✓ Based on the results of inventory, develop recommendations for improved analytical accounting and control of assets and liabilities;
- ✓ Submit written information on surplus/deficit detected during the inventory to the management of the LSG upon completion of comparison with the accounting data;
- ✓ Signs the Act of Inventory. When commission member does not agree with the results of inventory and denies signing the Act of Inventory, he/she shall address the head of the LSG in writing (explaining the reasons) and enclose this explanatory note to the Act of Inventory.

It is unacceptable to take inventory with an incomplete composition of the inventory commission. The results of inventory that were taken in conditions of incomplete composition of the inventory commission are invalid.

Work of the inventory commission is formalized by the Act of Inventory, which is signed by all members of the inventory commission.

Inventory is performed by checking each asset physically and recording it in the physical inventory document with a description which includes its full name, purpose, number of inventory and basic technical or operational characteristics.

If the asset is missing from the accounting data or is registered incorrectly, the inventory commission shall recognize this and register in inventory description correctly.

In case of detecting unaccounted assets, the inventory commission shall investigate when and from whom the unaccounted asset was received, when and how are recorded the expenses incurred in relation to this asset in accounting-reporting of the organization and includes collected information in the Act of Inventory and marks the asset.

Unaccounted assets detected during inventory shall be valued at their receipt value (purchase, production, etc.) and depreciation shall be computed according to the receipt date and at the pre-defined rate. If it is impossible to define the value of the unaccounted asset based on the existing documentation, it is value shall be established on the basis of an expert report prepared by the invited qualified specialist upon request of the inventory commission.

Damaged assets that cannot be restored are not included in the common physical inventory. For this kind of assets there is a separate inventory list which includes information on the purchase year and the reason for the uselessness (damage, complete amortization, etc.)

Useless assets are subject to being writed off from the balance sheet and scrapped or destruction.

5.4 Filling the Inventory Reports

It is necessary that inventory reports are filled correctly when taking inventory. Inventory reports are approved by the Order #449 of the Minister or Finance of Georgia, dated December 31, 2013.

Inventory form (comparison report) is filled by the inventory commission.

Form # INV-1

Inventory
(Comparison Act)

#	Name of inventory	Registration document			Inventory number	Unit	Cost GEL	Actual quantity		As per accounting data (residual value)		Results of Inventory				NOTE
												Deficit		Surplus		
		Name	Date	Number				Q-ty	Amount GEL	Q-ty	Amount GEL	Q-ty	Amount GEL	Q-ty	Amount GEL	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17

Chairman of Commission ____________________ ____________________
Full Name Signature

Members of Commission ____________________ ____________________
Full Name Signature

____________________ ____________________
Full Name Signature

____________________ ____________________
Full Name Signature

____________________ ____________________
Full Name Signature

*To be filled in case of intangible assets

It comprises the following:

Column 2 – Full name of the asset

Columns 3, 4, 5 – They are filled in case of inventory of intangible assets and indicate the name of the document based on which the intangible asset was received, also the date and the number of the document.

Column 6 – Inventory number of the asset, if any (fixed assets and long-term low-cost assets shall have inventory numbers).

Column 7 – Measure unit (e.g. pcs, kg, etc.)

Column 8 – Primary value of the unit

Column 9, 10 – Actual quantity detected during inventory

Column 11, 12 – Quantity as per the accounting data and their value

Column 13,14,15,16 – Results of inventory, surplus/deficit

Column 17 - Note

Another report that shall be filled during inventory is the report of deviations, a document being a proof of comparison of the results of inventory with accounting data.

Deviations report as a result of Inventory #

Organization ____________________

Structural sub-division ____________________

Materially responsible person ____________________

Form # INV-1

#	Name of inventory	# of inventory	Unit	Balance Value	Results of Inventory								Surplus			
					Deficit				Surplus							
					Natural losses				Above natural losses							
					Q-ty	Amount GEL	Debit	Credit	Q-ty	Amount GEL	Debit	Credit	Q-ty	Amount GEL	Debit	Credit

Prepared by ____________________ ____________________ ____________________

Position Signature Full Name

Accountant ____________________ ____________________ ____________________

Position Signature Full Name

Results of inventory are approved by the Act of Inventory.

Head of Organization (structural sub-devision) ________________ __________________________

Signature Full Name

________ __________________ ________

Act of Inventory Results #

Organization ________________________

Materially responsible person ________________________

Commission with membership of:

(Position, Full Name)

(Position, Full Name)

(Position, Full Name)

(Position, Full Name)

(Position, Full Name)

appointed on ________________________________ based on Order # __________

(Date)

has drawn this act to certify that for the period of ____

(from-to)

inventory of ____ was performed which is

stored under responsible storage by ____

(position, full name, materially responsible person)

Based on inventory (comparison act) # ________ __________________________________

(date)

deviation act was developed and the following was determined:

Deviation Report # _________ dated _______________ developed as a result of taking inventory

is enclosed in _________ pages.

Chairman of Commission: _______________ _____________________

(Full Name) (signature)

Members of Commission: _______________ _____________________

(Full Name) (signature)

_______________ _____________________

(Full Name) (signature)

_______________ _____________________

(Full Name) (signature)

5.5 Adjustment of Differences Demonstrated as a Result of Inventory and Formalization of the Results

After taking inventory, the results shall be compared to the accounting records.

Before drafting the comparison report, the accounting department of the organization is checking accuracy of all calculations given in inventory descriptions. In case of inaccuracies in the inventory descriptions, the amendments shall be made and approved by all members of the inventory commission.

The inventory commission shall obtain written explanation for each deficit, loss of surplus also the accounts receivable validity of which is expired, from relevant responsible people, based on which the character of deficit, loss or surplus shall be defined.

Unaccounted items detected during inventory shall be valued at their receipt value (purchase, production, etc.). depreciation shall be calculated from their date of receipt and the pre-defined rates. For this purpose, relevant documentation (Agreements, Acts of Acceptance, etc.) shall be used. If it is impossible to define the value of the unaccounted asset based on the existing documentation, it is value shall be defined on the basis of the expert report prepared by the invited qualified specialist upon request of the inventory commission.

The results of the physical inventory are discussed by the management of the LSG and a special Act is drawn up as a result of this. The act shall detail reasons of deficit, loss and surplus and indicate the people responsible and guilty for that. It should also define the measures for adjustment of the differences between actual quantities and accounting data.

Differences demonstrated through inventory are adjusted the following way:

- ✓ Deficit within the pre-defined norms (if any) shall be written off against the relevant expense accounts upon decision of the manager.
    - o Deficit norms shall be defined by the competent body or the producer. (e.g. fuel evaporation, raw materials which may have dried out).
- If the deficit was above norm deficits of assets and other inventory and was caused by the fault of those materially responsible people, compensation is to be collected from them. In addition to this, within 5 days from completion of inventory, evidence collected in respect of the deficiency are transferred to law enforcement bodies upon decision of the manager of organization.

Deficit and loss of financial assets and inventory above norms shall be written off to the account of other non-operational expenses (8200), if perpetrators of the theft have not been identified and the court couldn't impose restitution on them.

Surplus of financial requirements and inventory demonstrated through the process shall be reflected in the debit of relevant account and in credit of other non-operation revenues (8100).

As to the liabilities, as a result of inventory, write off of liabilities is performed to debit of non-operation revenues and credit of the relevant liabilities account. Increase of unaccounted liabilities is reflected to debit of liabilities account and credit of other non-operation expenses (8200).

Compensation of deficit imposed upon culprits upon decision of the head of organization can be paid in cash or in form of commodity. If deficit is compensated in a commodity form, balance value won't change. In case compensation is paid in a cash form, payment shall be performed by market price based on expert report.

Final results of the inventory and minutes of meeting of the inventory commission are approved by the head of organization within 2 weeks from the date of completion of inventory.

6. Reimbursement of Business Trip Expenses

Relevance

Expenses incurred during business trip, related to the activity of the LSG are reimbursable. This chapter demonstrates authorization of such expenses and technical aspects of documentation. This is of interest of accounting as well as budgeting specialists. Knowledge of these aspects ensures planning and spending of all business-related costs in compliance with the rates defined by the legislation.

Laws and regulations discussed:

- ✓ Resolution #211 of the Government of Georgia dated April 25, 2017 on the “rules of business trip of public officials, reimbursement of business trip costs and volume and conditions of compensation.”

All payments must be traceable, uniquely identifiable and accounted for in a timely manner.

6.1. Preparation of Business Trip Related Documents

Business trip reimbursement rules are defined by the resolution #211 of Government of Georgia “On the Rules of Business Trip of Public Officials, Reimbursement of Business Trip Costs and Volume and Conditions Of Compensation” dated April 25, 2017. A business trip is a trip undertaken by an official with the purpose of execution of his/her official duties beyond the borders of his/her permanent working place on the bases of the order issued by the head of the LSG or the authorized person. Business trips abroad might be short (up to one month) or long term (more than one month). An official who is sent on a business trip shall get complete reimbursement of business trip related costs through the whole period of the trip, excluding the pre-defined exceptions.

The official shall receive business trip amounts before departure, though in case the trip is inside the borders of the country, he/she might receive business trip amount after he/she is back from the trip no later than 30 days from submission of receipts of actual expenses.

Within 60 days from the date of business trip, an official having returned from abroad shall submit to the LSG documents of actual expenses. An official having returned from internal business trip shall submit to the LSG documents of actual accommodation and travel expenses no later than 1 month after completion of trip.

In case if the official cannot submit to the organization documents proving that he/she completely spent the amount received in advance, the official is obliged to return to the organization the difference between the received advance amount and actual costs. Accountable people will not receive advance amounts for the next business trip unless all outstanding advances are cleared.

In case of fail to submit documentation of transportation costs within the borders of the country, transportation costs shall be reimbursed as per the officially minimum rates effective within the country for road or railway transport.

When being on business trip the employee maintains their position held and the commensurate salary.

6.2. Business Trip Rates

Business trip expenses are made of daily subsistence rates (per diem), transportation, accommodation and visa costs. For business trips to places that are up to 30 km distance from their regular place of work only transportation costs are reimbursed. High officials get supplement to the daily rate when on business trip abroad. During preparation of government delegation visits abroad the employees also get reimbursement of transport and communication costs, while members of delegation get reimbursement of communication costs.

Daily subsistence rate of business trip within the borders of the country is 15 GEL. Daily subsistence rates of business trips abroad are defined according to the Annex 1 to the resolution #211 of the Government of Georgia "On The Rules Of Business Trip Of Public Officials, Reimbursement Of Business Trip Costs And Volume And Conditions Of Compensation" dated April 25, 2017.

Example 6.2-1: Daily and accommodation rates for business trips abroad (extract)

		Daily rates		
Country	**Foreign Currency**	**Short term business trip**	**Short term business trip for employees of Georgian entities abroad, within the borders of the state where this entity is located.**	**Accommodation rates**
Column 1	Column 2	Column 3	Column 4	Column 5
Commonwealth of Australia	AUD	43	30	220 Canberra, 200 other areas
Austria	EUR	49	35	89
Afghanistan	USD	30	21	75
Azerbaijan	USD	35	25	125 Baku, 60 other areas
Albania	USD	48	34	120
Algeria	USD	41	29	45
USA	USD	60	43	235 New York, 180 other areas

6.3. Reimbursement of Business Trip Costs

Daily expenses are calculated according to the number of actual days spent on business trip including weekends and public holidays, as well as the day of departure and arrival.

Example 6.3-1

An employee was sent on a business trip from Tbilisi to Batumi from May 2, 2017 to May 28, 2017 for performance of official duties. On May 2, 2017 at 11:00 PM the employee left for Batumi and was back to Tbilisi on May 28, 10:00 AM.

In the given case, the number of actual days spent on business trip will be all days from May 2 to May 28, i.e. 27 days, despite the fact that 8 days out of them were weekends (6, 7, 13, 14, 20, 21, 27, 28), 3 days were public holidays (9, 12, 26) and departure and arrival days.

During long term business trip abroad, for the first 30 days the employee gets reimbursement of per diem costs as per the "rates defined for short term business trip abroad", only after that the rates defined for short term business trip for employees of Georgian entities abroad, within the borders of the state where this entity is located shall apply.

Example 6.3-2

An employee was sent to the New York, USA, on a business trip in May 2017 for 35 days. Actual days spent on business trip was 34 days.

In the given case, the employee shall get reimbursement of:

Per Diem costs = ($60 x 30) + ($43 x 4) = $1,972

Accommodation costs = $235 x 34 = $7,990

If the hosting party pays for the meal costs of the employee during the business trip abroad, then the employee will only get reimbursement of 30% of daily rate.

Example 6.3-3

An employee was sent on a business trip in Baku, Azerbaijan, in May 2017 for 28 days. Actual number of days spent on the business trip was 28 days. The hosting party covers meal costs of the employee, which is documented by the notification received from the hosting party.

In the given case, the employee shall get reimbursement of:

Per Diem = $35 x 28 x 30% = $294

Accommodation = $125 x 28 = $3,500

Transportation costs shall be reimbursed considering the cost of transportation of that specific direction/destination, but not more than the value of economy class ticket, excluding the defined exceptions. In addition to this, despite the exceptions it is prohibited to reimburse business class ticket in case the total duration of flight (including transit flights) is less than 5 hours (including reimbursement of travel costs according to the actual costs incurred). Employee who is going on a business trip shall submit to the LSG travel costs document (i.e. receipts, boarding pass) to get reimbursement of travel expenses.

For business trips within the borders of Georgia accommodation reimbursement covers no more than costs of average class hotel room, for worldwide business trips this amount is limited to the pre-defined

When the hosting party covers meal costs during business trip abroad, the official only gets 30% of per diem rate. For countrywide business trips per diem rate is issued in whole.

Business trip related short-term requirements are recorded to the natural account 1461 “Requirements Through Business Trip Within the Country” and natural account 1462 “Requirements Through Business Trip Abroad.” While business trip related short-term liabilities are recorded on natural accounts 3253 “Liabilities Through Business Trip Within the Country” and 3254 “Liabilities Through Business Trip Abroad.”

In case of advance payment of business trip amounts accounting entry shall be the following:

Debit) Natural Account 1461/1462 – Requirements Through Business Trip

Credit) Natural Account 1100-1200 – Cash resources

After submission of relevant documentation, requirement coverage shall be recorded the following way:

Debit) Natural Account 7220 – Business trip

Credit) Natural Account 1461/1462 – Requirements Through Business Trip

In case advance payment exceeds actual costs of business trip, covering of the requirement shall be recorded the following way:

Debit) Natural Account 1100-1200 – Cash resources

Credit) Natural Account 1461/1462 – Requirements Through Business Trip

In case actual costs of business trip exceed the advance payment, liability with difference amount is recognized:

Debit) Natural Account 7220 – Business trip

Credit) Natural Account 3253 - Liabilities Through Business Trip Within the Country

or

Credit) Natural Account 3254 - Liabilities Through Business Trip Abroad.

Accommodation costs and per diem reimbursement in foreign currency shall be performed in accordance with the official exchange rate of the National Bank of Georgia.

7. Temporary Disability Benefits

Relevance

This and the following chapters are of technical character. Information represented below is useful for people who make calculation of payments to employees of LSG. This chapter provides rules for calculation of benefits payable by the LSG due to temporary disability.

Aid is a social benefit issued by the LSG to the employee, to mitigate the financial difficulties caused by their disability.

Laws and regulations discussed:

- ✓ Georgian Law on Public Service
- ✓ Order #87/N of the Minister of Labor, Healthcare and Social Security of Georgia dated February 20, 2009 on „rules for issue and disbursement of benefits due to temporary disability."

7.1. Conditions for Issue and Reasons for Rejection of Temporary Disability Benefits

Benefits for temporary disability are issued in accordance with the Order #87/N of the Minister of Labor, Healthcare and Social Security of Georgia on "Rules for Issue and Disbursement of Benefits Due to Temporary Disability"

According to the above-mentioned order, benefits are issued to all the employees in case of temporary disability. Allocation, calculation and disbursement is made by the relevant budget (treasury) unit. This unit also holds responsible for correct calculation.

Submission of a document of temporary disability (bulletin) (or the copy, in case of loss of original) issued in compliance with the rules defined by the legislation represents basis for issue, calculation and disbursement of temporary disability benefit. Bulletins are compiled in a separate folder and are numbered chronologically from the beginning of the year. Each page bears the number of statement that enables accrual.

Employee/public servant might receive temporary disability benefit in case if:

A) Disability is caused by illness or mutilation;
B) Caring of disabled member of family;
C) Due to quarantine;
D) Due to prosthetic rehabilitation

Temporary disability benefits are paid issued by the the LSG for the whole period of disability starting from the date of submission of bulletin.

In case of dismissal of an employee due to liquidation of legal the LSG, organization liquidation or staff lay off /reorganization, if the bulletin is open, temporary disability benefit shall be paid till the day of lay off.

In case disability starts during vacation, benefit shall be issued for the whole period of vacation. In such a case, the use of vacation days shall be suspended proportionally with the number of days stated in the bulletin. The employee shall have those vacation days which are recognized as sick days reinstated to the leave account.

If disability starts during the period of dispute over lay off, in case of reinstatement, benefit calculation shall start from the day of reinstatement.

In case of term contracts (i.e. fixed period contracts) the employer/the LSG shall pay temporary disability benefit only within the period of contract validity.

Temporary disability benefits do not apply to:

A) People who were injured during the commitment of a criminal activity or those who intentionally damaged their health;
B) In case of non-compliance with the regime or treatment as prescribed by the doctor;
C) If temporary disability is caused by disease or damage inflicted due to non-sober condition (alcohol, narcotics or other psychoactive agents);
D) If employee was removed from their place of work in accordance with the rules defined by the law or if employee undergoes non-voluntary stationary psychiatric treatment upon the court decision or is under forensic-medical expertise examination.

7.2. Benefit Calulation and Disbursement

Basic salary of the employee is the basis of calculation of temporary disability benefit. In case of revision of the base salary during temporary disability period, benefit calculation before revision update, the calculation shall be done according to the old base; from the day of update of calculation base - according to the updated calculation base.

If the basic salary is not defined by the employment agreement, in this case temporary disability benefit calculation base will be average monthly salary of the last 3 months before the date of temporary disability.

In case of variable salary, temporary disability benefit calculation base shall be average monthly wages accrued during the last 3 months before temporary disability.

If the employee has been working at the employer for less than 3 months or the last 3 months wages have not been accrued, his/her average monthly salary shall be calculated from the average monthly salary of the other employees of similar profession and qualification working at the same employer.

Calculation of temporary disability benefit does not envisage:

A) Simultaneous financial aids, bonuses and material awards;
B) Overtimes and supplements
C) Payments received for one-time assignment that doesn’t represent a salary received for his/her basic official duties.

Total amount of temporary disability benefit is defined collectively for the month indicated in the bulletin (for each month separately) by multiplying average daily salary (basic salary) to the number of days absent within the given month.

Average daily salary (basic salary is calculated through dividing average monthly salary (basic salary) by number of working days of the month of disability (for each month separately).

Example 7.2-1 “Temporary Disability”

In October an employee was absent for 5 days due to temporary disability as per their bulletin. Basic salary of the employee is 1,000 GEL. Number of working days in October was 22 days.

$$Average\ daily\ salary = \frac{Basic\ salary}{number\ of\ working\ days} = \frac{1{,}000}{22} = 45.4$$

Total amount of temporary disability benefit = average daily salary X number of days absent due to disability = 45.45 x 5 = 227.25 GEL.

In case of working at several employers at the same time, temporary disability benefit shall be issued by each employer separately.

To obtain temporary disability benefit the employee/public servant shall submit to the employer/the LSG a proof of temporary disability (bulletin), employer/the LSG is obliged to disburse temporary disability benefit or send a written rejection notification to the employee/public servant within 10 working days.

Temporary disability benefit is not payable if proof of disability (bulletin) is not submitted to the LSG within 3 months from the date of closing the bulletin.

8. Maternity Leave Reimbursements for Pregnancy, Childbirth, Newborn Adoption and Child Care

Relevance

This chapter is of a technical character and describes how maternity leave reimbursement shall be calculated. Details are important for those calculating salaries of employees. Others may have interest just to have an idea on social benefits issued by the LSGs.

Laws and regulations discussed:

- ✓ Order #231/N of the Minister of Labor, Healthcare and Social Security of Georgia dated August 25, 2006 on approval of "rules for reimbursement of maternity leave due to pregnancy, childbirth and childcare, also newborn adoption."
- ✓ Georgian Law on Public Service

8.1. Basis for Benefits and Compensation

As per the Article 64, clause 2 of the Law on Public Service of Georgia the LSG from its budget shall issue benefit for public servant due to pregnancy and childbirth with the amount of salary of the public servant.

Salary of public servant comprises basic salary and supplements defined by the Law on Public Service.

Public servant gets supplement according to:

- ✓ Rank of the servant
- ✓ For overtimes performed upon assignment of higher rank official
- ✓ When additional functions are imposed, including night hour work, weekends/public holidays and when his/her works are performed in tough working conditions.

Allocation, calculation and disbursement of benefits and compensations for pregnancy, childbirth and child care, also newborn adoption are regulated as per the Order #231/N Of The Minister Of Labor, Healthcare And Social Security Of Georgia, dated August 25, 2006 "On Approval Of Rules For Reimbursement Of Maternity Leave Due To Pregnancy, Childbirth And Child Care, Also Newborn Adoption". As per the mentioned order, employer shall ensure calculation and its accuracy, while reimbursement is a prerogative of "Social Service Agency" (further indicated as "Agency"). As to the reimbursement of vacation, calculation and payment is ensured by the relevant public entity.

Basis for maternity leave reimbursement due to pregnancy; childbirth and child care; and newborn adoption, is a bulletin filled in with the name of employee/public servant, or in case of newborn adoption the court decision entered into force. For cases envisaged by the Georgian Law on Public Service, article 64, clause 6, (child adoption when parent actually takes care of a child) - birth certificate of a child and a notification issued by the relevant organization stating that the mother of a child has not used paid vacation for pregnancy, child birth and child care.

8.2. Vacation Reimbursement Conditions

Public servant may obtain vacation reimbursement for:

A) Pregnancy, childbirth and childcare;
B) Newborn adoption

Public servant might also obtain vacation remuneration for cases envisaged by the Georgian Law on Public Service, article 64, clause 6, (child adoption when parent actually takes care of a child).

Public servant, upon request, obtains vacation due to pregnancy and childcare – 730 calendar days, out of which 183 are reimbursable. In case of birth complications or twin birth 200 calendar days are reimbursable. The employee may distribute reimbursable vacation according to her need between pregnancy and after birth period.

Employee/public servant who adopted a child up to 1 year of age, is granted a vacation for newborn adoption upon her request for 550 calendar days from the date of childbirth, out of which 90 days are reimbursable.

For cases envisaged by the Georgian Law on Public Service, article 64, clause 6, the employee (father) is granted a vacation upon his request for childcare for 550 calendar days from the date of childbirth, out of which 90 days are reimbursable. In addition to this, employee (father) will get the vacation for childcare only in case the mother of the newborn has not used her paid vacation or the part of it.

Family members of pregnant (mother) woman are not eligible for vacation and respectively its reimbursement due to pregnancy, childbirth and child care. There is an exception in cases where the mother dies due to complications during or after birth, but the child is born alive. In such cases the father or the guardian gets the benefit.

In case employee/public servant is dismissed due to liquidation of employer/public entity, if the bulletin is open, benefit/vacation remuneration shall be paid for the whole period of vacation for pregnancy; childbirth and childcare; and newborn adoption in compliance with the Law.

Vacation for pregnancy; childbirth and childcare; and newborn adoption are not subject to reimbursement if 6 months have passed from the date of closing the bulletin or the date of court decision entry into force.

9. Disbursements Made by Entities Served by the State Treasury

Relevance

Single treasury account principle is practiced in Georgia. All payments done by the LSGs are made from the single treasury account. Accuracy and adherence to the rules is utmost important when working in the system, otherwise the problems may arise that will hamper achievement of the LSG goals and fulfillment of its obligations. This chapter describes the principle of treasury operation, i.e. how payments shall be done in compliance with the law. This information is interesting for technical as well as for administrative personnel so that all of them have proper comprehension of legislative requirements.

Laws and regulations discussed:

- ✓ Georgian Law “Budget Code”
- ✓ Georgian Organic Law “Local Self-Government Code”
- ✓ Order #424 of the Minister of Finance of Georgia dated December 31, 2014 on approval of “Rules for payments made by entities served by the state treasury.”

For the purpose of proper procurement management, there must be robust procedures which document all commitments, purchases contracts and payments due. These must ensure appropriate management of cash flow and optimal resources use. It must be noted that at any given time there may be products and services which have been ordered or received by the organization but not yet paid for. Items ordered represent a commitment of the organization. Items received but not paid represent a debt. The recording of obligations is useful for planning cash flow in an organization, though commitments fall outside the scope of a conventional accounting system

9.1 Procedures for Budgetary Payment

As per Article 16, part 2, Clause “a” of the Local Self-Government Code, its own authority of the municipality to “manage the budget resources, perform treasury financial operations and bank transactions in accordance with the Georgian Law”.

Besides, as per the article 184, part 3 of the Budget Code “Authority to allow management and operation control of the state treasury single account and other accounts, also write off of cash resources from these accounts lies with the state treasury only, except of other exceptions envisaged by the Georgian Legislation.”

Payments within the frames of allocation defined by the budget of budgetary organizations envisaged by the budget of LSG are performed through treasury electronic service system, ”etreasury.ge“.

Procedures of payment of budget resources comprise submission of information on formalized agreement to the electronic system, registration of liability document, registration of payment order, and verification of advance payment (in case of advance payment).

Adherence to the following procedures is necessary when making payments:

1. Submission of information on formalized agreement (in case the basis for payment is the agreement);
2. Registration of liability document;
3. Registration of payment order;

4. Verification of advance payment (in case of advance payment)

It is noteworthy that the term “liability” in treasury operations (payments) has different meaning from “liability” in accounting. According to accounting terms, liability is born out of a past event, coverage of which shall result in outflow of the LSG ’s resources in a form of economic benefit or service potential.

While performing treasury operations (payments), taking responsibility on payments (liability) means registration of liabilities at the state treasury in conformity with the pre-defined rules by the budget organization for those payments due within the budget year.

Quite often these two definitions are mixed up, which is a mistake.

Payment order is a request for payment submitted to the state treasury by the organization.

Verification of advance payment means approval of economic event by verification of advance payments. Thus, by advance payment the purpose of this payment is achieved which is justified by the relevant documents (Act of Acceptance, bill of lading, etc.)

9.2 Information on Agreements Signed

Information on formalized agreements shall be submitted by the organization to the state treasury within 10 working days from signature of the agreement. In case of delay in submission of information on signed agreement, registration is possible upon decision of the head of treasury service.

In line with the agreement, the organization shall fill the monthly payment schedule according to treasury codes within the budget year. In case the purchase/procurement agreement does not define schedule of payment or/and goods or/and service delivery/execution of works, the organization shall fill in the indicative schedule for payments.

Information regarding agreement on state purchase shall be filled in compliance with the Common Procurement Vocabulary approved by the State Purchasing Agency and corresponding to the methodology of downloading the agreement data from the state common procurement electronic system, or/and budget classification and economic operations financial accounting-reporting methodology.

In case the purchases made by the organization are not subject to Georgian Law on State Purchases and /or state purchase agreement is not uploaded into the system, information regarding the agreement shall be filled in state treasury electronic service system.

Payments shall be performed in compliance with the payment schedule. If amounts defined by the schedule do not coincide with the actual amounts payable, the organization shall adjust the schedule.

9.3 Document of Liability

As already mentioned above, liability is a registration of liabilities at the state treasury in conformity with the pre-defined rules by the budget organization for payments due within the budget year.

It is impossible to make payment without liability document. The purpose of registration of liability document is to reserve relevant amounts according to the plan envisaged by the budget to enable timely payment upon the fact.

A liability is recognized based on the program classification envisaged by the budget, according to the sum of gross amount of quarterly plan for each article of budget classification.

Organization creates a liability document with indication of source/origin from which the disbursement will be covered, e.g. budget sources without funds, LSG reserve fund, LSG indebtedness fund, targeted grant, etc.

There are two types of liability document: “liability document” and “quarterly application”

Basis for “liability document” might be signed purchase agreement, administrative-legal act, court decision, written application of the organization, etc.

Agreement is a basis for registration of liability document when payments are to be done on the basis of the agreement.

It is possible to recognize the liability on the basis of individual administrative-legal act of the head of the organization or the authorized person for internet purchases, increase of capital of the entities partially owned by the state, representative costs, also other similar payments, where there is a legal document recognizing the liability of payment.

Based on the written application of the organization, liability might be taken on expenses that are not covered by the requirements of the Georgian Law on State Purchases if a relevant administrative-legal act is existent, e.g. utilities costs (water, electricity), payments to budget (property tax, fees) and other costs.

The liability document makes a record on which a specific entity shall receive the payment. Since quarterly application does not include such information on recipient of amount, it is therefore possible to make payment in favor of several entities with one quarterly application.

Through the quarterly applications liabilities are taken for the following payments:

- ✓ Salary in a cash form, remuneration of freelancers;
- ✓ Business trips;
- ✓ Secret expenses envisaged by the Georgian Law on “State Secret”;
- ✓ International organizations cooperation and membership costs;
- ✓ Student’s vouchers, state educational grants and scholarships, President’s or other grants and scholarship costs;
- ✓ Payments for compensation of natural disaster damage or injuries;
- ✓ Social benefits;
- ✓ Coverage of accounts payable born out of salaries of previous years.

Liability is taken through the treasury electronic system; treasury service discusses the document in relation with the instruction requirements and verifies into the treasury information base. Incomplete documentation is returned to the organization.

It is prohibited to move the registered liability to another article or to finance the liabilities with resources allocated for another libility.

Organization is entitled to cancel the registered liability completely or partially.

Organization is eligible to make changes to the registered quarterly application.

9.4 Preparation of Payment Order

Payment of funds from budget is conducted by budgetary organisations based on a Payment Order.

The Payment Order is a request submitted by the organization to the State Treasury for payment of funds and it is created through the Treasury Electronic System.

The organization drafts the Payment Order after the occurrence of an economic event, based upon an economic event certifying document and for the purpose of requesting an amount be recognized within the registered liabilities.

Documents certifying the economic event include the following: acceptance-delivery act, waybills, reconciliation report, etc. I.e. all the documents relevant to explain the content of the source document.

Original billing document issued by the vendor is required to initiate any payment. Copies can be used only if it is duly authorized as outlined in the procurement policy. Approved payments must be executed within the time period agreed upon in contractual terms.

Source documents must include the following requisites: name of the document (form), date of creation, content of economic operation, unit of measure (if it has physical measurement unit, which can be linked to prices), quantity, price, amount, names of the parties involved in economic operation, signatures of responsible persons for properly drafting the documents, as well as other data, deriving from the content of the event and features of data processing technology.

There are frequent cases and practices of using tax invoice as a certifying document of economic event. However, according to the Tax Code, the tax invoice is a deduction document. It is also issued in case of advance payment and more importantly, the date of tax invoice issuance is not restricted in time. Accordingly, the exact date of occurrence of economic event cannot be defined (for instance, a tax invoice for services rendered on December 20, can be issued on February 20 of the next year).

“Advance payment” as the basis for a Payment Order, along with the deadline of submitting a prepayment verification document within the scope of agreement and/or relevant bank guarantee is indicated in case of advance payment.

Advance payment verification is carried out within the deadline envisaged by the Payment Order, within the amounts defined by this order. Several certification documents can be drafted for one order.

In case of failure to submit certification document within the determined deadline, the State Treasury shall suspend a new liability under the same classification article. The State Treasury provides monthly notifications to the relevant controlling authorities on non-provision of certification document on time.

Several payment orders can be drafted for one liability.

The Payment order on due payments for the purpose of procurement of goods/service/work, shall indicate CPV hierarchycal category, quantity, measure unit, unit price and total value. If the physical unit of measure is impossible to define, then, ”0” should be written down in the unit of measure.

Payments to be made for business trip costs (except for the titled “Secret”) along with the Payment Order constitute the information on payments to be made for business trips.

When executing foreign currency transactions, conversion takes place. Conversion Order shall be submitted to the Treasury on the day before transaction, according to the official exchange rate of National Bank of Georgia, at 17:00, after the official exchange rate of the following day is determined by the National Bank of Georgia. If the GEL amount indicated in payment order of conversion is within the relevant liability or relevant allocation, the payment order of conversion is sent to the National Bank for execution.

Conversion requested by the State Treasury is executed by the National Bank and the currency amount is reflected on multicurrency account of the State Treasury on the following day. The organization sends a Currency Payment Order to the State Treasury on the following day of conversion order. Conversion requirements are reflected in cash expenses of the organization with the date of conversion executed by the National Bank.

9.5 Debt Payment and Refunds Management

For treasury transactions purposes, the debt is an actual cost of the previous budgetary year, a payable amount, to be covered by current budgetary year allocation.

In order to cover the debt of previous year, the following two conditions are required: the debt shall be reflected in previous financial statements (in balance sheets) and the liability document for the indicated payment in previous years shall be registered in the system.

The organization is allowed to register liabilities in the previous year electronic system of the Treasury before the approval of financial statement, but not later than March 1 of current year.

Before introduction of liability accounting (before organizations switched to treasury principles), the generated liability was covered within financial liabilities accrued according to the organization's financial statement (balance sheet) data.

In case of return of payment within the budgetary year it was made, the amount is returned on the Treasury Code of Budget Revenues 9921 – "Return of Payment made in Current Year".

Upon returning the payment, cash expenses and the Payment Order are reduced by corresponding amount.

In case of returning the amount to the budget, the code of budgetary program, the number of Order and the article of economic classification need to be indicated in order to get the cash expenditure promptly restored by the Treasury Service.

And the payments, made in previous years, are returned on Treasury Code 3460 of Budget Revenues: "Returned budget funds unused in previous year". In this case, they are reflected in budget revenues of the year when they were returned.

10 LAW ON PUBLIC SERVICE

Relevance

The information provided in this chapter is useful for all individuals. In addition to management aspects of human resources employed in public sector, other technical issues are also reviewed. The material shall be read and studied by all individuals employed in LSGs.

Discussed laws and regulations include:

- ✓ Law of Georgia on Public Service.

10.1 Public Servant

A new law on public service has entered into force since July 1st, 2017, which defines the status of a public servant; employment and promotion conditions of a professional public servant; public service management issues; and regulates official legal relations of public servants working at the state, autonomous republic and municipal entities (institutions), as well as in legal entities of public law.

There are three types of civil servants, as follows:

- ✓ Professional public official/public servant or civil servant;
- ✓ Person employed by an administrative contract;
- ✓ Person employed by a labor agreement.

An official is a public servant, appointed on a staff position of public service for unlimited term and exercising public legal power, as his/her basic professional activity, ensuring protection of public interests and in turn, getting the corresponding remuneration and social and legal protection guarantees.

A person employed by administrative contract assists the state-political official in exercising his/her power by providing him/her with field/sectorial advices and intellectual-technical assistance and/or implementing organizational-managerial functions. These are the assistants, advisors to the state political official or the employees of his apparatus/secretariat/bureau.

The state political officials are the President of Georgia, members of the Parliament of Georgia, the Prime Minister of Georgia, other members of Georgian Government and their deputies, members of Supreme Representative Authorities of Autonomous Republics of Abkhazia and Adjara, members of governments of autonomous republics of Abkhazia and Adjara and their deputies.

A person employed by labor agreement is a civil servant, who, for providing public service, has the authority to fulfil auxiliary or non-permanent tasks for state institution based on labor agreement.

An official shall be appointed on vacant position only on the basis of competition, except for the cases of reorganization or liquidation of public institution, when the official is transferred to the relevant position with the same hierarchical rank and/or to other functionally similar position.

The official, upon his/her consent, may be transferred to the position equal to his/her current position or to a lower position in the same or other public institution, with respect to his/her competence.

There are two types of competition: closed and open competition.

The closed competition is announced on the scale of public service system and implies recruitment of the appropriate candidate out of sitting officials, from the officials enrolled in the reserve and persons employed by labor agreement. In addition to this, a person employed by labor agreement has the right to participate in a closed competition if he/she has been working in the system of public service for not less than 1 year.

The closed competition is announced for appointment on the position of first, second or third rank official, and the open competition is announced for appointment on the position of the fourth rank official.

The open competition may be conducted for appointment on the position of first, second or third rank officials, if the appropriate candidate was not recruited on the basis of closed competition, or there is a reasonable recommendation by Civil Service Bureau, that considering additional qualification requirements defined for the relevant vacant position, a suitable candidate cannot be recruited based on closed competition.

The new law has introduced the following hierarchical ranking of positions:

- ✓ First rank – high management level;
- ✓ Second rank – middle management level;
- ✓ Third rank – senior specialist level
- ✓ Fourth rank – junior specialist level

The position of the head of primary structural unit of public institution corresponds to the first rank, i.e. high management level.

The position of the deputy head of primary structural unit of public institution and the head of the secondary structural unit of public institution corersponds to the second rank, i.e. middle management level.

The first category senior specialist, the second category senior specialist and the third category senior specialist of public institution correspond to the third rank, i.e. senior specialist level.

The first category junior speciliast, second category junior specialist and third category junior specialist of public institution correspond to the fourth rank, i. e. junior specialist level.

An official can be granted with a class of public official based on assessment results. The total number of classes of public officials is 12.

The class assigned to the civil servant is constantly retained and at the same time he/she is paid a salary supplement.

The official's labor remuneration is comprised of official salary assigned to the position and salary supplement.

Amount of salaries for positions assigned to each hierarchical rank of officials is determined by the law of Georgia "On Labor Remuneration in Public Institution".

Salary supplement is given to the official:

- ✓ considering the class of the official;
- ✓ according to overtime work performed by instruction of the superior official
- ✓ During assignment of additional functions, including at nighttime, at weekends/holidays and due to hard working conditions.

The new law on public service does not envisage the forms of supplementary compensation for officials, such as bonus awards, however, there are following forms of incentives based on official's performance results:

- ✓ Announcement of appreciation;
- ✓ Awarding with money-prize;
- ✓ Giving a valuable non-monetary gift.

The performance of an official is assessed once a year according to the functions, competences, skills, conduct manners of the official and/or goals and objectives (components) achieved by him. Evaluation is performed through examination of documentary materials and an interview with the official.

In case of cancellation of the decision on official's dismissal by a superior body or court, the public institution is obliged to immediately reinstate the official on the same position, and in the absence of such a position, on equal position in the system of the same public institution. If the official cannot be reinstated in public system of the institution, then the institution immediately addresses the Civil Service Bureau with the request to find equal position in other public institution. Reinstatement on equal position in other public institution is permissible with the mutual consent of the unlawfully dismissed official and of the relevant public institution.

The re-employed official is given a labor remuneration for enforced idleness from the date of dismissal till the date of reinstatement. If the re-employment of the official is impossible, he/she is enrolled in the reserve of civil servants and is given a labor remuneration for enforced idleness, as well as the compensation with the total amount of basic official salary for 6 months.

If the official is dismissed due to staff reduction as a result of reorganization, liquidation and/or merger of the organisation with the other public institution, and his/her employment is impossible on equal position in the same or other public institution, he/she is enrolled in the reserve of civil servants upon his/her consent and is given a compensation with the amount of official salary for three months.

10.2 Leave of the Official, Other Forms of Suspension of Official Duties and Their Remuneration

The official shall receive a paid leave for 24 working days, he/she shall have the right to use these days piece by piece. In addition to the paid leave, the official can enjoy unpaid leave for no more than 1 year, if it does not contradict the interests of public institution.

The official shall be entitled to request a leave after 11 months of his/her employment. With the consent of an authorized person, the official may be given a leave before expiry of this term. From the second year of appointment, the official will be given a leave at any time of the working year.

The official is also entitled to use unused paid leave in the next calendar year. In this case, the leave periodicity shall be agreed with the head of public institution.

The official also receives a paid leave for participation in a mandatory professional development program with the duration of this program. The official is also entitled to enjoy paid leave not more than for three months and unpaid leave not more than one year for participation in professional development program outside the civil service system.

The official shall be granted pregnancy, childbirth and childcare leave with the amount of 730 calendar days upon her request. Out of these, 183 calendar days are paid, and in case of childbearing complications or twins – 200 calendar days are paid.

The official, who has adopted a child under the age of 1 year, shall be granted leave on the basis of newborn adoption with the amount of 550 calendar days from the childbirth. Out of these days, 90 calendar days are paid.

Also, a parent, who actually takes care of a child, can enjoy a childcare leave. In the mentioned case, the official is granted a leave with the amount of 550 calendar days after the childbirth and 90 calendar days are paid, only if the mother of a newborn had not enjoyed the leave provided by this article.

Leave for pregnancy, childbirth and childcare will be issued from the budget of the relevant public institution, in the amount of labor remuneration of the official.

Suspension of work relations of the official means his/her temporary exemption from performing official duties.

The suspension of official authority of a civil servant is based on the following:

- ✓ leave of a civil servant
- ✓ temporary disability of a civil servant;
- ✓ if a relevant decision is made during disciplinary proceedings
- ✓ In case of civil servant’s nomination in elections
- ✓ During recruitment of a civil servant to a military service or alternative labor service, military reserve service or mobilization.
- ✓ during detention or administrative imprisonment of a civil servant according to the rules established by legislation
- ✓ In othe cases of temporary dismissal of a civil servant according to legislation or on its basis.

During suspension of official authority, a civil servant retains labor remuneration over a suspension period. Except for civil servant’s nomination in elections and recruitment to a military service or working in alternative labor service, reserve military service and in case of mobilization.

10. 3 Assigning Temporary Functions to a Civil Servant

Deriving from the interests of public institution and/or health condition of a civil servant, he/she may be assigned with functions, not included in his/her duties.

Temporary functions shall be assigned by the head or a designated person of public institution and a relevant administrative-legal act shall be issued for this occasion.

A civil servant may temporarily be assigned with additional functions and at the same time, he/she can be performing his/her basic functions, or he/she may be assigned with other functions and he/she may be exempt from performing his/her basic functions.

Assignment of other functions to an official (when at the same time, the person is exempt from his/her basic functions) is allowed based on the interests of the institution operating in public service system.

The total duration of performing additional functions shall not exceed 3 months.

Duration of performance of other functions in the system of public service shall not exceed 3 months, except the cases envisaged by the legislation.

Temporary functions can be assigned to a civil servant for more than 1-month period only upon his/her request.

Unreasonable decline by a civil servant to perform temporary functions for less than 1-month period may become the basis for his/her disciplinary responsibility.

It is impermissible to assign a civil servant with temporary functions that are not relevant to his/her competence.

During assignment of additional functions, a civil servant is granted with a salary supplement.

11. TAX CODE

Relevance

Everyone is responsible to adhere to the Tax Code Requirements. This chapter reviews comprehensive information with regards to different types of taxes, starting from income tax and ending with a property tax. Some information may be regarded as solely an accounting topic, however the knowledge of it is valuable for others as well. Elected state officials and budgeting specialists should know the structure and methodology of taxation, especially of taxes, which represent local taxes – a property tax.

Reviewed laws and regulations include:

- ✓ Tax Code of Georgia

11.1 Income Tax

According to the Tax Code of Georgia, a person is obliged to pay general – state and local taxes.

An income tax is a general - state tax and its payers are the following entities:

a) Resident physical person;

b) Non-resident physical person, receiving income from the source existing in Georgia.

The object of taxation by income tax of resident physical person is a taxable income, defined as the difference between total income received during a calendar year and deductions for the same period envisaged by the Tax Code.

Taxable income of a physical person is taxed by 20%, and the income receieved by a physical person as a result of renting a residential area to an organization, legal entity or physical person for residential purposes and who does not perform deductions from this income, is taxed by - 5%.

Total income of the resident consists of sources exisiting in Georgia and incomes received abroad, where as the total income of nonresident consists of – revenues received from sources existing in Georgia.

Total income includes income received in any form and/or as a result of any activity:

a) income received as wages

b) income received from economic activities, not related to hired work;

c) other income, not related to hired work and economic activities

In addition to this, the following activities are not recorded in the total income:

- ✓ transfer of goods and/or rending the service free of charge to the state and/or LSG;
- ✓ reimbursement of paid costs to a member of city council, who is not the official of the city council, based on the ordinance of the city council, envisaged by paragraph 3, article 41 of the “Code of Local Self-Governance” of the Organic Law of Georgia, except for compensation of costs paid to a member of Tbilisi city council.

Any remuneration or benefit receieved by a physical person as a result of contracted work, including the revenue received from previous workplace such as a pension or in any other form or the income received from future workplace is attributed to the income received as a salary.

The below indicated amount is considered to be a value of benefit, which is reduced by the amount paid to an employee by an employer upon receiving this benefit:

A) When receiving any type of automobile for personal use - 0,1% of balance value of this automobile at the beginning of corresponding tax year for each day of private use of this automobile by an employee;
B) When issuing a loan to the employee by an employer with the interest rate lower than the interest rate determined by the Minister of Finance of Georgia - the amount corresponding to the payable interest according to the interest rate determined by the Minister of Finance of Georgia (Annual interest rate determined by the Minister of Finance of Georgia amounts to 20% according to the Order #34 28.01.2011);
C) Market price of goods/services – when they are delivered or transferred without compensation by an employer to an employee;
D) Annual market price of leasing rent (proportional to the corresponding period) – when employer transfers the residence to the employee for use.
E) The value of assistance provided by an employer for getting education – when the employer provides assistance to the employee or the persons supported by him/her to get education (regardless of training program directly related to performance of duties of the employee);
F) Reimbursement amount – when the employer compensates costs to the employee.
G) When the employer forgives the debt or liability to an employee - the amount of debt or liability, except for the case, when expenses to be incurred for measures envisaged by Georgian legislation for enforced payment of cash requirement exceeds the amount of cash requirement.
H) The volume of insurance premium or other amount paid by an employer – when paying an insurance as a bonus or other money to an employee in case of life and health insurance or according to pension insurance agreement;
I) In other cases – according to the market price of benefit.

Income received as a salary does not include the following:

A) Reimbursement of business trip costs paid to an employee within the norms determined by the Minister of Finance of Georgia
B) Reimbursement of representative costs
C) Organized transportation of an employee from residence place to a workplace or from workplace to a residence place by an employer, if it cannot be made by means of public transport or if the travel requires unreasonable costs and/or unreasonable expenditure of time from the employee.

For accounting purposes income tax is accrued at the moment of reimbursement:

Debit) Natural Account 3250 – “Liabilities related to employees and scholars”

Credit) Natural Account 3243 - payable income tax

Income tax, transferred to the budget, is posted as follows:

Debit) Natural Account 3243 - payable income tax

Credit) Natural Account 1100-1200 – cash funds

Example 11.1-1 “Employer delivered goods to the employee”

The employer delivered goods to the employee with a market value of 118 GEL including VAT. For these goods the employee pays only 50 GEL to the employer.

Under these conditions, the amount of the revenue received by the employee as a salary is 68 GEL (118-50).

Example 11.1-2 “Employer pays monthly insurance”

The employer pays monthly insurance fee with the amount of 100 GEL based on health insurance agreement, according to which the insured and beneficiary is the employee. The employee does not pay anything to the employer for this benefit.

Under these circumstances, monthly amount of income received by the employee as a salary is 125 GEL (100 GEL insurance, 25 GEL income tax).

Example 11.1-3 “The employer issued an interest-free loan”

On April 1st, 2011, the employer issued an interest-free loan with the amount of 1,500 GEL to the employee with the term of 8 months. The employee repaid the loan completely on November 30, 2011.

*In this case, considering that annual interest rate determined by the Minister of Finance of Georgia is 20%, the amount of income received by the employee as a salary is 25 Gel (1,500*20%/12).*

11.2 Resident and Nonresident Entities

A resident entity can be either a resident physical entity or resident legal entity (Georgian enterprise or Georgian organization).

A physical entity, who actually is on the territory of Georgia for 183 days or more during any period of continuous 12 calendar months, which ends in this tax year, or a physicial entity, who, over this tax year was abroad performing the state service of Georgia, is considered to be the resident of Georgia during the whole current tax year.

An enterprise, the activity and/or management place of which is located in Georgia is considered as an enterprise of Georgia. The place of activity is the state registration place of the enterprise, and in the absence of such - legal address of the enterprise, indicated in founding documents of the enterprise (charter, agreement, provision) is deemed to be the state registration place of the enterprise. While the place of management of the enterprise can either be considered to be the physical location where actual management of the enterprise take place, or the place where according to founding documents of the enterprise (charter, agreement, provision), the directorate (other body of management) of the enterprise carries out management function,.

The place of activity and the place of management of the organization are determined by the rule set by the Tax Code.

The income received by a nonresident from a source existing in Georgia, which does not belong to the non-resident's permanent establishment in Georgia being on tax registration, is taxed without deductions at the source/origin of payment by the following rates:

- ✓ Dividends - 5%;
- ✓ Interests – 5%;
- ✓ Royalty – 5%;
- ✓ The amounts for international telecommunication services and transportation services of international shipping paid by an enterprise, organization and/or entrepreneurial physical entity - 10%
- ✓ lease service fee paid to a physical entity – in case of leasing a residential area to an organization, legal entity or physical entity for residential purposes - 5%;
- ✓ other payments which, according to this Code are considered as income received from entity existing in Georgia – 10%
- ✓ Income received as a salary – 20%.
- ✓ Interests, roalty and other payments received by an entity registered in a country with preferential taxation, are taxed by 15% without deductions at the sourceof payment. Countries with preferential taxation are defined by resolution N 615, December 29, 2016, of the Government of Georgia.

Example 11.2-1 "A non-resident company provided consultation services"

A non-resident company, which is not registered in the country with preferential taxation, has provided consultation services to a Georgian enterprise, with the value of 30,000 GEL. The service was rendered in May of 2017, and the remuneration amount was paid in June of 2017.

The Georgian enterprise should withhold 3,000 GEL (30,000 X 10%) from the remuneration amount paid to nonresident company and transfer it to the budget in June.

Example 11.2-2

A company, registered offshore, has provided services to a Georgian enterprise – developing a project of an exhibition complex to be constructed in Georgia, with the value of 50,000 GEL.

The Georgian enterprise should withhold 7,500 GEL (50,000 X 15%) from the service remuneration amount paid to the company registered in offshore and transfer to the budget.

The service rendered by a nonresident entity (except for a Georgian citizen physical entity) or nonresident enterprise to a tax agent on the territory of Georgia is subject to reverse charge by VAT. For reverse charging purposes, any taxpayer resident (except for a non-entrepreneurial physical entity and the enterprise of free industrial zone) and a permanent establishment of a nonresident is considered to be a tax agent. The tax agent charges VAT at the rate of 18% on the amount to be transferred for the service. In addition, the delivery of goods or provision of service, which is exempt from VAT, is not subject to VAT reverse charge.

Example 11.2-3

A resident legal entity registered as a VAT taxpayer has ordered a foreign company, which does not have a permanent establishment in Georgia, to conduct a certain type of marketing research of Georgian market based on the agreement. The value of the service amounts to 15,000 GEL. The service was performed in May.

The resident legal entity should charge VAT on the amount to be paid for a rendered service and 2,700 GEL (15,000 GEL X 18%) shall be reflected in the accounting of May (within the accounting month of service delivery).

Example 11.2-4

An LSG has ordered a British company, which does not have a permanent establishment in Georgia, to develop a project for the head office based on the agreement. The service value was determined to be 20,000 GEL. The British company delivered the abovementioned project via internet in June of 2017.

The resident legal entity (the LSG) should charge VAT on the amount payable for the service rendered by the foreign company and 3,600 GEL (20,000GEL X 18%) shall be reflected in accounting of June.

11.3 Withholding a Tax at the Source of Payment

A tax agent, which is a legal entity, enterprise/organization or a enterprenourial physical entity, is required to withhold a tax at the source of payment, in particular:

A) the entity, which pays a salary to an employee
B) the entity, which pays a pension to a person, except for the pension, issued by state social security system.
C) the entity, which pays specific taxes to a nonresident;
D) the enterprise/organization or an entrepreneurial physical entity, which compensates the value of rendered service to the physical entity, not having a taxpayer's certificate;
E) the entity which pays a scholarship to a person, except of the state scholarship;
F) a resident enterprise, which pays a dividend to a person, in addition to this, the dividends paid to the state are not taxed at the source of payment;
G) the entity, which pays the interest to a person, in addition to this, interests paid to the state are not taxed at the sourceof payment;

H) the entity, which pays a royalty to a physical entity, in addition to this, royalty paid to the state is not taxed at the sourceof payment;

I) the entity, which transfers a property free of charge to a physical entity, not having a taxpayer's certificate, except of free transfer of property with the value up to 1,000 GEL by this entity to the same physical entity over the tax year.

The responsibility for withholding a tax at the sourceof payment and for its transfer to the budget lies with the entity paying remuneration/benefit. In case of failure to withhold the tax amount, the entity paying remuneration/benefit is responsible to transfer the tax amount, which was not withheld according to actually paid remuneration and the sanctions related to it, to the budget. The entity, withholding the tax at the source of payment, is responsible:

- ✓ to transfer the tax to the budget upon payment of the amount to the person and in case of nonmonetary form of payment – on the last day of the corresponding month.
- ✓ upon salary payment, to give a certificate to the physical entity receiving the income upon his request, indicating the name and surname of this person, income amount and type, as well as the withheld amount (if the tax was withheld).
- ✓ to submit a certificate to the tax authority indicating the registration number, surname and name, address of the place of residence, total amount of income for a reporting period and the total amount of withheld tax of the entity receiving the income not later than 15th of the month following the month when the tax was withheld and to hand over the certificate to the person receiving the income upon his/her request.

Example 11.3-1

An organization remunerates the value of goods/service (costs of usage of mobile phone – 100 GEL, utilities – 200 GEL, travelling costs, not related to business trips -500 GEL, costs for meal -100 GEL, fuel costs – 300 GEL) as well as the amount of fine, penalty of 400 GEL to an employee.

*The organization should attribute the abovementioned amounts to the benefit of the employees and accordingly they should be taxed by income tax. The income tax amounts to 320 GEL ((100 + 200 + 500 + 100 +300 +400)*20% = 320).*

11.4 Value Added Tax

The following entities are considered to be value added tax–(VAT) payers:

A) an entity registered as a VAT payer

B) an entity which is obliged to be registered in the registry as a VAT taxpayer;

C) an entity which imports or temporarily brings goods in Georgia, however without an obligation of registration for this import or temporary importation.

D) nonresident (except for the physical entity being a Georgian citizen), providing service without registration as a VAT taxpayer in Georgia and without permanent establishment of a nonresident being registered at taxpayer's office of Georgia, only for this service and is subject to reverse charge.

E) an entity, which makes a transfer of ordered item (goods) to the ownership of a creditor within the measures of ensuring fulfilment of contractual obligations and is subject to reverse charge without obligation of registration only for this operation;
F) an entity, for which goods are sold within the tax debt enforcement measures or for purposes of other monetary debt payment enforcement (except for criminal or administrative sanctions) by means of auction, direct sale or other rules, without obligation of registration only for this operation;
G) an entity, whose custodial property is sold by a specific rule defined by the Georgian legislation on “insolvency proceedings” without obligation of registration only for this operation.

For an entity conducting economic activity, the total amount of VAT taxable transactions of which, carried out during any continuous 12 calendar months, exceeds 100,000 GEL VAT taxable transactions, is obliged to address tax authorities for registration no later than 2 working days after the day of exceeding 100,000 GEL VAT taxable transactions. The entity is considered as a VAT taxpayer from the moment of conducting that taxable operation (including this operation), according to which the total amount of operation exceeds 100,000GEL.

The entity can as well be registered as a VAT taxpayer voluntarily. It is considered to be a VAT taxpayer from the day of addressing to the tax authority, but not later than the date defined for obligatory registration.

Example 11.4-1 “VAT taxable operations”

LTD “A” was registered on March 1st, 2016. In the same month, it conducted VAT taxable operations with the value of 10,000 GEL. By March 1st of 2017, the VAT taxable operations amounted to 95,000 GEL. From March 1st of 2017 till April 1st of 2017, “A” has sold goods with a value of 9,000 GEL. The sale of these goods is a VAT taxable operation.

An obligation for registering as a VAT taxpayer is not generated by LTD “A”, because after its foundation, during not a single period of continuous 12 calendar months, the VAT taxable operations did not exceed 100,000 GEL. As already mentioned above, from March 1st of 2016 till March 1st of 2017 the sum of VAT taxable operations amounted to 95,000GEL, and from April 1st of 2016 till April 1st of 2017 – 94,000 GEL (95,000+9,000-10,000).

Example 11.4-2

A non-enterprenurial (noncommercial) legal entity conducts activites in accordance with the requirements of Georgian legislation "On Grants". It is granted with the status of a charitable organization. It implements educational, science-research, healthcare, cultural, sports, ecological and social projects through the funds (Grants) obtained from donors. As well as financing the programs of state and public significance, the non-entrepreneurial (non-commercial) legal entity constructs schools, theatres, stadiums and hospitals with its own resources, as well as other facilities of state and public importance. After completion of construction, the relevant commission (LSG) takes them into commission and registers the asset in public registry. Only after these processes, buildings and facilities and other movable property is transfered to charitable organizations free of charge, for further charitable activities.

Free of charge transfer of constructed buildings and facilities to charitable organizations by the non-entrepreneurial (non-commercial) legal entity is a charitable, not an economic activity and shall not be considered when determining an obligation of mandatory registration as a VAT taxpayer.

VAT taxable transactions are the following:

A) delivery of goods and/or rendering a service within economic activity on the territory of Georgia, when the taxable transaction amount is determined according to the compensation amount received or to be received by a VAT tax payer without VAT and/ or fine and the moment of goods delivery or service provision is considered to be the time of conducting the taxable transaction, but:
   - ✓ not later than the moment of submission of remuneration request (invoice) for the delivered goods or rendered services by the supplier, except for continuous delivery of goods/services and receipt of compensation amount/part of amount for goods/service to be delivered in advance;
   - ✓ not later than the last day of each reporting period, if the goods (with guaranteed capacity, electricity or termal energy, gas or water) or services are provided regularly or continously.
   - ✓ not later than the moment of payment of compensation amount/part of amount for the goods/services to be delivered, if the amount is paid before delivery of goods/provision of services, except for regular or continous supply of goods/services.

B) use of goods/services purchased with VAT for noneconomic activity, (except for delivery of goods/rendering of service free of charge to the state and/or local self-governance by a legal entity of public law), if the tax payer has received a VAT deduction for these goods/services, when the amount of taxable transaction is defined by the market price of goods/service (including taxes, fees and other duties) without VAT and the moment of commencement of use of the goods/services is considered to be the time of execution of taxable transaction;

C) if VAT tax payer's registration is cancelled, the balance of goods, for which the payer has received a deduction, when the taxable transaction amount is determined by the balance of goods existing on the day of cancellation of registration, for which the tax payer had receieved a deduction and the day before cancelation enters into force is considered to be the time of execution of taxable transaction.

D) use of buildings and facilities of own production as a fixed asset, when the amount of taxable transaction is defined by the value of the assets, including their purchase, production, construction, installation and setup costs (expanditures) as well as other costs (expanditures) which increase the value of the assets and the moment of commissioning of the assets is considered to be the time of execution of a taxable transaction.

E) receipt of service or goods for individual ownership in turn of shares from enterprise and/or a partnership (in this case, withdrawal and/or registration of property is considered as delivery of property by the partnership), when the amount of taxable transaction is determined by the market price of goods/services (including taxes, fees and other duties) excluding VAT and the moment of receipt of goods/service into individual ownership is considered as the time of execution of a taxable transaction.

The amount of taxable transaction is defined by the market price of goods/services (including taxes, fees and other duties) excluding VAT:

A) a VAT tax payer receives or has the right to receive goods/service as the result of a taxable transaction;
B) in cases of goods/service delivery between the interdependent entitites;
C) in case of goods/service delivery to employees;
D) in case of goods/service delivery without reimbursement.

Example 11.4-3

*An organization has paid a telecommunication company the price of internet service for 3 months (March, April and May of 2017) 180 GEL (= 60 GEL * 3) in advance, on February 15, 2017.*

*In the given case, a new regulation on VAT taxation of advance payments, despite the advance payment made in February 2017, does not cause any changes in time during the taxable transaction, as the internet service provision is considered a regular and continuous service supply. Accordingly, the telecommunication company will declare the charged VAT in March (the period of service provision) VAT - 9.15 GEL (= 60 * 18/118 GEL), April – 9.15 GEL (= 60*18/118 GEL), May – 9.15 GEL (= 60*18/118 GEL).*

Example 11.4-4

An organization ordered to a company consultancy service at a cost of 17,000 GEL (incl. VAT) on March 19, 2017. On March 19, 2017 the organization paid an advance of 7,000 GEL to the company. The remaining part of service cost (10,000 GEL) was paid on June 9, 2017, while service was provided on May 30, 2017.

*The company shall declare part of VAT charged on advance payment with the amount of 1,067.80 GEL (= 7,000 * 18/ 118 GEL) in declaration of March 2017 (accounting period of advance payment receipt). The same month the company will issue a tax invoice (7,000 GEL) for the organization (the organization is entitled for VAT deduction the same month of March on the basis of this tax invoice). The company shall declare VAT amount charged on the remaining part of taxable operation (10,000 GEL) – 1,525.42 GEL (10,000*18/118) in May 2017 declaration (which is the accounting period of service delivery). The same month (May) the company shall issue a tax invoice (for 17,000 GEL) for the organization. In addition to this, the company is entitled to reflect service provision tax invoice data together with data of tax invoice issued for advance payment amount of the same service in annex of VAT declaration of May and reduce VAT amount charged according to the tax invoice. (Based on this tax invoice the organization is entitled to deduct VAT only with the amount of 1,525.42 GEL (10,000*18/118) in May).*

For accounting purposes VAT paid for procurement of goods/services/works is recorded to the natural account 1356 – “Paid VAT”, while VAT payable for realization of goods, works and services as a result of economic operation, also VAT payable for taxable import of goods is recorded at the natural account 3242 “Payable VAT”.

11.5 Property Tax

Property Tax is a local tax determined by the tax code. Authority to impose property tax (within the limited rates) lies with the LSG representative bodies (changes in payment conditions or cancellation of imposed tax).

For the purpose of property tax, the word “Property” comprises taxable property and land. Location of taxable property is a place where the real estate is actually located; Location of the movable property is a place where it is registered in accordance with the Georgian legislative requirements. If registration place of movable property does not exist, location of taxable property is considered a place where the movable property is actually located.

Property tax applies to:

A) Resident enterprise/organization – for assets accounted on its balance as fixed assets or/and investment property, uninstalled equipment, uncompleted construction, also for lease property;
B) Nonresident enterprise – for the property located at the territory of Georgia and defined by the first part of this article (inter alia, property located at the territory of Georgia and transferred on the basis of lease, rent, usufruct or any similar type of agreement);
C) Physical entity:
    - ✓ Property owned by him/her (inter alia, uncompleted construction, buildings and facilities or their parts), yachts (boats), helicopters, airplanes and passenger vehicles defined by article 8703 of the National Commodity Range of Foreign Economic Activity.
    - ✓ Property received from non-resident through lease;

- ✓ In case of performance of economic operation, for fixed assets accounted on its balance, uninstalled equipment, also the property leased by it.

For enterprise/organization annual rate of property tax is defined by no more than 1% of value of the taxable property. Value of taxable property is an average annual balance sheet residual value (which is an average of the values of assets in the beginning and by the end of the year), increase of which is allowed only in relation of real estate for the cases enlisted below:

A) Assets received before Y2000 – 3 times;
B) Assets received from Y2000 to Y2004 – 2 times;
C) Assets received in Y2004 – 1.5 times;
D) For those assets information on receipt of which is not available – with the rate defined by clause A) of this part.

Increase of value defined by sub-clauses A-D is not applicable to:

A) Enterprise which performs accounting of its balance sheet real estate with the use of revaluation method and possesses financial reports audited by the people defined by the ordinance of Government of Georgia.
B) State enterprises defined by the Government of Georgia

Example 11.5-1

As of January 1st of the reporting year, an entity has on balance buildings and facilities with total value of 50,000 GEL purchased in 2004. In the beginning of 2016 net balance value of the building was 17,500 GEL, by the end of 2016 it amounted to 15,000 GEL.

*In the given case, average balance sheet residual value amounts to 16,250 GEL ((17,500+15,000)/2). In this case tax payer is obliged to increase average annual balance sheet value (16,250 GEL) of assets purchased in 2004 by 1.5 times to define the volume of property tax, thus property tax for this particular building shall be calculated from 24,375 GEL, which is 24,375*1%=243.75 GEL.*

For enterprise/organization, except of leasing company, annual rate of property tax, for taxable property transferred by leasing, is defined by no more than 1% of average annual balance sheet residual value of the taxable property (which is an average of the values of assets in the beginning and by the end of the year). For the purposes of this part, balance value of leased taxable property is the value of the property at the moment of lease; for every next year, the value is considered to be balance sheet residual value that the property would have had in case of non-lease.

For leasing company annual tax for leased taxable property for the whole period of lease shall be defined with no more than 0.6% of the primary balance value by the moment of first lease of the taxable property.

Tax authority is entitled to define the value of taxable property of taxpayer with the market value during tax audit. **If market value of the taxable property exceeds its balance value:**

A) The entity shall be charged with basic amount of property tax on the difference value of the taxable property. Besides, it will be charged with fine on the mentioned amount starting from the 30th day from reception of payment order and the mentioned difference shall not be considered as tax reduction;
B) The entity is obliged to use the market value for the taxable property for the next 3 reporting years.

Annual rate of taxable property tax is differentiated for physical entity, depending on the revenue of family of the taxpayer during the tax year and is the following:

A) Families with revenue up to 100,000 GEL – not less than 0.05% and no more than 0.2% of market value of taxable property by the end of tax period.
B) Families with revenue of 100,000 GEL and more - not less than 0.8% and no more than 1% of market value of taxable property by the end of tax period.

Revenues of nonresident physical entity being a citizen of Georgia are considered revenues received from the source located in Georgia.

Payment liability on taxable property is defined according to the rate valid by December 31 of tax year.

An entity is a land property taxpayer as of April 1 of the tax year:

A) For the land in its ownership
B) For the land owned by the state, possessed or used by the entity;
C) For the land owned or/and used by the entity, which is registered on the name of passed away person, except of the cases when land is used based on lease, rent, usufruct or any other similar agreement.

For agricultural land property tax rate is calculated the following way:

A) Government of Georgia determines an annual base rate in GEL per hectare:
    i. For meadow and grazing – according to the territorial units, from 5 to 20 GEL within the limit values;
    ii. Arable and homestead - according to the territorial units, from 50 to 100 GEL within the limit values;
    iii. Use of forest lands for agricultural activities – for relevant category of land of items A.i. and A.ii. within the limit values;
B) Tax rate is defined upon decision of LSG representative unit. The tax rate shall not exceed 150% of annual base rates determined by the Government of Georgia and represented in sub-clauses A.i., A.ii. and A.ii. of this part.

Property tax rates of non-agricultural land for specific land plot is calculated according to the location, in the following manner:

A) Tax base rate is determined as 0.24 GEL for 1 m2 annually;
B) Upon decision of LSG representative body, the relevant base rate is multiplied by the territorial coefficient. Besides, territorial coefficient shall not be more than 1.5.

Land allotted on the basis of relevant license for use of natural resource is taxed by no more than 3 GEL per 1 hectare.

Tax liability for land is defined as per the rates valid by April 1 of the tax year.

Government of Georgia defines the list of necessary information to be submitted to the tax authority by the National Agency of Public Registry, other registering bodies and LSGs for the purposes of property taxation and the rule of submission of that information.

Tax period for property tax is a calendar year.

Enterprise/organization submits property tax declaration to the relevant tax authority no later than April 1 of the calendar year and pays property tax within the same period. In declaration data on taxable property is filled according to the previous tax year and data on taxable land – according to the current tax year.

In tax declaration calculation of total amount of tax liability is performed in even GEL, consequently tax liability up to 1 GEL is considered as zero.

Example 11.5-2

As of January 1st of reporting year, the enterprise balance demonstrates fixed assets with total value of 50,000 GEL (residual value); uninstalled equipment with total cost of 5,000 GEL; and uncompleted capital investment with total value of 10,000 GEL. While as of December 31 of reporting year - the same assets with total values of 55,000 GEL, 4,000 GEL and 3,000 GEL.

In given case, by the beginning of the year value of taxable property amounts to (50,000+5,000+10,000) 65,000 GEL, while by the end of the year it makes up (55,000+4,000+3,000) 62,000 GEL. Average annual balance value is [(65,000+62,000)/2] = 63,500 GEL.

The following entities are considered as organizations: Non Entrepreneurial (Non Commercial) Legal Entities, Social or Religious organizations (unions), Georgian branches of organizations created according to the legislation of foreign country, budget organizations, legal entities of public law, corporations, institutions, international organizations, embassies, consulates, representations, foreign non entrepreneurial organizations.

If the organization performs economic activity, part of its property and activity, directly related with its economic activity, is regarded as a property and activity of the enterprise. In those parts, where such separation is not available, basis for calculation of value of property and activity related to economic activity of the organization is relative share of revenues received through the economic activity in total revenues received by the organization.

Example 11.5-3

Out of the building owned by the organization with total area of 2,000 m2 and balance value of 100,000 GEL, the organization has leased, i.e. used for economic activity, part of it with area of 500 m2.

In given case, cost of taxable property (building) is [(500/2,000)X100,000] = 25,000 GEL.

Example 11.5-4

Balance value of property owned by Legal Entity of Public Law is 100,000 GEL. Revenue of LEPL amounted to 200,000 GEL during tax year, inter alia, funding in a form of budget allocation made up 150,000 GEL, while revenue from economic operations, e.g. delivery of service, made up 50,000 GEL.

In given case, volume of taxable property is [(50,000/ 200,000) X 100] = 25%, [(100,000 X 25%)] 25,000 GEL.

Enterprise/organization is paying property tax as a current payment, with the amount of annual tax of previous tax year, not tater than 15th of June of tax year, while land property tax is payable not later than 15th of November of calendar year.

If taxpayer enterprise/organization has been existing for incomplete calendar year, it will make property tax payment proportionally with this period.

Example 11.5-5

An enterprise was established on April 15, 2015 and purchased fixed asset (building) at a price of 200,000 GEL. In Y2015 average annual balance value subject to property taxation amounts to (200,000/2) 100,000 GEL. The same year according to the assets shown on its balance, volume of property tax made up 1,000 GEL.

*In given case, the enterprise does not have liability to make current payment as of June 15, 2015. The enterprise is obliged to pay property tax of Y2015 proportionally with the period of its operation (9 months) with the volume of 750 GEL (1,000/12*9) not later than April 1, 2016. The enterprise is obliged to make current payment of annual tax with the volume of total amount (1,000 GEL) of previous (2015) year no later than June 15, 2016 according to the place of tax registration.*

Property tax of physical entity shall be calculated by the tax authority based on submitted declaration.

Physical entity submits property tax declaration to tax authority no later than November 1 of calendar year. Data on taxable property in declaration shall be filled according to the previous tax year, while taxable land data – according to the current tax year.

Physical entity shall pay property and land tax no later than November 15 of calendar year.

12. Property of Municipality

Relevance

LSGs possess property of various types. Basic property is discussed below in this chapter. Information presented here is useful for all employees of LSGs, as self-cost of assets makes influence on current as well as future financial condition of LSG. Accountants should know how to recognize and register revenues and expenses related to municipal property. While management, appointed as well as elected officials, need to know what influence the mentioned property has on financial resource of the LSG.

Rules and regulations discussed:

- ✓ Organic Law of Georgia "Local Self-Government Code"

12.1 Property of Municipality and its Formation

As per Georgian legislation, property of municipality are all things and intangible property owned by the municipality, inter alia:

- ✓ Property belonging to municipality by the rule of law;
- ✓ Property transferred to municipality ownership by the state;
- ✓ Property transferred to municipality ownership by the Autonomous Republic;
- ✓ Property created, purchased or registered by the municipality in accordance with the Georgian Legislation.

Municipality property is divided into two categories - basic (non-alienated) and complementary property.

Basic (non-alienated) property is a basis for performance of municipality authority. Basic property may only be used for performance of public functions of the municipality and exercising its power.

Complementary property is a property, which is not a part of basic (non-alienated) property and which might be used by the municipality in accordance with the requirements of Georgian Legislation.

It is prohibited to alienate basic (non-alienated) property of municipality except for the cases when this property has lost its functional destination.

As per the Local Self-Government Code municipality property comprises:

- ✓ Roads of local importance and parts of such roads, streets, underground crossings and pedestrian crossings, pavements, traffic lights, streetlight structures, squares, parks, boulevards, fountains, plants and riverbank protection structures.
- ✓ Non-agricultural land, except of privately-owned land and lands attached to the state property and state shareholding property.
- ✓ Forest and water resources of local importance;
- ✓ Agricultural land except of those not possessed by the municipality, inter alia:
    - Agricultural land in private ownership and registered as state owned;
    - Unregistered agricultural land within the borders of the municipality;
    - Cattle tracks

- Agricultural land located within 500 m long border line;
- National reserves, nature monuments, national parks and restriction lands;
- Lands denoted for historic, cultural, natural and religious monuments of state importance;
- Land of state forest fund;
- Land of state water fund;

Municipality may create its property by transfer of state owned property, by funds allocated from own budget, as a result of those events related to generation of civil-legal results as per Georgian Legislation, by creating or purchase of property in correspondence with the rules of Georgian Legislation, also by receiving property or/and works performed free of charge.

12.2 Legal Entities of Public Law by Municipality

Municipality are entitled to establish Joint Stock Company (JSC), Limited Liability Company (LLC) or Non-Entrepreneurial and Non-Commercial Legal Entity (N(N)LE) within the frames of its authority and in accordance with the Georgian Legislation. Municipality is also authorized to become a partner/shareholder/member of JSC, LLC or N(N)LE.

Municipalities are entitled to establish JSC, LLC, N(N)LE together or become partners/shareholders/founders of JSC, LLC established by other entities, including other municipality/s, and a member of N(N)LE with the aim of mutual business in accordance with legislative and subordinate acts.

Decision on establishment, reorganization and liquidation of Legal Entity under Public Law (LEPL) of the municipality, purchase of share or becoming a member of N(N)LE is made by the executive body of the municipality upon consent of municipal council.

Decision on appointment/dismissal of management/representative of LEPL of the municipality(s) is made by the executive body of the municipality as a founder/partner/shareholder/member of LEPL, in accordance with charter (provision) of relevant legal entity.

Alienation of basic property also transfer with the right to use of those enterprises where share of municipality exceeds 50%, also of N(N)LE established by the municipality and N(N)LE member of which is only municipality is performed in a form of public or electronic auction.

Free of charge transfer of property of LEPL of municipality(s) with the right to use, without auction is allowed for no more than 2 years, except of those cases when the property is transferred with the right to use to the bodies of Autonomous Republic of the state, municipalities, Legal Entity of Private Law established by them and LEPLs.

12.3 Disposal of Property of Municipality

Disposal of municipal property means privatization, transfer with the right to use, right to manage of municipal property or free of charge transfer in ownership with the right to use.

Privatization is transfer of municipal property into ownership of physical or/and legal entity in a form and with rules defined by this law.

Transfer with the right to use, means transfer of municipal property to physical, legal entity of public or/and private law with the right to use in correspondence with the pre-defined rules. Rights to use include right to build, usufruct, lease, rent, transfer in temporary use and other forms of use as defined by the Georgian Legislation.

Transfer of municipal property with the right to use is performed in a form of auction or by the rule of direct disposal. Decision on transfer of municipal property with the right to use through auction is made by the executive body of the municipality, while decision on free of charge transfer of property with the right to use by the rule of direct disposal is made by the executive body of the municipality upon consent of municipality council.

Transfer of municipal property with the right to use by the rule of direct disposal might be free of charge or may incur costs/fees - it may also be unconditional or conditional. Maximum period of free of charge transfer of municipal property with the right to use is 2 years.

There is no time limit for transfer of municipal property if it is transferred without auction based on free of charge right-to-build agreement, free of charge usufruct agreement and in temporary use to entities of autonomous republics, other municipality, LEPL (except of political parties), N(N)LE established by the municipality, enterprise which is partially (more than 50% of shares) owned by the municipality(s) or to the legal entity of private law established by this legal entity of private law itself.

Privatization of municipal property is performed in a form of public or electronic auction.

In case of privatization of municipal property through public auction, information is published in a local or other printing information editions and on a webpage: www.eauction.ge.

Disposal of municipal property might be performed in a form of electronic auction. In case of privatization of municipal property through electronic auction, information is published, and bidding is conducted on a web page www.eauction.ge.

The purpose of disposal of municipal property in a form of auction is to grant ownership rights, which will offer the highest price to the entity disposing the property.

An interested entity shall submit unconditional and irrevocable letter of credit issued by the authorized body with the pre-defined amount or shall pay advance for participation into the auction.

After evaluation of the total value of property or/and upon performance of the auction conditions, the buyer is granted an ownership certificate.

Intangible property of municipality includes shares, requirements and rights, that might be transferred to the other party or is targeted to bring material benefit to their owner or/and entitle the owner to put up requirements against the other entity.

Forms of disposal of shares include privatization of shares and transfer of management rights of shares.

Privatization of requirements and rights owned by the municipality is performed in a form of auction.

Revenues received from disposal of municipal property is directed to the budget of relevant municipality by the authorized body.

13 PREPARATION OF FINANCIAL (ACCOUNTING) REPORTS

Relevance

The Financial Reporting process encompasses the functions involved in ensuring that guidance in laws and regulations are followed. Included are the preparation of journal entries and posting; gathering and consolidating the information required for the development of financial statements and other financial reports and preparing and reviewing the financial statements and other reports. The accounting unit is charged with the responsibility of developing and issuing financial statements; senior managers are ultimately responsible for ensuring their fiscal information is accurate and submitted timely.

Financial reporting is the most tangible product of accounting. Accurate preparation of financial report is as much important as the ability to read, comprehend and use it. This chapter covers both parts. Despite describing how, when and why financial reports are prepared, purpose of this chapter is to increase comprehension of accounting forms required by the Georgian Legislation.

Laws and regulations discussed include:

- ✓ Order #364 of the Minister of Finance of Georgia dated April 2008 on "Accounting reporting forms for entities financed by Autonomous Republics' budgets and Local Self-Government budgets"
- ✓ Georgian Law "Budget Code"
- ✓ Georgian Law on "Legal Entity of Public Law"

Controls must be established to ensure all journal entries have been processed. Adherence to closing and reporting schedules and cutoffs must be strict and consistent. Under no circumstances should it be possible to make adjustments to accounting entries in a period for which the accounting unit has already prepared and issued financial report. A formal plan in which all responsibilities are clearly defined and include a timetable for completing tasks must exist.

Standardized journal entries must be utilized whenever possible. A process must be in place to identify standardized journal entries that were omitted or duplicated. Procedures for review and approval of the accounting treatment of non-standard or unusual transactions must be established.

All items in the financial statements and disclosures must be independently agreed to the underlying supporting documentation before submission.

Timely analysis of actual results compared to budget and forecasted information must be completed. All significant variances must be investigated

13.1 General Principles and Deadlines for Preparation of Financial (accounting) Reports

Financial reporting is a structural visualization of financial condition of entity and financial results of its operation.

Purpose of general financial reporting is to present information on financial condition, financial outcomes of entity 'operation and cash flow of entity so that it is useful for wide circles of users in decision making process and for evaluation of the entity. It might be used as a source of forecast.

Financial report in cash form describes the final results of financial-economic operation of entity represented by assets, liabilities, and equity and off-balance sheet articles. It also enables protection and effective control over economic resources of organization.

Usefulness of information represented in financial reports depends on quality characteristics: comprehensiveness, relevance, reliability and comparativeness.

Comprehensiveness means provision of information in a comprehensive way, so that the interested person understands it, implying that he/she has basic knowledge of financial issues.

Relevance means that information is presented in a way that satisfies general requirements of an interested person and assists him/her in evaluation of past, current and future operations.

Reliability is a characteristic of a financial report, when information presented doesn't include substantial inaccuracies and is not subjective.

Based on comparativeness, the user gets information on accounting policy and financial indicators in the beginning and by the end of reporting period.

Budgetary organizations financed by the budget of LSG shall prepare financial reports in accordance with the forms approved by the order #364 of the Minister of Finance of Georgia dated Y2008 on approval of "Accounting reporting forms for entities financed by Autonomous Republics' budgets and Local Self-Government budgets."

Financial reporting shall be prepared regularly quarterly – As of April 1, July 1, October 1 and annually. Spending organizations being financed by the budgets of Autonomous republics and LSG bodies shall submit accounting reports to local financial authorities within the terms determined by them; While budget organizations, LEPLs and N(N)LEs financed by the same sources are reportable against relevant controlling authorities within the terms determined by them.

As per the Code of Budget, regulations defined for LEPLs including accounting of financial–economic operations, reporting and balance sheet preparation, are applicable to N(N)LEs when it comes to budget processes relations.

As per the Law on "Legal Entities of Public Law", LEPL is obliged to perform accounting and reporting of financial-economic operation in accordance with the rules defined by the Georgian Legislation, prepare balance sheet and submit for approval to the relevant state controlling authority.

Annual balance of LEPL is verified by an independent audit appointed by the state controlling authority.

13.2 Financial (Accounting) Report for Management Purposes

The currently approved 14 accounting reporting forms provide a starting basis to improve financial management of the LSG. Managers must request accountants to present this information in relevant formats.

Financial reporting is compliance oriented and is used for external purposes. Unlike financial reports, management accounting is not mandatory and is for internal use only. Management reporting is focused on segments of the LSG. By segmenting, you can get into the details and analyze the drivers to gain insight on specific areas. If management reporting is not done each month, information could be missing that can help, or prevent from implementing, costly programs that don't provide results.

The financial statements are a record of the activities but do not provide an evaluation of the data. In order to be able to use the information contained in the various financial statements for financial decision-making, a number of measurements and evaluations needs to be made to the numbers. Only then will the information be useful as a tool for decision-making. This work must be done by accountants and must be requested by LSG management. The purpose of conducting measurements and making evaluation is to provide answers to questions. The process of conducting measurements and making of evaluation basically consists of the rearranging of the accounting data in order to obtain information in a format that can be used to appraise the performance, activities, financial health, stability and growth potential. It should be remembered that the financial statements reflect the historic activities and that decisions are taken about the future. This can only be done by drawing conclusions about trends of the different ratios, rather than the actual historic numbers.

Financial statements can contribute greatly to understanding the financial condition of the LSG through the addition of a comparison of actual results to budget results for each reporting period. The standard reports can provide useful information if current period results are compared with the same period results from the prior fiscal year. Furthermore, the usefulness as a management tool for the financial statements currently being prepared would increase if the actual results were presented period by period as well as year to date.

Preparing management orientated financial statements which display current year versus prior year results, as well as actual results compared to budget results, help internal controls. Trends are highlighted as well as patterns in numbers. The validity of actual results can be supported through management financial statements. A well-prepared budget is an excellent control over actual expenses. Fraudently activities or misuse of resources is often highlighted when budget variances are examined in closer detail.

13.3 Filling the Forms (balance and its annexes) of Financial (accounting) Reports

As per the approved instruction accounting consists of 14 forms, which are mandatory to fill, some are closely interrelated and shall not be neglected.

Form #1 Balance is filled according to the balances existing on natural accounts as of the start and the end of reporting period. To verify the balance, we shall use well known balance equation: sum of "Equity" section equals to sum of "Financial Assets and Requirements" section less sum of "Liabilities."

Net Value (5100) equals to "balance by the end of period" in annex "Form #3." Besides, if the organization is performing economic operations "Retained Earnings" (5220) or "Uncovered Loss" (5230) shall be equal to "Balance by the end of year (quarter)" in "Form #4". "Uncovered loss" is recorded in balance with negative mark.

Non-financial assets related items in Balance, in the beginning and by the end of reporting period shall equal the data of "Form #5."

Balance annexes "Form #2", "Form #2-1" and "Form #2-2" are filled according to budget performance, data might be withdrawn from treasury electronic system, e.g.: adjusted plan, liability, requirement and payment (cash expenses), as to the "Form 2" actual expenses it represents an actual expenses on natural accounts, besides "retained earnings" shall equal the balance of „Form 4."

Report on net value Form #3 represents difference between revenues received through budget resources and expenses according to accounting data. Report cash flow of revenues received from non-budgetary operations Form #4 represents difference between non budgetary revenues and non-budgetary sources.

Report on flow of non-financial assets (Form #5) is filled with non-financial assets inflow and outflow data considering chart of accounts. Receipt section describes origin of assets, while outflow section details outflow of assets according to their economic character.

Other forms are of informative character and are filled according to relative data.

Form #1

Balance

Name of Organization

____

Submission date ________________________________

Submitted by ____

(signature)

Periodicity: Annual, Quarterly

Measure Unit: GEL

Code	Asset	# of account	Balance as of beginning of year	Balance as of end of year (quarter)
1	2	3	4	5
	I. Financial assets and requirements			
010	Cash in national currency	1110		
020	Cash in foreign currency	1120		
030	Current account in a bank in national currency	1211		
040	Current account in a bank in foreign currency	1212		
050	Other accounts in a bank	1220		
060	Current account for non-budgetary resources in treasury	1230		
070	Account for targeted grants and targeted funding	1240		
080	Account for organizations' cash expenses through budgetary funds	1250		
090	Deposits in treasury in national currency	1260		
100	Deposits in treasury in foreign currency	1270		
110	Treasury currency account	1280		
120	Other accounts in treasury	1290		
130	Securities, except of shares	1310		
140	Short term loans	1320		
150	Shares and other equity	1330		
160	Derivative financial instruments	1340		
170	Interests charged on budgetary loans	1351		
180	Interests charged on non-budgetary loans	1352		
190	Interests charged on deposits and other financial assets	1353		
200	Requirements for charged fines, sanctions and other property-related revenues	1354		
210	Requirements for cash and cash equivalents through delivery of assets/services	1355		
220	Paid VAT	1356		
230	Pre-paid profit tax	1357		
240	Other tax assets	1358		
250	Requirements for deficit of cash and cash equivalents	1359		
260	Other short-term financial assets	1360		
270	Requirements for barter	1410		
280	Requirements against insurance companies	1420		
290	Requirements for goods and service delivery based on advance payments	1431		

300	Requirements for receipt of assets based on advance payments	1432		
310	Requirements by deficit of non-financial assets	1440		
320	Requirements against accountable entities	1450		
330	Requirements against employees	1460		
340	Requirements by pre-paid payments	1470		
350	Other short-term requirements	1480		
360	Long-term loans	1510		
370	Shares and other equity	1520		
380	Other long-term financial assets	1530		
390	Other long-term requirements	1540		
II. Non-financial assets				
400	Strategic inventory	1610		
410	Other inventory	1620		
420	Buildings and facilities	2110		
430	Machinery and equipment	2120		
440	Other fixed assets	2130		
450	Uncompleted fixed asset	2141		
460	Substantial improvement of property received through operational lease	2142		
470	Long-term low-cost assets	2200		
480	Values	2300		
490	Non-manufactured assets	2400		
	Balance			
Code	Liabilities and Equity	# of account	Balance as of beginning of year	Balance as of end of year (quarter)
1	2	3	4	5.00
I. Liabilities				
500	Short-term financial liabilities	3100		
510	Liabilities through goods and service delivery	3210		
520	Liabilities through asset supply	3220		
530	Liabilities by barter	3230		
540	Payable profit tax	3241		
550	Payable VAT	3242		
560	Payable income tax	3243		
570	Other payables	3244		
580	Liabilities accrued against budget	3245		
590	Salaries of basic staff	3251		
600	Salaries of freelancers	3252		
610	Liabilities through business trip within the borders of the country	3253		
620	Liabilities through business trip abroad	3254		
630	Liabilities through social benefit in a cash form issued by the employer	3255		
640	Liabilities through social benefit in a commodity form issued by the employer	3256		
650	Liabilities through amounts detained from employees' salaries	3257		
660	Scholarships payable	3258		
670	Social insurance payables	3259		
680	Liabilities against deponents	3260		
690	Liabilities by social benefits	3270		
700	Other short-term accounts payable	3280		
710	Long-term liabilities by credits	3310		
720	Other long-term financial liabilities	3320		
730	Long–term accounts payable by service provision	3331		
740	Long-term accounts payable by provision of assets	3332		

750	Other long-term accounts payable	3333		
II. Equity				
760	Net Value	5100		
770	Profit/loss of reporting period	5210		
780	Retained earnings	5220		
790	Uncovered loss*	5230		
	Balance			
III. Off balance sheet items				
800	Fixed assets with operation lease	01		
810	Inventory received under storage responsibility	02		
820	Written off debts of insolvent debtors	03		
830	Expensed inventory in operation	04		
840	Contingent requirements	05		
850	Contingent liabilities	06		
860	Equity generation with own resources	07		
870	Amortized fixed assets	08		
880	Overdue indebtedness	09		
890	Expensed long-term low-cost assets in operation	10		
900	Movable property transferable for disposal	11		
910	Bank guarantees	12		

Head of organization: ___________________________________

Chief Accountant: ____

Stamp

*Data of this raw are deducted from the sum of balance liabilities and equity

Balance Annex Form # 2

Report according to economic classification of expenses

Name of organization ------------------------	Code -------------------------------------
Periodicity: Annual, Quarterly -----------------20 -------- year, month	Unit: GEL

Row Code	List of expenses	Code	As per the plan approved by budget	As per unapproved plan of reporting period	Liability	Requirements	Payment (cash expenses)	Actual expenses	Deviation between actual expenses and payments (9-8)
1	2	3	4	5	6	7	8	9	10
010	**1. Expenses**	**2**							
020	**1.1 Labor remuneration**	**21**							
030	**1.1.1 Salaries**	**211**							
040	1.1.1.1 Salaries in a cash form	2111							
050	1.1.1.1.1 Basic salary	21111							
060	1.1.1.1.2 salary by rank	21112							
070	1.1.1.1.3 Bonus	21113							
080	1.1.1.1.4 Supplement	21114							
090	1.1.1.1.5 Royalty	21115							
100	1.1.1.1.6 Compensation	21116							
110	1.1.1.2 Salaries in a form of commodity	2112							
120	**1.2 Goods and Services**	22							
130	1.2.1 Remuneration of freelancers	221							
140	1.2.2 Business trips	222							
150	1.2.3 Office expenses	223							
160	1.2.4 Representative costs	224							
170	1.2.5 Meals	225							
180	1.2.6 Medical costs	226							
190	1.2.7 Expenses related to purchase of soft inventory and uniforms, also private hygiene	227							
200	1.2.8 Expenses of transport, techniques and tools operation and maintenance	228							
210	1.2.9 Cost of purchase of military equipment and bullets.	229							
220	1.2.10 Other goods and services	2210							
230	**1.3 Main capital consumption**	23							
240	**1.4 Interest**	24							
250	**1.4.1 On foreign liabilities**	241							
260	1.4.1.1 On bilateral creditors	2411							
270	1.4.1.2 On multilateral creditors	2412							
280	1.4.1.3 On commercial organizations	2413							
290	1.4.1.4 On other foreign liabilities	2414							
300	**1.4.2 Internal liabilities except of the state entities**	242							
310	**1.4.3 Internal liabilities through the state entities**	243							
320	**1.5 Subsidies**	25							

Row Code	List of expenses	Code	As per the plan approved by budget	As per unapproved plan of reporting period	Liability	Requirements	Payment (cash expenses)	Actual expenses	Deviation between actual expenses and payments (9-8)
1	2	3	4	5	6	7	8	9	10
330	**1.6 Grants**	26							
340	**1.6.1 Grants to the governments of foreign countries**	261							
350	1.6.1.1 Current	2611							
360	1.6.1.2 Capital	2612							
370	**1.6.2 Grants to international organizations**	262							
380	1.6.2.1 Current	2621							
390	1.6.2.2 Capital	2622							
400	**1.6.3 Grants to the other level state entities**	263							
410	1.6.3.1 Current	2631							
420	1.6.3.2 Capital	2632							
430	**1.7 Social Security**	27							
440	**1.7.1 Social Insurance**	271							
450	1.7.1.1 In cash form	2711							
460	1.7.1.2. In commodity form	2712							
470	**1.7.2 Social benefits**	272							
480	1.7.2.1 In cash form	2721							
490	1.7.2.2. In commodity form	2722							
500	**1.7.3 Social benefits issued by the employer**	273							
510	1.7.3.1 In cash form	2731							
520	1.7.3.2. In commodity form	2732							
530	**1.8 Other expenses**	28							
540	**1.8.1 Property related expenses, except of interest**	281							
550	1.8.1.1 Dividends	2811							
560	1.8.1.2 Cash from revenues of quasi corporations	2812							
570	1.8.1.3 Property related expenses applicable to insurance policy holders	2813							
580	1.8.1.4 Rent	2814							
590	**1.8.2 Various expenses**	282							
600	1.8.2.1 Current	2821							
610	1.8.2.2 Capital	2822							

Data on number of basic staff and freelancers				
Description	Budgeted		Off-budget	
	Planned	Actual*	Planned	Actual*
1. Number of basic staff				
2. Number of freelancers				

* Actual number of basic staff is calculated by average number of employees according to months within the reporting period. (Sum of average monthly number of employees shall be divided by the number of months within the reporting period).

Head of organization: ___________________________________

Chief Accountant: ____

Stamp

Balance Annex Form #2-1

Report on cash operations by non-financial assets

Name of organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ _ _20 Year, Month _ _	Unit: GEL

Row Code	List of non-financial assets	Non-financial assets operation codes	As per the approved planned	Adjusted plan	Liability	Requirement	Payment (cash expense)
1	2	3	4	5	6	7	8
010	**1. Non-financial assets**	**31**					
020	**1.1 Fixed assets**	**311**					
030	**1.1.1 Buildings and facilities**	**3111**					
040	1.1.1.1 Residential buildings	31111					
050	1.1.1.2 Non-residential buildings	31112					
060	1.1.1.3 Highways	31113					
070	1.1.1.4 Streets	31114					
080	1.1.1.5 Roads	31115					
090	1.1.1.6 Bridges	31116					
100	1.1.1.7 Tunnels	31117					
110	1.1.1.8 Sewage and water supply systems	31118					
120	1.1.1.9 Transmittion lines	31119					
130	1.1.1.10 Pipelines	311110					
140	1.1.1.11 Other buildings and facilities	311111					
150	**1.1.2 Machinery and equipment and inventory**	**3112**					
160	1.1.2.1 Transportation means	31121					
170	1.1.2.2 Other machinery and equipment and inventory	31122					
180	**1.1.3 Other fixed assets**	**3113**					
190	1.1.3.1 Cultivated assets	31131					
200	1.1.3.2 Intangible fixed assets	31132					
210	1.1.3.2.1 Licenses	311321					
220	1.1.3.2.2 Other intangible fixed assets	311322					
230	**1.2 Inventory**	**312**					
240	**1.2.1 Strategic inventory**	**3121**					
250	**1.2.2 Other inventory**	**3122**					
260	1.2.2.1 Raw materials and materials	31221					
270	1.2.2.2 Uncompleted production	31222					
280	1.2.2.3 Readymade product	31223					
290	1.2.2.4 Goods purchased for further realization	31224					
300	**1.3 Values**	**313**					
310	**1.4 Non-manufactured assets**	**314**					
320	**1.4.1 Land**	**3141**					
330	**1.4.2 Natural resources**	**3142**					
340	**1.4.3 Other natural assets**	**3143**					
350	1.4.3.1 License for use of radiofrequency spectrum	31431					
360	1.4.3.2 Other natural assets	31432					
370	**1.4.4 Non-manufactured intangible assets**	**3144**					

Head of organization: ___________________________________
Chief Accountant: ____
Stamp

Balance Annex Form # 2-2

Report on cash operations by financial assets and liabilities

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ _ _ 20 Year, Month	Unit: GEL

Code of row	Financial assets and liabilities	Operational codes of financial assets and liabilities	As per approved plan	As per adjusted plan	Liability	Requirement	Payment (cash expense)
1	2	3	4	5	6	7	8
010	**1. Financial assets**	**32**					
020	**1.1 Internal**	**321**					
030	1.1.1 Currency and deposits	3212					
040	1.1.2 Securities except of shares	3213					
050	1.1.3 Loans	3214					
060	1.1.4 Shares and other equity	3215					
070	1.1.5 Insurance technical reserves	3216					
080	1.1.6 Derivative financial instruments	3217					
090	1.1.7 Other accounts receivable	3218					
100	**1.2 External**	**0 322**					
110	1.2.1 Currency and deposits	3222					
120	1.2.2 Securities except of shares	3223					
130	1.2.3 Loans	3224					
140	1.2.4 Securities and other equity	3225					
150	1.2.5 Insurance technical reserves	3226					
160	1.2.6 Derivative financial instruments	3227					
170	1.2.7 Other accounts receivable	3228					
180	**1.3 Monetary gold and special drawing rights**	**323**					
190	**2. Liabilities**	**33**					
200	**2.1 Internal**	**331**					
210	2.1.1 Currency and deposits	3312					
220	2.1.2 Securities, except of shares	3313					
230	2.1.3 Loans	3314					
240	2.1.4 Shares and other equity (state enterprises and organizations only)	3315					
250	2.1.5 Insurance technical reserves	3316					
260	2.1.6 Derivative financial instruments	3317					
270	2.1.7 Other accounts payable	3318					
280	**2.2 External**	**332**					
290	2.2.1 Currensy and deposits	3322					
300	2.2.2 Securities, except of shares	3323					
310	2.2.3 Loans	3324					
320	2.2.4 Shares and other equity (state enterprises and organizations only)	3325					
330	2.2.5 Insurance technical reserves	3326					
340	2.2.6 Derivative financial instruments	3327					
350	2.2.7 Other accounts payable	3328					

Head of Organization: ___________________________________

Chief Accountant: ____

Stamp

Balance Annex Form # 3

Report on net value

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ __ _20 Year, Month _ _ _ _	Unit: GEL

# of account	Debit	Amount	# of account	Credit	Amount
	Balance as of the beginning of year			Balance as of the beginning of year	
7100	Salaries of employees		4100	Funds received from budget	
7200	Goods and services		4200	Funds received from budget for pensions and benefits	
7300	Consumption of basic capital		6000	Revenues	
7310	Incl. physical depreciation		6300	Incl. Grant	
7400	Interest				
7500	Subsidies				
7600	Grants				
7700	Social security				
7800	Other expenses				
8200	Non-operation expenses		8100	Non-operation revenues	
3245	Accrued liabilities against budget*				
	Debit turnover			Credit turnover	
	Sum:**			Sum:***	
	Balance by the end of period			Balance by the end of period	

* This row includes budget funds received from revenues of budgetary organizations and other receipts.
** Debit balance as of beginning of year is added to debit turnover
*** Credit balance as of beginning of year is added to credit turnover

Head of Organization: ___________________________________
Chief Accocuntant: ____
Stamp

Report on turnover of resources received from non-budgetary activity

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ _ _20 Year, Month _ _ _ _	Unit: GEL

Code of row	Description		Planned	Cash	Actual
1	2		3	4	5
010	Cash balance as of the beginning of year				
020	Balance of retained earning/uncovered loss as of the beginning of year				
030	**Receipts**				
040	**Operational revenues**				
050	**Revenues of accounting period according to classification**				
060	**Taxes**				
070	**Grants**				
080	**Other revenues**				
090	a) revenues from property				
100	b) realization of goods and services				
110	c) sanctions, penalties, fines				
120	d) voluntary transfers, except of grants				
130	e) mixed and other non-classified revenues				
140	**Receipts**				
150	**Decrease of non-financial assets**				
160	**Decrease of financial assets**				
170	**Increase of liabilities**				
180	**Total operational revenues and receipts**				
190	**Payments**				
200	Operational expenses				
210	1. Expenses according to economic classification	Code			
220	1.1. Salaries	**21**			
230	1.2 Goods and services	**22**			
240	1.3 Consumption of basic capital	**23**			
250	1.4 Interest	**24**			
260	1.5 Subsidies	**25**			
270	1.6 Grants	**26**			
280	1.7 Social security	**27**			
290	1.8 Other expenses	**28**			
300	**Payments**				
310	**2. Increase of non-financial assets**	**31**			
320	2.1 fixed assets	311			
330	2.2 Inventory	312			
340	2.3 Values	313			
350	2.4 Non-manufactured assets	314			
360	**3. Increase of financial assets**	**32**			
370	3.1 Internal	321			
380	3.2 External	322			
390	**4. Decrease of liabilities**	**33**			
400	4.1 Internal	331			
410	4.2 External	332			
420	**Total operational expenses and payments**	332			

Code of row	Description	Planned	Cash	Actual
1	2	3	4	5
430	**Non-operational revenues and expenses**			
440	Non-operational revenues			
450	Revenue received through exchange rate difference			
460	Non-operational revenues from non-financial assets			
470	Non-operational revenues from financial assets			
480	Non-operational revenues by liabilities			
490	Non-operational expenses			
500	Loss received through exchange rate difference			
510	Non-operational expenses from non-financial assets			
520	Non-operation expenses from financial assets			
530	Non-operation expenses by liabilities			
540	Profit tax			
550	Balance by the end of year (quarter)			

Head of Organization: ___________________________________
Chief Accountant: _______________________________________
Stamp

Balance Annex Form # 4-1

Report on targeted funding and targeted grants

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ __ _20 Year, Month _ _ _	Unit: GEL

		In foreign currency	In national currency	Total in GEL		
				Planned	Cash	Actual
1	**Total volume of Grant**					
2	Incl. amount received					
3	Incl. total approved volume					
4	Incl. the last transfer					

1	Balance by the beginning of period			
2	Volume of current year			
3	Total (1+2)			
4	Expenses			
5	Labor remunerations			
6	Goods and services			
7	Interest			
8	Subsidies			
9	Grants			
10	Social Security			
11	Other Costs			
12	Increase of non-financial assets			
13	Increase of financial assets			
14	Decrease of liabilities			
15	Total volume approved by the current year			
16	Liabilities against budget by grant amount			

Head of Organization: ___________________________________
Chief Accountant: _______________________________________
Stamp

Annex # 5

Report on flow of non-financial assets

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly_ _ _ _ _ _ _ _ __ _20 Year, Month _ _ _ _	Unit: GEL

			Receipt									Outflow														
	Non-financial assets	Balance as of the beginning of year	Purchase by reduction of previous year	Purchase of current period	by Barter	by non-operational revenues	by Grants	by other revenues	Equity formation by own sources	by loss reinstitution	other receipts	by sales	by Barter	Non-operational expenses	in a form of shares and other equity	Salaries in a form of commodity	by Subsidies	by Grants	by Social benefits	by deficit	by other costs	Equity formation by own sources	Basic capital consumption	by goods and services	other expenses	Balance by the end of year (period)
010	**1. Inventory**																									
020	1.1. Strategic inventory																									
030	1.2. Other inventory																									
040	1.2.1. Raw materials and materials																									
050	1.2.2. Uncompleted production																									
060	1.2.3. Ready made production																									
070	1.2.4. Goods purchased for further realization																									
080	1.2.5. Cash documents																									
090	1.2.6. Spare parts																									
100	1.2.7. Other remaining inventory																									
110	**2. Fixed assets**																									
120	2.1 Buildings and facilities																									
130	2.1.1 Residential buildings																									
140	2.1.2 Non-residential buildings																									
150	2.1.3 highways																									
160	2.1.4 Streets																									
170	2.1.5 Roads																									
180	2.1.6 Bridges																									
190	2.1.7 Tunnels																									
200	2.1.8 Utility systems																									
210	2.1.9 Other buildings and facilities																									
240	2.2 Machinery and equipment and inventory																									
250	2.2.1 Transportation means																									
260	2.2.2 Other machinery and equipment and inventory																									
270	2.3 Other fixed assets																									
280	2.3.1 Cultivated assets																									
290	2.3.2 Intangible fixed assets																									
300	2.4 Other fixed assets																									
310	2.4.1 Uncompleted fixed assets																									
320	2.4.2 Substantial improvement of property received by operational lease																									

	Non-financial assets	Balance as of the beginning of year	Purchase by reduction of previous year advances	Purchase of current period	by Barter	by non-operational revenues	by Grants	by other revenues	Equity formation by own sources	by loss reinstitution	other receipts	by sales	by Barter	Non-operational expenses	in a form of shares and other equity	Salaries in a form of commodity	by Subsidies	by Grants	by Social benefits	by deficit	by other costs	Equity formation by own sources	Basic capital consumption	by goods and services	other expenses	Balance by the end of year (period)
330	**3. Long-term low-cost assets**																									
340	**4. Values**																									
350	4.1 Precious stones and metals																									
360	4.2 Works of art																									
370	Other values																									
380	5 Non-manufactured assets																									
390	5.1 Land																									
400	5.2 Natural resources																									
410	5.3 Other natural assets																									
420	5.4 Non-manufactured intangible assets																									

*makes account of use of raw materials and materials in production and other flow of non-financial assets

Head of Organization: ___________________________________

Chief Accountant: _______________________________________

Stamp

Report on change of financial assets and liabilities

as a result of non-operational revenues and non-operational expenses

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ _ _ _20 Year, Month _ _ _ _	Unit: GEL

	Name of financial assets and liabilities	Non-operational revenues Credit (8100)	Non-operational Expenses Debit (8200)
010	**Financial Assets**		
020	Currency and deposits		
030	Securities, except of shares		
040	Loans		
050	Shares and other equity		
060	Insurance technical reserves		
070	Derivative financial instruments		
080	Other accounts receivable		
090	Monetary gold and special drawing rights		
100	**Financial liabilities**		
110	Currency and deposits		
120	Securities, except of shares		
130	Loans		
140	Shares and other equity		
150	Insurance technical reserves		
160	Derivative financial instruments		
170	Other accounts payable		

NOTE – Corresponding accounts of non-operational revenues and non-operational expenses accounts (8100 – 8200) are those accounts relevant to the items indicated in rows # 010-170 and the form is filled as trial balance.

Head of Organization: ___________________________________

Chief Accountant: ______________________________________

Stamp

Information on analytical accounting data of non-financial assets

Name of Organization _ _ _ _ _ _ _ _ _ _ _ _ _	Code _ _ _ _ _ _ _ _ _ _ _ _ _
Periodicity: Annual, Quarterly _ _ _ _ _ _ _ _ _ _20 Year, Month _ _ _ _	Unit: GEL

Description		As of beginning of reporting period		Inflow of reporting period				Outflow of reporting period				Expenses (cash) incurred in reporting period				Expenses (actual) incurred in reporting period			
				Purchase		Received the other way		Operational consumption		Consumed the other way									
		Quantity	Cost	Quantity	Cost	Quantity	Cost	Quantity	Cost	Quantity	Cost	Total Cost	Including repair	Including fuel	Incl. spare parts	Total cost	Incl. repair	Incl. fuel	Incl. spare parts
1	**Total number of transportation means:**																				
	Including																				
1.1	*Light*																				
1.2	*Jeeps and pickups*																				
1.3	*Passenger vehicles*																				
1.4	*Freight vehicles*																				

Head of Organization: ___________________________________

Chief Accountant: ______________________________________

Stamp

Form # 7

Information on accounts receivable accrued on accounts

N	Description	Accrued accounts payable as of Y 20 ___	Inter alia, according to the year of origin										
		Total	Y1996-2006	Y2006	Y2007	Y2008	Y2009	Y2010	Y2011	Y2012	Y2013	Y2014	Y2015
1	2	3	4	5	6	7	8	9	10	11	12	13	14
010	Total												
020	Receipts (indebtedness by accrual)												
030	Grants												
040	Other revenues												
050	Decrease of non-financial assets												
060	Decrease of financial assets												
070	Payments (indebtedness by advance payments)												
080	Labor remuneration												
090	Goods and services												
100	Including wages of freelancers												
110	Business trips												
120	Office expenses												
130	Representative costs												
140	Meals costs												
150	Medical expenses												
160	Soft inventory, uniforms and private hygiene expenses												
170	Transport and technique operation and maintenance expenses												
180	Military technique and bullets purchase expenses												
190	Other goods and services												
200	Interest												
210	By foreign liabilities												
220	Internal entities except of state entities												
230	By internal liabilities obtained from state entities												
240	Subsidies												
250	Grants												
260	Social security												
270	Other costs												
280	Increase of non-financial assets												
290	Other requirements (except of items defined by the budget classification)												
300	Deficit												
310	Barter												
320	Other requirements												

Head of Organization: ___________________________________ Date

Chief Accountant: ____ Date

Stamp

Form # 8

Information

On accounts payable accrued on accounts

N	Description	Date	Inter alia according to date of origin										
		Total	Y 1996-2005	Y 2006	Y 2007	Y 2008	Y 2009	Y 2010	Y 2011	Y 2012	Y 2013	Y 2014	Y 2015
1	2	3	4	5	6	7	8	9	10	11	12	13	14
010	**Total:**												
020	**Revenues (indebtedness born out of funds received in advance)**												
030	**Payments**												
040	**Salaries**												
050	**Goods and services**												
060	*Including wages of freelancers*												
070	*Business trips*												
080	*Office expenses*												
090	*Representative expenses*												
100	*Meal costs*												
110	*Medical costs*												
120	*Soft inventory, uniforms and private hygiene inventory purchase expenses*												
130	*Transport and technique operation and maintenance expenses*												
140	*Military technique and bullets purchase expenses*												
150	Other goods and services												
160	**Interest**												
170	**Subsidies**												
180	*Salaries*												
190	*Goods and services*												
200	*Social security*												
210	*Other expenses*												
220	**Grants**												
230	**Social security**												
240	**Other expenses**												
250	*Other current expenses*												
260	*Various capital costs*												
270	**Purchase of non-financial assets**												
280	*Fixed assets*												
290	*Inventory*												
300	*Values*												
310	*Non-manufactured assets*												
320	**Financial liabilities**												
330	**Other liabilities**												
340	Barter												
350	Other liabilities												

Head of Organization: ___________________________________ Date
Chief Accountant: ____ Date
Stamp

Information on accounts receivable in organizational context

N	Name of Organization	Debit amount	Date of origin	Basis	Item	NOTE
1						
2						
3						
4						
5						
6						
7						

Head of Organization: ___________________________________ Date
Chief Accountant: ____ Date
Stamp

Form # 10

Information on accounts payable in organizational context

N	Name of Organization	Credit amount	Date of origin	Basis	Item	NOTE
1						
2						
3						
4						
5						
6						
7						
8						
9						

Head of Organization: ___________________________________ Date
Chief Accountant: ____ Date
Stamp

14 LOCAL GOVERNMENTS' INVESTMENT PROJECTS

Relevance

Implementation of local governments' investment projects depends on their ability to raise the necessary funds from a combination of own resources and external financing. External financing enables municipalities to carry out more infrastructure projects in a shorter time period as compared to the financing from own funds.

Financing institutions be they the capital market, donors or internal organizations such as the MDF, MRDI need readable, credible, transparent and comparable financial documents and reports as an input in the credit risk analysis of local governments. This can only be achieved if local governments fully comply with legal and regulatory guidance and accounting standards, which accurately reflect the true financial position of local governments.

Below is provided a review of credit obtaining procedure as well as the Municipal Development Fund processes and criteria. The objective is to build skills in comprehending what is required as well as the reasons which stand behind them.

14.1 Assessment of Investment-Worthiness [1]

Definition of creditworthy: This is an organization financially sound enough to justify the extension of credit. Creditworthiness is a creditor's judgment of an the LSG 's current and future ability, and inclination to honor debt obligations as agreed upon. It is usually based on the credit history, credit rating, and character of the LSG.

In general, the creditworthiness assessment of a (local) government is based on the following three broad factors: #1 Economic Risk, # 2 Political Risk, and # 3 Financial Risk

A credit rating is an assessment of an the LSG 's ability to pay its financial obligations. The LSG whose creditworthiness is being assessed typically is referred to as an obligor or issuer. Credit ratings generally reflect a relative ranking of credit risk. Credit ratings typically are expressed on a scale of alpha and/or numeric symbols, and these symbols are defined by the particular credit rating agency issuing those ratings.

A credit rating may reflect a credit rating agency's subjective judgment of an issuer's business and management. While historical financial and operating experience and collateral performance may factor into the analysis of an obligor, credit ratings are simply a prediction of how an obligor may behave in the future. Predictions are based on the views of the credit rating agency, which may differ. A credit rating is not a guarantee that a financial obligation will be repaid.

There are no standard or agreed-upon methods to measure the accuracy of credit ratings. this is partly because of the subjective nature of credit ratings.

There are two major types of debt instruments available to finance municipal capital expenditures: # 1 loans and # 2 bonds. Loans are granted by a financial institution (e.g. commercial bank) directly to the local

[1] Source of submitted information is partially Network of Associations of Local Authorities of South-East Europe - http://www.nalas.eu together with US securities and exchange commission.

government. Applying for a loan is less complex than the procedures required for bond issuance. From this point of view, loans are more advantageous to small and medium size municipalities seeking external financing. Please note that per the Law of Georgia on Public Debt (March 1998), public debt securities can only be issued by the Ministry of Finance and and borrowing undertaken by LSGs can only be done after approval from the central government.

Municipal bonds are debt securities issued to fund day-to-day obligations and to finance capital projects. The type of municipal bond issued affects both the risk of default and the value of the municipal bond. Repayment may come from the issuer, an obligor, or from a single tax or revenue source. There are two major types of municipal bonds: “general obligation bonds” and “revenue bonds.”

General obligation bonds are issued by governmental entities and are not backed by revenues from a specific project or source. Some general obligation bonds are backed by designated taxes on real property and, on occasion, other taxes. Other general obligation bonds are payable from general funds and are often referred to as backed by the “full faith and credit” of the government. Revenue bonds are backed by revenues from a specific project or source. There can be a wide diversity of types of revenue bonds, each with unique credit characteristics.

A key concern is whether the issuer or other obligor will be able to pay interest and principal in full. The creditworthiness of a local government measures both quantitatively and qualitatively its ability to repay. This involves:

1. A thorough analysis of the local governments financial position,
2. An assessment of the local economy in which the municipality operates (e.g. economic and political context) and
3. An evaluation of the national macroeconomic environment.

Key in the analysis of the strength of the local economic structure are the following factors:

- ✓ Economic and Social Infrastructure and Socioeconomic Trends underpinning the demand for public services provided by the Local Government
- ✓ Per Capita Income and its Volatility
- ✓ Real Annual Local GDP Growth
- ✓ Composition of Local GDP
- ✓ Natural Resources
- ✓ Employment Growth & Quality of Workforce
- ✓ Economic Policies

In addition, the relationship between the central and local governments has to be also taken into account as this may have an impact on transfers or grants from the central government and direction of investments in new projects. Political risk is a judgmental factor. It should consider the (political) stability of the local government in the past and the attitudes of major political parties towards important issues for the local community.

Municipal senior management must be well prepared to identify, evaluate and mitigate the main sources of risk for the financial situation of the local government, un-controlled expenditures and commitments. The financial situation and financial management culture of a local government is crucial as this determines the ability to manage public finances. Factors that have an impact on the financial condition of local governments include:

- ✓ Revenue and Expenditure Structure and Dynamics
- ✓ Net Operating Result
- ✓ Ongoing Liquidity and Cash Flow Management
- ✓ Financial Flexibility – Autonomy to Raise Taxes and Fees,
- ✓ The Ability to Balance Financial Operations Over Economic Cycles
- ✓ Willingness and Ability to Monitor, Evaluate and Control Expenses
- ✓ Indebtedness – both on and off-balance sheet debt

When determining local government borrowing capacity projecting the future financial position, revenues and expenditures is a key factor. The forecasting framework of local revenues and expenditures must incorporate the economic, political and financial risk factors. Maximum borrowing capacity of a local government can be estimated as the present value of its future net operating surpluses (operating surplus minus debt service on outstanding debt). The discount rate used in the present value calculation should be the interest rate charged by banks for loans to borrowers with a similar credit profile. Local governments should be able to demonstrate that they are able to generate persistent positive net operating results in the future, as a precondition for borrowing.

The ratio of expected net operating result to expected debt service is probably one of the most important indicators of local governments' debt carrying capacity. If the ratio is close to one, then any major fluctuation in a local government's operating revenues or expenditures could result in serious problems in meeting the debt service obligation. A ratio significantly higher than one indicates that the local government has a comfortable financial position relative to its debt obligations.

The below information has been extracted from the OPERATIONS MANUAL of the MDF for the SECOND REGIONAL AND MUNICIPAL INFRASTRUCTURE DEVELOPMENT PROJECT the full document is available on the MDF website (http://mdf.org.ge) for downloading.

14.2 Municipal Development Fund Application Preparation

Municipal Development Fund of Georgia

The Municipal Development Fund of Georgia (MDF) is a legal the LSG of public law whose purpose is to mobilize financial resources from donors including international and Georgian financial institutions, donor agencies, countries, economic organizations, as well as the Government of Georgia and LSG units, and to make them available for investments in local infrastructure and services, while simultaneously helping LSG units to strengthen their institutional and financial capacity.

MDF was established by the Government of Georgia by Presidential Decree #294 dated June 7, 1997 'On Management of Funds Designated for the Development of the Municipal Sector in Georgia' for the purpose of managing the investment component of the First Municipal Development and Decentralization Project (MDDP I). MDF Charter was adopted by the Decree of the government of Georgia #118 dated July 23, 2005 (updated from time to time).

In carrying out its activities, the MDF acts in accordance with the provisions of Law 'On Legal The LSG of Public Law' of May 28, 1999, the provisions of other relevant laws of Georgia, Orders and Decrees of the

President of Georgia, agreements of the Government of Georgia with international financial institutions, including the World Bank, and other donors, its Charter, and the instructions of this Operations Manual (OM). MDF is financially autonomous, has its own bank account in a commercial bank. It has its own seal with the MDF emblem and Georgian-English printing. Its head office is located in Tbilisi.

General Overview of MDF Activities

MDF activities fall into three broad categories:

- Financing of investments through extension of loans to MDF clients and mobilization of resources from internal and external financing sources as well as from loan repayments by MDF clients.
- Management of implementation of investment projects partially financed by MDF loans on behalf of MDF clients.
- Provision of technical assistance to entities of the Government and MDF clients within the frames of programs of institutional development and improvement of management capacity.

Second Regional and Municipal Infrastructure Development Project (RMIDP II)

The World Bank has provided support to the GoG's decentralization agenda through the Second Regional and Municipal Infrastructure Development Project (RMIDP II) (with a possible additional loan from Council of Europe Development Bank and grant from SDC). The priority is to improve the ability of subnational level governments to carry out their core functions related to service delivery to the population and accountability through facilitating LSGs access to viable financing to implement priority infrastructure investments.

Types of eligible investments

Investment projects financed by MDF loans and grants from RMIDP II resources will be for rehabilitation and repair of existing service infrastructure and facilities and/or replacement of equipment required for service delivery in the following categories, upgrade as well as construction of the new ones. Any sub-project falling into another category can only be considered upon prior consultation and agreement with the World Bank.

No MDF financing can be used for schools, commercial enterprises, land acquisition, working capital or other operating budget support, acquisition of used vehicles and equipment, maintenance and operation activities.

14.3 Municipal Development Fund Application Procedure

The outlined below apply exclusively to investment sub-projects and other activities carried out by the MDF under RMIDP II. MDF operations financed from other sources will be governed by the instructions and regulations of the respective donors.

All World Bank rules and regulations apply, and the instructions contained in this OM may be adjusted by mutual agreement from time to time to reflect any such changes.

Nature of MDF Business Products

Investment Project Financing: MDF will prepare Sub-project Summary Reports (SSRs) for investments less than \$2.5 million and Sub-projects Appraisal Reports (SARs) for investments more than \$2.5 million and approval of the Supervisory Board.

A) LOAN FINANCING (WINDOW 1)

The financing of investment projects by MDF under RMIDP II will be based on the following rules governing the sharing of contributions from the three sources of funding involved:

- ✓ 20 % to be covered by LSGs' contribution
- ✓ 30 % to be covered by Grant (Donor)
- ✓ 50 % to be covered by the MDF loan. Reimbursable under the following terms and conditions:
  - Interest rate: 7 % per annum
  - Maturity: 6-12 years
  - Grace period: up to 18 months (for principal)

Interest on the loan will accrue from the respective dates on which amounts will be disbursed and will be computed on the basis of a 360-day year of twelve 30-day months. The MDF client does not start loan repayment during the period of works, considered under the project. The payment of interest accrued on the loan principal starts upon the completion of works (after the last disbursement is made). The day of the repayment coincides with the starting day for interest accrual.

The MDF client will repay the full amount of interest accrued during the period of works execution. The further repayments will be made on a monthly basis. During the grace period following the date of the first disbursement the MDF client is not repaying the loan principal and interest. Upon the completion of this period, it will make monthly repayments of the loan principal portions along with the accrued interest on the basis of equal monthly installments.

Minimum and Maximum Loan Amount from MDF: The minimum capital cost of an investment sub-project to be financed by MDF on lending basis will be $ 200,000. This will reduce the transaction cost of managing the loan portfolio. While the maximum loan amount is traditionally the credit capacity of a municipality but not more than 8 million USD per LSG.

Any exceptions to this rule will require the prior agreement of the World Bank on the expected investment cost, the scope and nature of the feasibility and other preparatory studies are required, and the proposed implementation plan as well as a satisfactory review of all such studies.

Any of the above terms and conditions for MDF loans may be changed by joint agreement of the Government of Georgia and the World Bank in the course of RMIDP II implementation to reflect new developments in the Georgian economy. However, once a loan agreement has been signed, its terms and conditions cannot be changed, unless explicitly stated so in the Loan Agreement and approved by the MDF client.

B) GRANT FINANCING (WINDOW 2)

A Grant Facility to Assist Non-Creditworthy or LSGs with Limited Credit Capacity.

A grant facility will be established to fund municipal services and infrastructure sub-projects under component 1.2 in small, noncreditworthy or LSGs with very limited credit capacity. The minimum cost of a sub-project will be $100,000 and the maximum grants amount per LSG is $2.00 million. For any sub-project to be considered by MDF, a 15% contribution of the total cost of sub-project from the beneficiary LSG will be required.

C) TECHNICAL ASSISTANCE FINANCING:

Unless otherwise specified, all technical assistance, training and consultant services will be provided on a grant basis and its cost will be financed to 80% from the Credit and 20% from GOG Co-financing, except training, which will be financed 100 % from IDA sources.

Investment Financing Eligibility Criteria:

Eligible Entities: Eligible for MDF investment project financing are LSGs which are authorized to borrow from MDF under Georgian law, have their own revenue sources and enjoy decision-making autonomy for the categories of investment for which MDF financing is sought:

- Self-Governing Cities
- Local Self-Governments

Upon prior approval of the World Bank given on a case by case basis, local utilities may also be eligible for direct MDF loan financing if they can demonstrate that they are financially autonomous (i.e. have independent balance sheets and income statements), receive the totality of their financial resources from tariff and fee income, and have decision-making autonomy over operating and capital expenditure.

Investment Sub-projects costing less than 2 million USD equivalent do not require prior approval by the World Bank, except of those cases where such Investment sub-projects would be classified as an Environmental Assessment Category “A” or require RAP.

Local Self-Governments: Eligibility Criteria

Financial Eligibility Criteria: LSG applying for a loan from the MDF must have an adequate borrowing capacity which will be calculated on the basis of the below mentioned requirements.

The LSG must also meet the below mentioned budget performance criteria. The following additional aspects apply when analyzing the borrowing capacity of the LSG:

1. Total annual debt service payments (principal, interest and any other charges) on all outstanding and proposed loans for the current year should not exceed 5% of the last year actual income resources or potentially collectable income resources, whichever falls less.
2. Actual income resources are the sum of tax, non-tax and capital revenues and the unconditional equalization grant from the national government within the last year and as recorded in the approved annual report.
3. Potentially collectable income resources is the sum of tax, not limited to the property tax, but including all taxes collectable in the municipality, non-tax and capital revenues within the last year and as recorded in the approved annual report.
4. Using the above-mentioned credit capacity formula, annual debt service payment should not exceed the municipality’s annual income from property tax for the same period. If the last year property tax amount is less than annual debt service payment, property tax amount will be considered as a debt repayment privileged amount.
5. Total outstanding debt should not exceed 150% of last year actual income resources.
6. The municipal government should have the capacity to repay at least GEL 176,000 per annum in debt service and forecast resources of more than GEL 3.510 million annually.

Investment Sub-project Preparation and Appraisal

Preparation and appraisal of an investment sub-project by the MDF will involve the following steps.

Step 1. The participating municipal government applying for the financing of a specific investment project submits a request to MDF for financing, together with a sub-project summary.

Step 2. MDF reviews the request with a view of determining whether:

1. The proposed sub-project concept and design are informed by a meaningful public consultation process with a diversity of local stakeholders including marginalized and vulnerable groups and equally representing gender;
2. The proposed sub-project is consistent with MDF financing principles;
3. The applying municipal government is eligible for funding under loan financing (loan-grant-co-financing combination) or grant financing (grant-co-financing combination);
4. The applying municipal government has the necessary borrowing capacity if funding is to be under loan financing;
5. Documentation available for the sub-project is sufficient for preparation of the SSR;
6. The proposed sub-project demonstrates positive expected impact on and/or involvement of vulnerable groups (defined as poor, IDPs, youth, ethnic minorities, women, elderly, disabled)
7. The proposed sub-project is designed the way to minimize needs for land acquisition, loss of assets, and relocation; and
8. The proposed sub-project falls under environmental Category A, or triggers World Bank's safeguard policies other than those triggered by the RMIDP II.

Step 3. MDF prepares SSR for all sub-projects and an SSR consists of the following:

1. Short description of the proposed sub-project
2. Investment plan (amount of proposed investment, structure)
3. Financial plan (loan amount, terms, grant amount, co-financing needs)
4. Description of all possible benefits
5. Information about implementation arrangements
6. Estimated impact to results framework indicators

Step 4. For the loan financing projects, MDF prepares a SAR. At this stage, a sub-project specific Environmental and Social Impact Assessment (ESIA) report including Environmental Management Plan (EMP), or a self-standing EMP as well as a sub-project specific Resettlement Action Plan, if required, shall be produced. If documentation is deemed insufficient to prepare SAR, MDF agrees with the municipal government on the scope, terms of reference and implementation conditions, and schedule of required feasibility, design, and other complementary studies and assessments required for project appraisal. In addition to the information set out under Step 4, SAR should provide information on a number of questions.

Step 5. If SSR and/or SAR is accepted by the MDF management board, MDF sends it to the WB (when a sub-project amount is more than 2.5 million USD).

Step 6. MDF prepares an Investment Financing Agreement (IFA) and forwards it to the municipal government for review. IFA for the project that requires SAR will be prepared upon WB's no objection to the SAR. MDF signs IFA with the municipal government.

The above information has been extracted from the OPERATIONS MANUAL of the MDF for the Second Regional and Municipal Infrastructure Development Project. the full document is available on the MDF website (http://mdf.org.ge) for downloading.

15 General Overview of International Public Sector Accounting Standards

Relevance

The information presented below is relevant to the order noted and additionally is utmost important in understanding the overall framework of International Public Sector Accounting Standards (IPSAS). Its fundamental knowledge is important in building an appreciation of the end product to which all accountants contribute, the financial statements of Georgia. Be acquainted with IPSAS is important. Being fully fluent in IPSAS is a technical function which requires in depth study beyond the scope of this Guidebook.

Order #429 of Minister of Finance of Georgia on approval of "accounting and financial reporting instructions for budgetary organizations" is based on IPSAS 2, IPSAS 3, IPSAS 4, IPSAS 6, IPSAS 13, IPSAS 19, IPSAS 22, IPSAS 23, IPSAS 24.

15.1 Background

International Public Sector Accounting Standards (IPSAS) are a set of accounting standards issued by the IPSAS Board for use by public sector entities around the world in the preparation of financial statements. These standards are based on International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB).

Accounting standards are the written statements consisting of rules and guidelines, issued by the accounting institutions, for the preparation of uniform and consistent financial statements and also for other disclosures affecting the different users of accounting information. Accounting standards are guidelines and harmonizer in the field of accounting process. They provide basis on which accounts are prepared and bring uniformity in accounting methods.

IPSAS aims to improve the quality of general-purpose financial reporting by public sector entities, leading to better informed assessments of the resource allocation decisions made by governments, thereby increasing transparency and accountability.

IPSAS are accounting standards for application by national governments, regional (e.g., state, provincial, territorial) governments, local (e.g. city, town) governments and related governmental entities (e.g. agencies, boards and commissions). IPSAS do not apply to government business enterprises, they are governed by IFRS.

In 2007 the Minister of Finance of Georgia decided to adopt IPSAS for central and sub-national governments, starting with the Cash-basis IPSAS, gradually adding disclosures about assets and liabilities in order to subsequently arrive at accrual accounting IPSAS. Governments that report on a cash basis do not account for significant liabilities, such as employee pensions and loans and assets such as property, plant and equipment and investments. In 2009 decision in principle was taken to publish IPSAS compliant financial statements for central and sub national levels of government by 2020. As of 2017, the central government remains preparing budget execution reports in accordance with the cash basis of accounting.

There are 38 standards on the accrual basis of accounting and one standard on the cash basis of accounting. 32 of these have been translated into Georgian and appear on the MoF web site (http://treasury.ge/5390)

Accrual-based IPSAS

Standard	Title of the standard
IPSAS 1	Presentation of Financial Statements
IPSAS 2	Cash Flow Statements
IPSAS 3	Accounting Policies, Changes in Accounting Estimates and Errors
IPSAS 4	Effects of Changes in Foreign Exchange Rates
IPSAS 5	Borrowing Costs
IPSAS 6	Consolidated and Separate Financial Statements
IPSAS 7	Investments in Associates
IPSAS 8	Interests in Joint Ventures
IPSAS 9	Revenue from Exchange Transactions
IPSAS 10	Financial Reporting in Hyperinflationary Economies
IPSAS 11	Construction Contracts
IPSAS 12	Inventories
IPSAS 13	Leases
IPSAS 14	Events after the Reporting Date
IPSAS 15	Financial Instruments: Disclosure and Presentation
IPSAS 16	Investment Property
IPSAS 17	Property, Plant and Equipment
IPSAS 18	Segment Reporting
IPSAS 19	Provisions, Contingent Liabilities, Contingent Assets
IPSAS 20	Related Party Disclosures
IPSAS 21	Impairment of Noncash-generating Assets
IPSAS 22	Disclosure of Financial Information about the General Government Sector
IPSAS 23	Revenue from Non-Exchange Transactions (Taxes and Transfers)
IPSAS 24	Presentation of Budget Information in Financial Statements
IPSAS 25	Employee Benefits
IPSAS 26	Impairment of Cash-Generating Assets
IPSAS 27	Agriculture
IPSAS 28	Financial Instruments: Presentation
IPSAS 29	Financial Instruments: Recognition and Measurement
IPSAS 30	Financial Instruments: Disclosures
IPSAS 31	Intangible Assets
IPSAS 32	Service Concession Arrangements: Grantor
IPSAS 33	First-time Adoption of Accrual Basis IPSAS
IPSAS 34	Separate Financial Statements
IPSAS 35	Consolidated Financial Statements
IPSAS 36	Investments in Associates and Joint Ventures
IPSAS 37	Joint Arrangements
IPSAS 38	Disclosure of Interests in Other Entities

Cash-based IPSAS

Standard	Title of the standard
Cash Basis	IPSAS Financial Reporting Under the Cash Basis of Accounting

When the cash basis of accounting underlies the preparation of the financial statements, the primary financial statement is

- ✓ The Statement of Cash Receipts and Payments

When the accrual basis of accounting underlies the preparation of the financial statements, the financial statements will include:

- ✓ The Statement of Financial Position (IPSAS 1),
- ✓ The Statement of Financial Performance (IPSAS 1),
- ✓ The Cash Flow Statement (IPSAS 2),
- ✓ The Statement of Changes in Net Assets/Equity (IPSAS 1),
- ✓ The Notes to the Financial Statements, Or Annex (IPSAS 1

15.2 IPSAS Financial Reporting using Cash Based Accounting

Cash basis

- ✓ Expenses and revenues are recorded when they are paid or received
- ✓ Allows for transparent financial reporting of cash receipts, payments and balances, under the cash basis of accounting.

Accrual basis

- ✓ Expenses and revenues are recorded when they are incurred or earned
- ✓ Focuses on revenue, cost, assets, liability and equity, instead of cash flow only.

This Standard applies to all public sector entities other than Government Business Enterprises which are profit oriented and use IFRS.

Government Business Enterprises (GBE) means an the LSG that has all the following characteristics:

- ✓ Is an the LSG with the power to contract in its own name;
- ✓ Has been assigned the financial and operational authority to carry on a business;
- ✓ Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery;
- ✓ Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and
- ✓ is controlled by a public sector the LSG

Financial statements prepared under the cash basis provide readers with information about the sources of cash raised during the period, the purposes for which cash was used and the cash balances at the reporting date. Notes to the financial statements may provide additional information about liabilities, such as payables and borrowings, and some non-cash assets, such as receivables, investments and property, plant and equipment.

This Standard comprises two parts (I & II):

Part 1 is Mandatory:

- ✓ It sets out the requirements which are applicable to all entities preparing general purpose financial statements under the cash basis of accounting.
- ✓ It defines the cash basis of accounting, establishes requirements for the disclosure of information in the financial statements and supporting notes, and deals with other specific reporting issues.

Part 2 is not mandatory.

- ✓ It identifies additional accounting policies and disclosures that an the LSG is encouraged to adopt to enhance its financial accountability and the transparency of its financial statements.

Mandatory

- ✓ Consolidated Statement of Cash Receipts and Payments
  - recognizes all cash receipts, cash payments and cash balances controlled by the LSG ;
  - separately identifies payments made by third parties on behalf of the LSG.
- ✓ Statement of Comparison of Budget and Actual Amounts
  - Comparative information should be disclosed in respect of the previous period for all numerical information required by this Standard.
  - Comparative information should be included in narrative and descriptive information when it is relevant for understanding of the current period's financial statements.
- ✓ Notes to Financial Statements
  - Present information about the basis of preparation of the financial statements and the specific accounting policies selected and applied or significant transactions and other events;
  - Provide additional information which is not presented on the face of the financial statements but is necessary for a fair presentation of the LSG's cash receipts, cash payments and cash balances.
  - Shall be fully cross referenced

Voluntary

- ✓ Statement of Cash Assets and Fund Balances
- ✓ Notes – Additional expository
- ✓ Statement of Outstanding Invoices (Liabilities)
- ✓ Statement of Unjustified Advances and Loans
- ✓ Non-financial assets disclosure notes
- ✓ Statement of Contingent Liabilities

A comprehensive study of the IPSAS requires significant time. It is beyond the goal of this PFM-GB to provide this information. However, a review and analysis of the operating activities and baseline skills for the local self-government indicated that the following IPSAS are relevant and a basic understanding of them should be conveyed;

15.3 IPSAS 1 - Presentation of Financial Statements

This chapter sets out the overall requirements for general purpose financial statements prepared under the accrual principle, including guidance for their structure and minimum requirements for the content of financial statements. General purpose financial statements are the statements intended to serve users who are not in a position to demand financial reports tailored to their particular information needs. The standard applies to all public sector entities other than GBEs (Government Business Enterprises). The objective of general-purpose financial statements is to provide information about the financial position, financial performance, and cash flow of an the LSG that is useful to a wide range of users in making and evaluating decisions about allocating resources.

The standard requires a complete set of financial statements to comprise:

- ✓ A Statement of Financial Position
- ✓ A Statement of Financial Performance
- ✓ A Statement of Changes in Net Assets/Equity
- ✓ A Statement of Cash Flows
- ✓ Notes, Comprising a Summary of Accounting Policies and other Explanatory Notes
- ✓ A Comparison of Budget and Actual Amounts (if Approved Budget is made public)

15.4 IPSAS 24 - Presentation of Budget Information in Financial Statements

The standard requires to make a comparison and to provide explanations for material differences between approved budget and actual information. Compliance with the requirements of the standard ensures that public sector entities discharge their accountability obligations and enhance the transparency of their financial statements by demonstrating compliance with the approved budget for which they are held publicly accountable and, where the budget and the financial statements are prepared on the same basis, their financial performance in achieving the budgeted results.

Key definitions

Original budget: the initial approved budget for the budget period.

Approved budget: the expenditure authority derived from laws, appropriation bills, government ordinances, and other decisions related to the anticipated revenue or receipts for the budgetary period.

Final budget: the original budget adjusted for all reserves, carry-over amounts, transfers, allocations, supplemental appropriations, and other authorized legislative, or similar authority changes applicable to the budget period.

An explanation should be presented of whether changes between the original and final budget a consequence of reallocations within the budget are, or of other factors. All comparisons of budget and actual amounts should be presented on a comparable basis to the budget. The notes to the financial statements should include details about 1) the budgetary basis and classification basis adopted in the approved budget 2) the period of the approved budget and 3) the entities included in the approved budget.

If the financial statements and the budget are not prepared on a comparable basis, actual amounts that are presented on a comparable basis to the budget should be reconciled to the following actual amounts presented in the financial statements, identifying separately any basis, timing and the LSG differences. Comparative information for the previous period is not required.

15.5 IPSAS 6 - Consolidated and Separate Financial Statements

This standard applies to entities that prepare and present financial statements under the accrual basis of accounting. Applies to all public sector entities other than GBEs. It prescribes when an the LSG must consolidate another the LSG and includes guidance to assess control and furthermore includes guidance for the preparation of separate financial statements and disclosures.

Balances, transactions, revenues and expenses between entities within the economic the LSG should be eliminated in full. The financial statements of the controlling and the controlled entities should be prepared on the same reporting date for consolidation purposes. If different reporting dates are used, the difference cannot exceed three months and adjustments for significant transactions and events should be made.

Minority interests are reported in net assets/equity in the consolidated statement of financial position, separately from the controlling the LSG 's net assets/equity.

Control is a matter of judgment based on the definition of control and the particular circumstances of each specific case. The two elements of control have to be taken into account; these are:

- ✓ the power element, the power to govern the financial and operating policies of the LSG
- ✓ the benefit element, ability to control the LSG to benefit from its activities

The power to control does not require the majority of the shareholding or the responsibility for the management. The power to control must be presently exercisable (i.e. it is derived from a legislation or an agreement).

Control is presumed to exist in case of following power indicators:

- ✓ the LSG has, directly or indirectly through controlled entities, ownership of a majority voting interest in the other the LSG.
- ✓ the LSG has the power, either granted by or exercised within existing legislation, to appoint or remove a majority of the members of the board of directors or equivalent governing body, and control of the other the LSG is by that board or by that body.
- ✓ the LSG has the power to cast, or regulate the casting of, a majority of the votes that are likely to be cast at a general meeting of the other the LSG.
- ✓ the LSG has the power to cast the majority of votes at meetings of the board of directors or equivalent governing body, and control of the other the LSG is by that board or by that body unless there is clear evidence that another the LSG holds control.

Control is presumed to exist in case of following benefit indicators:

- ✓ the LSG has the power to dissolve the other the LSG and obtain a significant level of the residual economic benefits or bear significant obligations. For example, the benefit condition may be met if an the LSG had responsibility for the residual liabilities of another the LSG.

- ✓ the LSG has the power to extract distributions of assets from the other the LSG, and/or may be liable for certain obligations of the other the LSG, unless there is clear evidence that another the LSG holds control.

15.6 IPSAS 33 - First-time Adoption of Accrual Based IPSAS

This standard grants transitional exemptions to entities adopting accrual-based IPSAS for the first time. The standard distinguishes between two kinds of transitional exemptions:

1. Transitional exemptions that do not affect fair presentation and compliance with accrual-based IPSAS during the period of adoption
2. Transitional exemptions that affect fair presentation and compliance with accrual-based IPSASs during the period of transition.

Of note, IPSAS 33:

- ✓ allows first-time adopters three years to recognize specified assets and liabilities. This provision allows sufficient time to develop reliable models for recognizing and measuring assets and liabilities during the transition period;
- ✓ addresses situations when reliable historical cost information about assets and liabilities is not available; and
- ✓ addresses the presentation of comparative information in transitional IPSAS financial statements and an the LSG 's first IPSAS-compliant financial statements.

For the presentation of comparative information on first-time adoption, IPSAS 33 encourages (but does not require) entities to provide comparative information in their transitional IPSAS financial statements or their first IPSAS financial statements. Disclosures should be made to assist users in tracking progress upon adoption and identifying possible deviations from IPSAS accounting policies during transition.

An the LSG that has applied the cash basis of accounting in its previous financial statements is not required to present:

A) A reconciliation of its net assets/equity reported in accordance with its previous basis of accounting to its opening balance of net assets/equity at the date of adoption of IPSASs

B) A reconciliation of its surplus or deficit in accordance with its previous basis of accounting to its opening balance of surplus or deficit at the date of adoption of IPSASs.

15.7 IPSAS 17 - Property, Plant and Equipment

Generally, property, plant and equipment are initially measured at its cost except when the property, plant or equipment is derived from a non-exchange transaction, than it is initially measured at fair value. Subsequently property, plant and equipment are measured either using a cost or revaluation model and depreciated so that its depreciable amount is allocated on a systematic basis over its useful life. Impairment testing should be performed at least once a year at the annual reporting date. This standard applies to entities that prepare and present financial statements under the accrual basis of accounting and applies to all public sector entities other than GBEs.

Key definitions:

Property, Plant and Equipment in the context of the Public Sector: Property, plant and equipment are assets held for use in the production or supply of goods and services rental to others or administrative purposes and are expected to be used more than one year. In the public sector context these assets can be cash-generating or non-cash generating, heritage assets (monuments, artworks, historical buildings, etc.), infrastructure (roads, water and power supply networks, sewerage, etc.)

Depreciable amount: the cost of an asset, or other amount substituted for cost, less its residual value.

Depreciation: Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

Recoverable amount: for a cash-generating asset, the higher of: A) the fair value less costs to sell or B) the value in use.

Recoverable service amount: for a non-cash-generating asset, the higher of: A) the fair value less costs to sell B) the value in use

Impairment loss: the excess of the carrying amount over the recoverable (service) amount

Property, plant and equipment is initially measured: A) at cost, including any transaction costs or B) at fair value, if the asset is acquired through a non-exchange transaction

Cost is the amount of cash paid or the fair value of other assets given (exchange of assets) to acquire an asset. Discounting may be needed if payment is deferred.

For Subsequent Measurement IPSAS 17 permits the application of two models : A) the fair value model ("the revaluation model") or B) the cost model.

If the fair value model is applied, the item of PPE is carried at a revalued amount, being its fair value at the date of revaluation less subsequent depreciation and impairment losses. Revaluations should be performed on a regular basis to ensure that the carrying amount is not materially different from the fair value at the reporting date.

If the cost model is elected by the LSG, the item of property, plant and equipment is subsequently carried at cost less accumulated depreciation and less accumulated impairment losses.

One accounting policy shall be elected by the LSG for each significant class of property, plant and equipment and apply this policy to the whole entire class.

The residual value and the useful life of an item of PPE should be reviewed at least at each annual reporting date and when expectations differ from earlier estimates, any change should be treated as a change in accounting estimate.

When an item of PPE is impaired (i.e. recoverable amount < carrying amount), the carrying amount is reduced to the amount of the recoverable amount. This decrease of the carrying amount is an impairment and is recognized in surplus or deficit. After recognition of an impairment loss, the depreciation charge of the asset shall be adjusted in future periods to allocate the asset's revised carrying amount over its remaining useful life.

An item of PPE should be derecognized: A) on disposal or B) when no future economic benefits are expected from its use or disposal. Gain or loss is the difference between the payment received (discounted if payment is deferred) and the carrying amount of the item. Gains or losses are recognized in surplus or deficit.

The following disclosures are required for each class of property, plant, and equipment:

- ✓ basis for measuring gross carrying amount
- ✓ depreciation method applied
- ✓ useful lives or depreciation rates
- ✓ gross carrying amount and accumulated depreciation and impairment losses at beginning and end of the period
- ✓ reconciliation of the carrying amount at the beginning and the end of the period, showing:
  - additions
  - disposals
  - acquisitions through entity combinations
  - revaluation increases or decreases
  - impairment losses
  - reversals of impairment losses
  - depreciation
  - net exchange differences
  - other changes

15.8 IPSAS 21 - Impairment of Noncash-Generating Assets

Key definitions:

Impairment: a loss in the future economic benefits or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation.

Cash-generating assets: assets held with the primary objective of generating a commercial return.

Non-cash-generating assets: assets other than cash-generating assets.

Recoverable service amount: the higher of a non-cash-generating asset's fair value less costs to sell and its value in use.

Value in use of a non-cash-generating asset is the present value of the asset's remaining service potential.

This standard describes procedures to ensure that an asset's carrying amount does not exceed its recoverable amount (i.e. the higher of fair value less costs to sell and value in use). With the exception of intangible assets with an indefinite useful life or intangibles not yet available for use, for which an annual impairment test is required, entities are required to conduct impairment tests when an indication of impairment of an asset exists**.**

A non-cash generating asset is impaired when its carrying amount exceeds its recoverable service amount.

At each reporting date the LSG has to assess that indicators of an asset that might be impaired exist. If such indicators exist, the LSG should estimate the recoverable amount of the asset. The test should be performed at any time during the reporting period provided that it is performed at the same time each year.

Following external and internal indicators of impairment are included in the standard [IPSAS 21.27]:

External:

- ✓ Substantial decline in, or (near) cessation of the demand or need for services provided by the asset
- ✓ Negative changes in the technological, legal, or government policy environment

Internal:

- ✓ physical damage of an asset;
- ✓ Asset is idle, or a decline or expected decline in the use of an asset as part of plans to discontinue, restructure or dispose the asset
- ✓ decision to halt the construction of the asset before it is complete or in a usable condition
- ✓ worse than expected service performance of an asset

The list of indicators in not intended to be exhaustive, other indicators of impairment may exist.

An impairment loss is recognized: A) whenever the recoverable service amount is below its carrying amount B) as an expense in the statement of financial performance/in surplus or deficit. A liability should be recognized when the impairment loss exceeds the carrying amount of the asset if this is required by another IPSAS. Depreciation for future periods should be adjusted

The reversal of the impairment loss will increase the carrying amount which will not exceed the depreciated (or amortized) carrying amount if no impairment loss would have been recognized. The reversal of the impairment loss will be recognized in surplus or deficit (Statement of Financial Position). Depreciation for future periods should be adjusted.

15.9 IPSAS 26 - Impairment of Cash-Generating Assets

Value in use of a cash-generating asset: the present value of the estimated future cash flows expected to be derived from the continuing use of an asset and from its disposal at the end of its useful life.

The calculation of value in use must reflect following elements

- ✓ an estimate of the future cash flows the LSG expects to derive from the asset;
- ✓ expectations about possible variations in the amount or timing of those future cash flows;
- ✓ the time value of money, represented by the current market risk-free rate of interest;
- ✓ the price for bearing the uncertainty inherent in the asset;
- ✓ other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the LSG expects to derive from the asset.

Cash flow projections should be based on:

- ✓ reasonable and supportable assumptions;
- ✓ the most recent budgets and forecasts;
- ✓ extrapolation for periods beyond budgets and forecasts.

Estimates of future cash flows should include:

- ✓ Projections of cash inflows from the continuing use of the asset;
- ✓ Projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and
- ✓ Net cash flows, if any, to be received (or paid) for the disposal of the asset at the end of its useful life.

Cash flow estimates should be based on the asset's current condition – future restructurings to which the LSG is not committed and expenditures to improve or enhance the asset's performance should not be anticipated. Estimates of cash flows should not include cash inflows or outflows from financing activities, or income tax receipts or payments.

In measuring value in use, the discount rate used should be the pre-tax rate that reflects A) current market assessments of the time value of money and B) the risks specific to the asset.

An impairment loss is recognized:

- ✓ whenever the recoverable amount is below its carrying amount;
- ✓ as an expense in the statement of financial performance/in surplus or deficit.

A liability should be recognized when the impairment loss exceeds the carrying amount of the asset if this is required by another IPSAS.

Depreciation for future periods should be adjusted.

When impairment losses recognized (reversed) are material in aggregate (but not individually disclosed as described above) to the financial statements as a whole, disclose:

- ✓ main classes of assets affected;
- ✓ main events and circumstances resulting in the (reversal) impairment loss.

16 BUDGETING

Relevance

A budget is an estimate of future income and expenditure for achieving the financial and operation goals of the local authority. It is an essential tool for effective financial control. Budgeting allows a local government to evaluate its needs in light of the revenue sources available to meet those needs. A complete budget justifies the imposition of fees and taxes as well as the making of the appropriations that give the government its authority to spend public money.

Budgeting is not simply something a local government does once every year or two. It is a continuous process; the budgeting process has four parts. The budget is: 1) prepared, 2) approved, 3) adopted, and 4) executed. After adopting the budget, the governing body makes the necessary appropriations and certifies to the county assessor the tax to be imposed.

Citizen involvement in the budget cycle is encouraged. It is up to each local government to prepare a budget that clearly outlines its fiscal policies for all interested parties. If a budget is clear and concise, taxpayers have a better understanding of what services their tax dollars are buying. Local govern-ments may find citizen input informative and rewarding.

16.1 Background

A budget is a financial plan that includes estimates of expenditures and revenues for a single fiscal year. The budget should be governed by several principles, including transparency, accountability, participation. The principle of transparency is important in the budget process, as it allows for informed analysis of government policies and facilitates the identification of weaknesses, leading to the implementation of needed reforms. Transparency can increase faith in the government. Effective participation can serve to ensure efficient provision and more equitable distribution of budgetary allocations. Accountability regarding the budget has several dimensions: accountability for objects of expenditure, performance and results (achieving results or meeting objectives for which public funds are spent), and budget processes that result in best value, quality and service for public money.

The local budgeting process provides procedures for evaluating a local government's needs and identi-fying revenue sources to meet those needs. A completed budget provides a means of controlling expenditures and a justification for imposing property taxes. The budgeting process is actually in three parts: The budget is prepared, approved, and finally adopted.

A local government's budget is a public document. Anything connected with the budget is subject to public inspection. The budget is a guide to the financial management of the local government. It provides information that encourages public participation in government. The detail of the budget should take into account common sense to make the document as informative and uncomplicated as possible.

16.2 Budget Message

A budget instruction is prepared annually by the senior executive officer i.e. Mayor. The extent of the budget instruction depends upon the size and complexity of the budget, and any changes in fiscal policy or financial position since the preceding year. The budget instruction is delivered to the budget committee at its first meeting. The budget instructions must be in writing, since it is a part of the complete budget document (please see Guidebook for Effective Program and Performance-based Budgeting, Appendix C for example of Mayor's budget instructions).

The budget instructions must:

- Explain the budget document.
- Include a brief description of the proposed financial policies for the coming fiscal year.
- Describe the important features of the budget document in connection with the financial policies of the local government.
- Explain the reason for changes from the previous year in appropriation and revenue items.
- Explain the major changes in financial policy.

16.3 Budget Calendar

The budget calendar will be based on the sequence of events that influence budget-making. The first step in the budget calendar is for budget committee members to be appointed and budget committee meetings, hearings, and publication of notices to be scheduled, along with a schedule for audit review and financial reporting. Since budget calendars are built around mandated requirements, it must be reviewed and revised if the laws change. The budget committee is a local government's fiscal planning advisory committee and its members should develop a general understanding of the budget process, the departments or programs included in the budget document, and the legal constraints imposed on the local government's tax, fees and license levies. The committee generally studies the budget by comparing the two previous years' actual data, the current budgeted data, and the figures proposed by the budget. The budget committee may reduce or increase the estimates of resources and requirements proposed by the budget. The committee may approve the budget at the first meeting. However, it could take several meetings to do so. Once the budget committee has approved the budget, it has completed all of the duties required of it. After the budget committee approves the budget, it is turned over to the governing body and the process enters into the adoption stage. The governing body has the final responsibility for allocating the resources of the budget to the programs and departments of the local government.

Sample budget calendar

1. Appoint budget officer and budget committee
2. Prepare proposed budget
3. Publish 1st notice of budget committee meeting
4. Publish 2nd newspaper notice of budget committee meeting at least 5 days before the meeting,
5. Budget committee meeting
6. Second budget committee meeting (if needed)
7. Publish notice of budget hearing 5 to 30 days before the hearing
8. Hold budget hearing
9. Board meeting to enact resolutions to adopt budget, make appropriations, impose taxes and fees

16.4 Estimating Budget Resources (Revenues) and Requirements (Expenditures)

Each LSG shall estimate in detail its budget resources for the ensuing year by funds and sources. Generally, an "estimate" is defined as an approximate calculation or an opinion formed from imperfect data. All resource and requirement estimates should be based on "good faith." That is, they should be reasonable and be reasonably likely to prove correct, based on the known facts at the time.

All known resources and requirements must be included in the budget. The only exception is if the following are true: (a) The LSG holds the resources merely for safekeeping; or (b) Expenditure of the resources is not under the control of the LSG or a third party chosen by the LSG.

Expenditures (requirements) generally are broken down first by fund, then by organizational unit or program, and then, more specifically, by object classification and object. Revenues (resources) are broken down by fund. Expenditure is classified in two ways in the Government Financial Statistics (GFS), i.e. either according to its function, or according to its economic characteristic. Expenditure is divided into four broad categories (economic classifications), namely current payments, transfers and subsidies, payments for capital assets and payments for financial assets:

1. Current payments: These are payments made by departments for their operational requirements. This includes personnel expenditure and expenditure for goods and services, including salaries, which are

expended within a short period of time, usually a year. This excludes purchases of capital assets or goods and services for the production of capital assets.

2. Transfers and subsidies: These are transactions in which a department passes funds to another institution or to an individual for final spending. Transfers and subsidies include current as well as capital expenditure. An example of this expenditure includes transfers to research institutions and conditional grants to provinces and municipalities.
3. Payments for capital assets: This reflects spending on assets with a productivity of more than one year, including the maintenance of such an asset. Payments for capital assets cover the purchases of new assets, as well as extensions and improvements to existing assets.
4. Payments for financial assets: This consists of payments made by a department as loans to public corporations or as equity investments in public corporations.

Should a reduction in the budget be planned, i.e., lower than previous year's actual expenditure, there must be specific actions and measures to generate this cost-saving and these are shown as part of the explanatory documents.

A fund is a fiscal and accounting entity with self-balancing accounts set aside to carry on a specific activity or to meet certain objectives in accordance with a specific regulation. The requirements and resources of a fund must always balance. Every budget has at least one fund (commonly called the General Fund) which is used for everyday operation of the local government.

Depending on the size and complexity of local government and the services it provides, it may also have a number of special funds. The most common reason for establishing a special fund is to account for a revenue source whose use is limited to a particular kind of expenditure.

Some funds are broken down to account for one or more organizational units or activities, which are merely subdivisions of a fund. An organizational unit might be a department, office, or division.

16.5 Program Budgets

Budget requirements must be prepared by program. Programs are groups of activities to accomplish a major service or function. Estimates for each program must be arranged by activity and then put into separate object classifications. The departmental budget is allocated by program, economic classification and standard item. Each program is divided into sub-programs and line items. Program budgeting considers the appropriateness of the policy goals or outcomes. It strengthens the link between strategic planning and budgeting.

The following provides a brief overview of the budget classification by program:

- Program budget: a program is structured around certain departmental functions. Program budgeting reflects policy development and departmental priorities. More funds are allocated to the programs that are designed to implement and address top government priorities. This also reflects the reprioritization (changes in the division of expenditure between programs) and highlights changes in the program structure of the department.
- Sub-programs: This is a sub-division of departmental programs into compatible activities. Program budgeting is further allocated to sub-programs, which collectively function to attain the objectives of

the main program. As with program budgeting, funds are allocated according to prioritized sub-programs.

16.6 Budget Changes After Adoption

After the beginning of the fiscal year, when a local government is operating with the adopted budget, changes in appropriated expenditures sometimes become necessary. Appropriations may be increased or decreased, transferred from one appropriation category to another, or new appropriation categories created. The method used to amend the budget is determined by the budgetary change needed. If the change involves a new fund or a new appropriation category, a supplemental budget is usually required. If the change is a transfer of appropriation authority (and the corresponding resources) from one fund to another, or within the same fund, then a resolution transfer is allowed.

A supplemental budget is most often required when new appropriation authority is needed. For example, circumstances may require expenditures that were not budgeted, or revenue which was not plan for in the budget is to be spent in the current fiscal year. A supplemental budget is usually not required if appropriations are not being changed. Supplemental budgets are good only through the end of the fiscal year in which they are adopted.

16.7 Overview of Budget Analysis

Budget analysis is an effective tool for detecting irregularities in government spending. Discrepancies in revenue and expenditure can be brought to notice in this way. It becomes easy to monitor government expenditure. The timing of budget analysis is critical when it comes to engaging with policy makers. Budget analysis further holds government, elected and appointed officials accountable to their stated policy priorities. Budget analysis has an immediate and measurable impact.

Managers must receive suitable budget reports each month. The reports must display the value of budget orders executed but not yet expended in addition to the amount of budget achieved. Managers must be given further information promptly when requested. Managers should be required to explain the differences between the agreed budget profile and the actual expenditure. Explanations must be provided in writing.

There are three main types of budget analysis: revenue-focused analysis, budget allocation analysis and budget expenditure analysis. Revenue focused analyses examine how local-self-governments generate income, pointing to areas in which the government is missing opportunities to generate revenue. Budget allocation analysis considers the budgetary characteristics of commitments to see if governments are fulfilling their obligations. Budget expenditure analysis compares budget allocation to actual spending.

16.8 Performing Budget Variance Analysis

To calculate a static budget variance, simply subtract the actual spend from the planned budget for each line item over the given time period. Divide by the original budget to calculate the percentage variance. A budget variance is the difference between the budgeted or baseline amount of expense or revenue, and the actual amount.

The purpose of all variance analysis is to provoke questions such as:

- Why did one operation or service perform better (or worse) than the others?
- Why are expenses higher or income lower than last year?

- Are variances being caused by execution failure, change in conditions, external actions, an unexpected event or unrealistic forecast?

The need and importance of variance analysis:

- Variance analysis aids efficient budgeting activity as management wishes to have lower deviations from the planned budgets. Wanting a lower deviation usually leads managers to make detailed and forward-looking budgetary decisions.
- Variance analysis acts as a control mechanism. Analysis of large deviation on key items helps the LSG in knowing the causes and it helps management look into possible ways of how such deviation can be avoided.
- Variance analysis facilitates assigning responsibility and engages control mechanism on departments where it is required

Variances fall into two major categories:

- Favorable variance: Actuals came in better than the measure it is compared to.
- Negative variance: Actuals came in worse than the measure it is compared to.

Budget variances can occur from controlled or uncontrollable factors. There are three primary causes of budget variance: errors, changing business conditions and unmet expectations Proper variance analysis requires some thought:

1. Identifying the causes.

   No accounting function is likely to know the cause of the variances. The finance department has a role to quantify the impact, but it is operational managers who should know why and only they should provide input into the management report on the figures. Without knowing the true cause, effective management decisions on the appropriate action are impossible

2. Taking appropriate action
   A. What is the cause, and will it happen again?
   B. What is the financial effect?
   C. What is being done or to be done
   D. Are there implications for other activities?

17 Linking Program Budgeting with Financial Management

Relevance

Linking program budgeting with financial management is moving from line-item to budgeting which enables understanding how government policies translate into spending. A LSG can be viewed as carrying out its responsibilities by way of five basic and sequential steps. 1) Planning; 2) Programming; 3) Budgeting; 4) Operations/Implementing; and 5) Evaluations. Each of these steps consists of a distinct, but interrelated function in the overall conduct of the LSG. Under line-item budgeting, it is know what inputs are being purchased, however there is often an absence of clear indication of what activities, purposes, or objectives -- or ultimately outputs or outcomes -- are being purchased, or how government policies translate into spending.

To be of full use, a program needs to connect the inputs with the objectives of spending. It means having some ability to allocate costs to programs on a reasonable basis so that the full costs of each program are reflected with the program. The program budget concept should integrate recurrent and capital budgets. The concept of a program---activities leading to a common purpose or objective ---necessitates thinking in terms of a production function. All inputs leading to the output or outcome need to be taken into the budget. This will entail direct labor, indirect costs and capital.

The "Guidebook for Effective Program and Performance-based Budgeting" should be read to obtain a comprehensive understanding of the subject area. This will ensure that there is a higher level of cognizance of the how financial accounting and program budgeting must be viewed as integrated elements so that they can contribute towards good financial management.

18.1 Background

Program budgeting is framework that streamlines resource allocation decisions, it is as well a vehicle for making performance management operational in the public sector. It provides a tool of policy analysis, allowing for comparison and evaluation of the cost-effectiveness of alternative spending options that have the same objective. Additionally, it is a way of improving government performance by creating ownership and accountability in managers. Furthermore, when integrated properly with bookkeeping practices and procedure it is a means of facilitating accounting for the full cost of government activities.

The program budgeting structure must incorporate two classification schemes that both serve important but essentially different purposes: the program classification and the organizational unit classification. It is at this point where program budgeting and financial accounting become interrelated. Organizational units are departments or similar functional units, it is here that accounting is performed on based upon the nature of the transactions i.e. type of revenue or expense.

18.2 Program Budgeting and Financial Accounting

Program based accounting has start and end dates – because programs have start and end dates. A Program-based budget starts when the program starts and ends when the program ends. The accounting work ends when the program moves through closure. Financial accounting is different, it is based on periods in a financial year, which may be shorter than the project life. Reporting in program based accounting is based on deliverables. Tracking spend against a certain milestone or various deliverables. Costs are tied back to the things being done; the work produced, and the outputs created. In financial accounting, reports don't relate to deliverables. Financial accounting hierarchies are based on departments and cost centers. Project accounting hierarchies are based on tasks and projects. Project costs relate to costs generated by deliverables and project activities.

So that a program-based accounting process is provides the most useful and accurate information procedures should be implemented to maximize the direct charging of items to programs and minimize those items which are allocated. This can be done by improving tracking requirement at a program transactional level. This means that the cost must be evaluated to be either direct costs or indirect costs.

Direct costs are those effectively controlled by the organization to which they are charged. Thus, wages and salaries, pensions and health benefits of public employees who work on particular activities, should be charged to programs that they work on. Indirect costs are costs that are not directly accountable to a cost object (such as a particular project, facility, function or product). Indirect costs may be either fixed or variable costs. For example, the expense of running departmental headquarters. These indirect costs are not controlled by operating units; hence they should not be charged for them. It would be counterproductive to allocate indirect and overhead costs. Doing so would have the effect of charging managers for costs they do not control.

It is very important to have clear definitions of direct and indirect costs. Project managers must be provided with program costs statements regularly. These activity reports must be scrutinized carefully. To have a proper Program Budgeting system in place, there has to be a proper program accounting system functioning. Often times there are “suspense” accounts used to capture unallocated costs. These accounts must be reviewed regularly. Managers must be diligent that accounting personnel allocate costs to projects correctly. Program Budget personnel must exercise care to ensure that the costs charged to their programs are correctly charged. Program budget personnel must be proactive to ensure that costs are properly accounted for and on a timely basis.

18 The Internal Control System and Process

Relevance

Fundamental to achieving the key initiatives and goals of the LSG is proper functioning internal control. Using controls properly prevents loss of resources, including capital assets, stores, proprietary information and cash. It also ensures compliance with applicable laws and regulations and good governance practices.

Weak internal control consequences can range from erroneous or imperfect information to the waste, abuse or misuse of assets, and even to embezzlement. Weak internal control means poor efficiency, effectiveness as well as the absence of economical used of resources. The most dangerous aspect of a weak internal control system is that it stimulates the absence of responsibility. Ethical behavior drops where internal controls are absent. People who feel that they cannot be held accountable often operate as if they are not accountable, their moral compass becomes weak and their behavior becomes self-serving. When adverse events occur, such as theft or a severe failure it can be challenging to identify the root cause and determine who may be responsible. As a result, innocent people may be under suspicion and time wasted. Healthy controls can help to identify who or what went wrong and what corrective actions are needed. On a more general level a lack of accountability can result in the erosion of public confidence and support. Moreover, this hinder the ability to serve the public effectively.

18.1 Background

The internal control process is supported by a commitment from all levels within the LSG. To succeed the government must manage its operations effectively. Internal control helps to bring order, direction and consistency to daily activities. Internal controls also demonstrate the value of programs and the reporting on accomplishments. An effective system of internal control provides managers the means to specify accountability for programs and to track established goals.

The processes of internal control must include functional and operational analysis, development of control procedures and techniques, communication and monitoring.

Functional analysis is required for the evaluation of risks and determination of the appropriate control objectives. Also, a cost versus benefit analysis must be performed to verify the cost of a control does not exceed its benefit. Based on the operational analysis, individualized control techniques or procedures are either developed when absent or revised when necessary. Once in place, the control activities must be monitored and evaluated. This can be realized through self-audits, internal audits and external audits. The feedback provided can be used to improve the internal control system further.

ISO 31000:2018, on "Risk Management" contains the generally accepted definition of "Risk," which is the possibility that some specified event will occur and that this will threaten or otherwise adversely affect the achievement of objectives. Objectives are formulated using mission statements, strategic plan and performance goals. Targets must be unambiguously defined so that identification of risks and determine risk tolerances can be undertaken.

Internal control mechanisms must be in place to anticipate, identify and react to risks presented by changes. These include:

A) Regular review of financial reports and preparation of management analysis statements
B) Periodic physical visits to all operating areas of the organization of significance
C) Prompt resolution of issues raised by auditors and other authorities

Internal controls can be grouped into one of the three groups. The groups are sequential in their approach. Level 1 controls come logically before Level 2 and Level 3 follows on after a transaction has passed through "defeated" both Level 1 and Level 2 controls. Each level builds on the prior, therefore all levels must be considered as one interactive unit.

Definition of Levels:

1. PREVENTIVE CONTROLS: Are designed to stop an adverse action from occurring initially
2. DETECTIVE CONTROLS: Help to catch any adverse reaction or violation after it has happened.
3. CORRECTIVE CONTROL: These put into place to correct any errors that were found by the detective controls.

18.2 Risk Assessment and Risk Management

Risk assessment involves a repetitive procedure for identifying and analyzing threats. The evaluation forms a basis for determining how risks should be managed. Those persons conducting a risk assessment must consider possible changes in the external environment and within that may impede the achievement of objectives. For each risk that is identified, management is ultimately responsible for selecting one of three possibilities and moving forward.

The three possibilities are:

1. Accept the risk,
2. Reduce the risk to an acceptable level
3. Avoid the risk.

Risk tolerance as defined by ISO 31000:2018 on "Risk Management is acceptable variation in performance relative to the achievement of objectives. Only management can determine the risk tolerances defined goals for the organization they are accountable for. Risk tolerance cannot be applied to compliance because there is either compliance or not. Risk tolerances must be established using terms similar to those used when establishing performance measures. As an example where accuracy is a performance measure of an objective then risk tolerance is defined as an acceptable percentage of error rate either monetary or non-monetary. The establishment of levels of variation for performance measures helps to ensure that appropriate internal control system is designed.

When developing risk management, those people responsible for implementation need initially to comprehensively identify objectives for every programme and unit. This must include: #1 the goals of the operations in the short, medium and long term, #2 reporting requirements in detail and #3 compliance requirements at all levels. Objectives must be sufficiently specific to provide direction for managing functions and should be stated in terms which pin responsibilities to names. After identifying all objectives, every risk to each must be documented. Threats may be either internal, external or a mixture.

It is absolutely essential that all risks associated with each objective be identified.

Every risk must be evaluated for the impact and probability of happening. These two factors combined allow for rating each of the identified risk. In risk management, these terms are applied in the following manner:

- "Impact" The effect an unfavorable event would have on achieving objectives. This effect could be some type of negative momentary or non-monetary result or the loss of an opportunity. The extent of the impact is also affected by how quickly an event may happen or speed of dispersion and its duration. If possible, consequences should be quantified in units of currency or described in terms sufficiently specific to point out the significance of the risk.
- "Probability of Occurrence." The probability that an adverse impact event would occur if there were control activities to avoid, contain or prevent the incident. The possibility of occurrence must be estimated for each identified risk.

The LSG senior management of the entity must specify the amount of risk willing to be accepted about achieving objectives thereby effectively quantifying tolerance for these risks. Executive judgment must be used to establish priorities for risks based on the impact and the probability of occurrence. A ranking of risks applying must be made in an objective and logical process from most significant (high impact) and most probable to occur (high likelihood) to the least significant (low impact) and least likely (low probability).

Government entities because they are fulfilling social needs usually cannot eliminate programmes to avoid risks wholly, transfer or sharing risks is also limited. As a result, most often, actions must be taken to reduce risks to acceptable levels. The risk assessment information will help identify the most effective and efficient control activities available for handling the risk.

The LSG is responsible for the implementation of risk management must provide clear, comprehensive answers to these questions:

- What is the root cause of each risk? By evaluating the root cause reasons why the risk exists, it is possible to identify potential control activities to prevent, contain or eliminate the threat.
- Is there a potential for fraud, waste or abuse? All possible threats must be evaluated for resulting fraudulent, wasteful or abuse activities.

- What is the cost of implementing and maintain a control versus the cost of the acceptance of the results of unfavorable event? A financial comparison of the cost carrying out various control approaches and activities must be performed. The most cost efficient one would be selected by the LSG with consideration to risk tolerance.
- What is the priority ranking of the risk? A well prepared and objective prioritized risks list to provides the best guidance for management to allocate resources among control activities option and more economically reduce risks.

The analysis and interpretation of the risk assessment must be retained as part of the documentation of the rationale that supports risk management decisions. The LSG must review these decisions periodically to determine whether changes in conditions warrant a different approach to managing and reducing risk.

The act of managing the risks associated with achieving a mission through objectives requires a continuous assessment of these risks, this must never be forgotten.

18.3 Control Culture and Oversight

An essential element of an effective internal control (IC) system is the influence that a control culture brings. Such a culture includes the ethical values which the LSG displays in their dealings, both inside and outside the organization. Attitudes and actions affect the integrity and ethics of the control culture as well as the words selected at each juncture. Supervisors should require the activities they supervise to have firm control cultures and should take a risk-focused approach in their work. Particular emphasis should be placed on written policies and procedures and the exchanges in writing as critical mechanisms.

Another essential element of a robust IC system is that every employee recognizes and acknowledges to inform without delay the appropriate personnel of any existing or potential problems, non-compliance with the code of conduct as well as other policy violations or illegal actions. Adherence to a practice of being pro-active and vigilant in reporting issues can best be achieved when operational procedures are well-defined, transparent and accessible to all relevant personnel.

Senior management of the LSG must include in their activities

1. Regular formal and objective discussions with operating personnel concerning the effectiveness of their risk-based internal controls
2. Reviewing internal control reports issued by management, internal and external auditors and other monitoring units.
3. Periodic follow-up to ensure that implementation of recommendations is addressing concerns expressed by auditors and supervisory authorities on risk-based internal control weaknesses.

18.4 Internal Controls Functioning

When correctly functioning internal controls can only deliver reasonable but not absolute assurance. The idea of “reasonable assurance” recognizes that the cost of control must not exceed the benefit derived. It also acknowledges the need for uncompromising integrity, sound judgment and a culture of good control practices. Good internal control provides “reasonable assurance” that goals and objectives are achieved, but they cannot guarantee that these are attained. This said it is much less likely to achieve goals and objectives if internal controls are inadequate.

There are three types of purposes for internal controls which emphasize their different aspects and intentions:

1. Operational: These pertain to the effectiveness and efficiency of operations, including operational and financial performance. They promote orderly, economic actions and help produce quality products and delivery of services consistent with the organizational mandate. They also protect resources from impairment due to waste, abuse, mismanagement, error and fraud.
2. Reporting: These are related to internal and external financial and non-financial reporting. They may include reliability, timeliness, transparency or other terms as set forth by regulators, recognized standards setters or policies.
3. Compliance: These deal with adherence to laws, regulations, contracts and management directives to which the entity is subject

Control activities must be embedded in daily operations. This must include regular reviews; activity controls; physical controls; periodic checking of compliance; a documented system of approvals and authorizations; and a system of verification and reconciliation. Senior management must periodically verify that all areas comply with established policies and procedures. There are three mutually supportive fundamental internal control objectives, these are:

1. Transactions are conducted following management's general or specific AUTHORIZATIONS
2. Transactions are appropriately accounted for and accurately and promptly RECORDED and
3. That the assets and supporting documentation resulting from the transactions are adequately SAFEGUARDED.

18.5 Segregation of Duties

Lack of segregation of duties plays a substantial part in significant losses. In addition to reducing exposure to losses, isolation of tasks can help reduce unintentional errors. Separation of responsibilities requires the separation of four incompatible functions, and these are:

1. Authorizations and approvals of transactions for those items; and
2. Custody of assets and liabilities;
3. Recording and reporting
4. Verification/Validation

Segregation of duties does not mitigate corruption risks related to conflicts of interest, bribery, illegal gratuities, or economic extortion. Corruption risks are addressed by codes of conduct/ethics and whistleblower hotlines.

Segregation of Duties Matrix.

Objectives	Input	Process	Output
1. Authorization	Is the source authorized?	Are the procedures approved?	Is it what was approved?
2. Recording	Is it accurate and complete? Is it timely? Is it documented?	Who does it? When? Are procedures followed? Is it recoverable? Is management review adequate?	Is it accurate and complete? Is there an audit trail? Is management review adequate? Does it balance?

Objectives	Input	Process	Output
3. Safeguarding and Security	Who must control? Are duties separated?	Who can access it? Are duties separated?	Is it confidential? Who must have it?
4. Verification	Are sources proper?	Are procedures followed completely? Are investigation and review of differences adequate?	Are differences properly resolved? Is management review adequate?

18.6 Continually Monitor the Overall Effectiveness of Internal Controls

Tracking of critical risks must be part of the daily operations and must include a defined process for elevating levels of concern. Senior management of the LSG must continually monitor and evaluate the overall effectiveness of internal controls. Ongoing monitoring quickly detects and facilitates the correction of deficiencies. Continuous monitoring includes such tasks as the review and approval of journal entries and management review and approval of exception reports for independent analysis.

Separate evaluations of the risk-based internal controls can be undertaken as self-assessments. In such instances, persons responsible for the function determine the effectiveness of controls for their actions. Self-audits documentation and results would then be controlled by senior management for further actioning

Internal control deficiencies, ineffective policies or procedures, need to be reported to the appropriate person(s) immediately upon discovery. Deficiencies or ineffective policies or procedures that are reported must be rectified on a timely basis. The cause of the problem and the lessons learned from resolution should be shared so that other organizations can benefit. Follow-up reviews must be carried out to ensure that deficiencies are corrected as well as to ensure that all issues are addressed promptly.

18.7 Fraud Deterrence

Black's Law Dictionary defines “fraud” as wrongful or criminal deception intended to result in financial or personal gain. Fraudulent behavior has been linked with the perceived opportunity and rationalization that such action is acceptable.

Further Black's Law Dictionary defines fraudulent financial reporting as the intentional or reckless conduct, whether, by an act of commission or of omission. These acts result in “materially” misleading financial statements.

In addition to fraud, there are other forms of misconduct which occur these are commonly called “waste and abuse.” Using resources carelessly, extravagantly or to no purpose is considered waste. And abuse is behavior that is deficient or improper when compared with practices generally accept to be “reasonable and necessary,” given the “facts and circumstances.” Waste and abuse do not require fraud or illegal acts to be present, although they often are. When fraud or other forms of misconduct has either been detected or suspected, the risk assessment process needs to be revised.

Every manager of the LSG has a duty ensure a control structure exists and an environment is present that will protect employees and other stakeholders from being in a compromising position where they have both the method and opportunity to commit fraud, waste or abuse.

Every member of the LSG must give support to preventing fraud, waste and abuse of government property and privileges. Where situations or potential of fraud, misuse or abuse are identified, these must be reported without delay to LSG senior management. Employees must not attempt personal investigations of suspected incidents of fraud, this is a specialized process and will be taken care of by experts from audit.

Annex 1 Knowledge Check

Self-Assessment Questionnaire 1

Full Name ______________________________

1. Which of the below listed is not a function of accounting service:
   a) Timely accrual of labor remunerations and other payments and control over disbursements;
   b) Preparation of financial reports in an approved form within the determined deadlines;
   c) Municipality draft budget preparation.

2. Which of the below information doesn't necessarily need to be reflected in source documents:
   a) Name of the document;
   b) Signatures of people responsible for operation and its proper documentation;
   c) Deadlines of storage of source documents at organization files.

3. Right or Wrong:
   Electronic document to have legal power shall comply with requirements of Law on electronic documents and electronic reliable service.
   Right ----, Wrong -----

4. Right or Wrong
   Accounting documents describing economic events are signed by the Head of organization (authorized person) and Accountant or their substitutes and cashier.
   Right ----, Wrong -----

5. Debit keeps record of:
   a) Increase of expenses
   b) Decrease of assets
   c) Increase of liabilities

6. Right or Wrong:
   When using cash-based method of accounting, revenues and expenses are recognized as soon as they are incurred or received not when the funds are received or paid.
   Right ----, Wrong -----

7. According to budget classification which of the following doesn't represent a revenue group:

a) Taxes;
b) Social contributions;
c) Interest.

8. Classification of non-financial assets and their operations doesn’t comprise the following group:
a) Fixed assets;
b) Inventory;
c) Goods and services.

9. Right or Wrong:
Double entry method of accounting means that changes generated through economic operations are recorded in Debit of one account and in Credit of another account with the same amount.
Right ----, Wrong -----

10. Right or Wrong:
Generally, value of assets as a result of economic events are defined according to the primary or purchase value, which is adjusted reflecting all those changes that have taken place after its purchase, free of charge transfer or production/service. These changes comprise: substantial improvement, basic capital consumption, profit/loss by ownership, depletion, impairment, quality deterioration, unforeseen aging, losses generated by accidental damage and other losses.
Right ----, Wrong -----

11. Inventory purchase expenses don’t include:
a) Purchase price;
b) Transportation expenses;
c) Refundable taxes.

12. Low cost assets are technique, inventory and equipment of multiple use, cost and useful life of which is:
a) more than 500 GEL and more than 1 year
b) less than 500 GEL and more than 1 year
c) less than 500 GEL and less than 1 year

13. Value is an derivative asset of a significant value which is stored as a mean of value collection and:
a) is not used in production /service process;
b) is not used for consumption;
c) is not used neither in production/service process, nor for consumption

14. Right or Wrong:

Non-manufactured assets include assets generated naturally or created through legal or accounting operations, protection of ownership rights of which can or cannot be ensured.

Right ----, Wrong -----

15. Right or Wrong:

Liability is a liability created by the past event, covering of which will result in outflow of the LSG resourcesin a form of economic benefit or service potential.

Right ----, Wrong -----

16. Funds received by the organization from the budget are accounted based on:
    a) Accrual method;
    b) Cash method;
    c) Modified cash method.

17. Share capital doesn't include:
    a) Profit/loss of reporting period;
    b) Retained earnings/uncovered loss;
    c) Fixed assets revaluation reserve.

18. Right or Wrong:

There are 4 main revenue sources for the state the LSG : Taxes and other mandatory transfers determined by the state entities; Property related revenues received through assets ownership; Sales of goods and services; and Voluntary transfers received from other entities.

Right ----, Wrong -----

19. Purchase of financial and non-financial assets are:
    a) Spending operations;
    b) Revenue operations;
    c) Exchange operations when the asset of one type is exchanged in asset of another type.

20. Right or Wrong:

Off balance sheet items are analytical accounting articles. They are not used for double entries, though in a technical point of view we may correspond them with virtual accounts.

Right ----, Wrong -----

21. Non-operational revenues exclude:

a) Revenues received as a result of change of value of asset or liability due to changes in price level and structure.

b) Revenues received from exchange rate fluctuation from assets and liabilities evaluated in foreign currency;

c) Revenues received from sales of goods and services.

22. Spending operation accounting time is defined by:

a) Accrual method;

b) Cash method;

c) Modified cash method.

23. Right or Wrong:

Fixed assets physical depreciation rates for organizations funded by the budget, are defined by the order of Head of the organization.

Right ----, Wrong -----

24. Depreciation is not accrued on:

a) Draught animal;

b) Library stock;

c) Buildings.

25. Expenses incurred on substantial improvement of assets exclude:

a) Modification of elements of buildings and facilities targeted at extension of their useful life and enhancement of capacity;

b) Upgrade of parts of machinery and equipment targeted at improved quality of production/services;

c) Expenses that don’t influence their production capacity, quality, service potential or lifecycle.

26. Purpose of taking inventory of assets and liabilities is not:

a) Determination of actual balance of material values recorded at assets and liabilities and off-balance sheet items;

b) Check of storage rules and conditions of financial and non-financial assets;

c) Determination of market value of non-financial assets.

27. Right or Wrong:

It is possible to perform inventory with incomplete composition of inventory commission.

Right ----, Wrong -----

28. Right or Wrong:

Deficit and loss of financial requirements and inventory above norms shall be written off to the account of other non-operational expenses (8200), if culprits have not been identified and the court couldn't impose loss compensation on them.

Surplus of financial requirements and inventory demonstrated through the inventory process shall be reflected in the debit of relevant account and in credit of other non-operation revenues (8100).

Right ----, Wrong -----

29. Employee might get compensation of business trip costs within the borders of the country after return from business trip upon submission of relevant documents of actual costs incurred not later than:

a) 30 days;

b) 60 days;

c) 5 days;

30. Right or Wrong:

In case of failure to submit documents of actual costs related to business trip within the country, transportation costs shall be remunerated within the frames of minimum tariffs of railway or road transport.

Right ----, Wrong -----

31. Per Diem rates of business trip within the country are defined by:

a) Order of Head of the organization;

b) Order #231 of the President of Georgia dated April 20, 2005 on "remuneration of business trip costs of employees" with the amount of 15 GEL per day.

c) Annex 2 of the order #231 of the President of Georgia dated April 20, 2005 on "remuneration of business trip costs of employees" and differs from regions.

32. Employee/servant is not eligible for temporary disability benefit:

a) in case disability is caused by disease or mutilation;

b) when taking care of disabled member of family;

c) for childcare after childbearing.

33. Temporary disability benefit is issued:

a) for people who were injured during criminal activity or intentionally damage themselves;

b) if temporary disability is caused by disease or trauma directly resulted from non-sober condition (use of alcoholic, narcotic or any other psychoactive substance);

c) when taking care of disabled member of family;

34. Right or Wrong:

Temporary disability benefit is issued by the employer/organization for the whole period of disability and starts from the date of bulletin.

Right ----, Wrong -----

35. Employee/public servant is given a benefit/vacation remuneration:

a) in case disability is caused by disease or mutilation;

b) taking care of disabled member of family;

c) for pregnancy, childbearing and childcare.

36. Employee/public servant is given a vacation upon his/her request for pregnancy, childbearing and childcare – 730 calendar days, out of which remunerable period is:

a) 183 calendar days;

b) 200 calendar days;

c) 90 calendar days.

37. Right or Wrong:

Compensation of maternity leave for pregnancy, childbearing and childcare, also for a newborn adoption defined by the Georgian Law on Public Service, Article 64, is performed from the budget of relevant the LSG with the amount equivalent to the employer's salary.

Right ----, Wrong -----

38. Right or Wrong:

Payments might be done without a liability document.

Right ----, Wrong -----

39. Right or Wrong:

Transfer of registered liability to the other article, also the use of resources allocated for one liability for funding other liability is prohibited.

Right ----, Wrong -----

40. Right or Wrong:

Several payment orders may be prepared for one liability.

Right ----, Wrong -----

41. Ranking of position hierarchy determined by the Law on Public Service doesn't include:

a) First rank – Top management level;
b) Second rank – Middle management level;
c) Third rank – Junior specialist level.

42. Right or Wrong:
An official shall be appointed on vacant position only on the basis of competition, except for the cases of reorganization or liquidation of public institution, when the official is transferred to the relevant position with the same hierarchical rank and/or to other functionally similar position
Right ----, Wrong -----

43. Revenues received in a form of salary exclude:
a) Transfer of residential apartment to employee by the employer with the right to use – annual market value of rent (proportionally with the relevant period);
b) a credit issued by an employer to employee with interest rate less than defined by the Minister of Finance of Georgia – Amount payable corresponding to the interest rate defined by the Minister of Finance of Georgia.
c) Organized transportation of employee from residential place to work place or from work place to residential place by the employer when use of public transport is not possible or if transportation takes unreasonable amount or/and unreasonable time from the employee – cost of transportation.

44. Right or Wrong:
Property tax annual rate for taxable property of physical person is differentiated based on the total revenue of family of taxpayer during taxable year.
Right ----, Wrong -----

45. Annual rate of property tax for enterprise/organization is defined not more than X % of value of the taxable property:
a) 1 %;
b) 2 %;
c) 5 %.

46. According to the Local Self-Government Code, municipal property includes:
a) Roads of local importance and their parts, streets, underground crossings and pedestrian crossings, pavements, traffic lights, street light structures, squares, parks, boulevards, fountains, plants and riverbank protection structures;
b) Non-registered agricultural land located at the territory of Municipality;
c) Agricultural land located at 500m long border line.

47. Right or Wrong:

Decision on transfer of municipal property with the right to use through auction is made by the executive body of the municipality, while decision on free of charge transfer of property with the right to use by the rule of direct disposal is made by the executive body of the municipality upon consent of municipality council.

Right ----, Wrong -----

48. Right or Wrong:

Spending organizations being financed by the budgets of Autonomous Republics and LSG bodies shall submit accounting reports to local financial authorities within the terms determined by them; While budget organizations, LEPLs and N(N)LEs financed by the same sources are reportable against relevant controlling authorities within the terms determined by them.

Right ----, Wrong -----

49. Right or Wrong:

International Public Sector Accounting Standards (IPSAS) are a set of standards issued by the IPSAS Board for use by public sector entities around the world in the preparation of financial statements. These standards are based on International Financial Reporting Standards (IFRS).

Right ----, Wrong -----

50. When financial report is prepared using accrual-based accounting, financial report doen's include:

a) Statement of Financial position;
b) Statement of Financial performance;
c) Budget performance report.

Self-Assessment Questionnaire 2

Full Name ______________________________

1. Right or Wrong:

Source documents received by the accounting service are subject to necessary check as in terms of form (complete and properly formalized, with all details filled) and contents (legality of economic operation, logical conformity of separate parts) as well as arithmetically.

Right ----, Wrong -----

2. Off-balance sheet items are not:
   a) Amortized fixed assets
   b) Long term low cost expensed assets in operation
   c) Long term low cost assets
   d) Conditional/contingent liabilities

3. Organizations perform synthetic and analytical accounting:
   a) In electronic or paper form;
   b) Only in a paper form;
   c) Only in electronic form.

4. With the aim of organization of accounting and control over maintenance and storage inventory numbers are given to:
   a) Inventory;
   b) Only fixed assets;
   c) Fixed assets, long term low cost assets and values.

5. Right or Wrong:

Action taken by the organization, that reflects the creation, transformation, exchange, transfer, or abolishment of the value, is the economic event

Right ----, Wrong -----

6. Right or Wrong:

Economic operation (transaction) is an action taken on the basis of mutual agreement between the entities related to changes in volumes, composition or value of assets, liabilities and equity.

Right ----, Wrong -----

7. Cash based accounting is used for:
   a) Spending operations;
   b) Asset operations;
   c) Liability operations;
   d) Funds received within the frames of budget allocations.

8. Right or Wrong:

Grants are non-mandatory transfers, received by the state the LSG from the same level state institution, government of other country or international organization.

Right ----, Wrong -----

9. Fixed assets are the assets which:

a) are multiply or continuously used for more than a year in production or service process and cost of which is more than 500 GEL;

b) are multiply or continuously used for more than a year in production or service process and cost of which is more than 150 GEL;

c) are multiply or continuously used for more than a year in production or service process and cost of which is less than 500 GEL;

d) are multiply or continuously used for more than a year in production or service process and cost of which is 500 GEL and more.

10. Which of the following methods is not used in defining self-value of inventory:

a) Evaluation method based on costs incurred individually;

b) Weighted average value method;

c) FIFO method – First In First Out;

d) LIFO method – Last In First Out;

11. Right or Wrong:

Maintenance, storage and current repair costs of fixed assets that doesn't affect their production capacity, quality, service potential or life cycle, are recognized as expenses.

Right ----, Wrong -----

12. Modification of elements of own buildings and facilities targeted at extension of their useful life and enhancement of their capacity are regarded as:

a) Current expenses

b) Capital expenses

c) Is added to the value of building and facilities

13. Right or Wrong:

Contingent requirements and contingent liabilities are recognized in balance sheet articles.

Right ----, Wrong -----

14. Financial assets are:
   a) Cash funds;
   b) Raw materials and materials;
   c) Licenses;
   d) Non-manufactured intangible assets.

15. Short term financial assets are those use (consumption)/coverage of which is expected:
   a) Within a year from the date of creation of the asset;
   b) Within a year from the reporting date;
   b) Within 2 years from the reporting date;
   c) Within 6 months from the date of creation of the financial asset.

16. Right or Wrong:

Inventory are non-financial assets designated for production/manufacturing, further transfer or service delivery.

Right ----, Wrong -----

17. Own consumption of inventory is registered at:
   a) Subsidies account (7500)
   b) Other expenses account (7820)
   c) Basic capital consumption account (7300)
   d) Goods and services account (7200)

18. Right or Wrong:

Liability is a liability generated through the past event covering of which will result in outflow of the LSG resources in a form of economic benefit or service potential.

Right ----, Wrong -----

19. Value of accounts payable born out of purchase of goods or services is:
   a) Market value of goods and services delivered
   b) Value of goods and services delivered
   c) Self-cost of goods and services delivered at a supplier
   d) Balance value of goods and services delivered

20. Salary accrual and payment rules shall be regulated by:
  a) The order of Head of Financial Service
  b) Provision of the organization
  c) The order of the Minister
  d) The internal regulation of the organization.

21. At the moment of salary accrual liabilities are generated against:
  a) Tax authority
  b) Self-Governing body
  c) Employees
  d) Bank

22. Is it possible to detain certain amount from the salaries of employees of the organization (e.g. insurance, trade unions, execution, etc.)?
  a) Not possible
  b) Possible

23. Net value is:
  a) Difference between all assets generated by the budget sources and all liabilities envisaged by the budget;
  b) Difference between all assets generated by own sources and all liabilities envisaged by own sources;
  c) Difference between all assets and liabilities generated by own and budget sources;
  d) None of the answers is correct.

24. As per the Budget Code all receipts of the state budget, autonomous republics republican or local self-governing the LSG budgets, LEPLs and N(N)LEs is immediately directed to:
  a) the state budget;
  b) the budget of local self-governing body;
  c) the relevant budget;
  d) remains in disposal of payment receiver.

25. Purchases of financial and non-financial assets:
  a) are spending operations;
  b) are not spending operations.

26. Depreciation is accrued on:

a) Fixed assets
b) Financial assets
c) Inventory
d) Long term low cost assets

27. Depreciation rate of intangible fixed assets is:
a) 20 %;
b) 10%;
c) accrued proportionally with useful life, if it is possible to define it, otherwise 10% rate will apply;
d) depreciation is not accrued on intangible assets.

28. Completely depreciated (amortized) assets:
a) are derecognized/written off
b) recorded in fixed assets accounts
c) recorded in low cost long term assets accounts
d) recorded in off balance sheet items

29. Taking inventory during transfer of assets by lease or redemption:
a) is not mandatory
b) is mandatory

30. Right or Wrong:
In case of necessity a qualified specialist might be invited for participation in working process of inventory commission.
Right ----, Wrong -----

31. Inventory acts/descriptions are compared with:
a) the data of materially responsible person;
b) accounting data;
c) comparison is not made.

32. Business trip costs don't include:
a) Transportation costs;
b) Visa related costs;
c) Accommodation costs;
d) Gifts costs (except of officials)

33. Accommodation cost during business trip abroad shall be remunerated to an employee:

a) according to the defined rates

b) according to the actual costs

c) according to the rates set by the organization

34. Per Diem rates of weekends and holidays during business trip shall be compensated to an employee:

a) As usual Per Diem rate

b) Shall not be compensated

c) 50% of Per Diem rate

d) 30% of Per Diem rate

35. Employee is not given a benefit for temporary disability:

a) in case of disability is caused by disease or mutilation;

b) when taking care of disabled member of family;

c) in times of quaranteen;

d) In case of medical examinations.

36. Temporary disability benefit is paid to the employees with term contract:

a) within validity period of the contract;

b) for the whole period of bulletin;

c) Is not payable;

d) Upon decision of the organization.

37. Right or Wrong:

By quarterly applications liability is taken based on the program classification envisaged by the budget, according to the sum of gross amount of quarterly plan of each article of budget classification

Right ----, Wrong -----

38. Liability is taken by quarterly application for:

a) Utility payments;

b) Payments to budget;

c) Social benefits;

d) Representative costs.

39. In case of failure to submit certification document within the determined deadline, the State Treasury shall suspend:

a) New liability under the same classification article;

b) Payment under the same classification article;

c) Postponement by the organization;

d) The state treasury shall not react in any way.

40. Public servant types include:

a) Professional public official/public official, a person employed under an administrative contract or under a labor agreement.

b) A person employed under a labor agreement, administrative contract or appointed by the order.

c) Only professional public official/public official and a person employed under a labor agreement.

d) All answers are correct

41. Has the public official right to use his/her paid vacation unused within the calendar year, the next calendar year?

a) No;

b) Yes, once in 5 years;

c) Yes and vacation period shall be agreed with the Head of the LSG ;

d) Yes, with consent of his/her supervisory director.

42. When is organization responsible for income tax detention at the source of payment?

a) When making payment to an enterprise for services provided.

b) When making payment to a physical person for goods and services provided.

c) When making payment to a physical person for goods and services provided and the physical person has a certificate of tax payer.

d) When making payment to a physical person for services provided and the physical person doesn't have a certificate of tax payer.

43. Taxable property of a property tax payer physcal person comprises:

a) Real estate in his/her ownership, yachts, helicopters, passenger vehicles;

b) Only real estate in his/her ownership;

c) Real estate and movable property in his/her ownership;

d) Only yachts and helicopters in his/her ownership.

44. Property tax rate is defined by:

a) Government of Georgia in agreement with the Parliament;

b) Representative body of LSG within the frames of marginal rates.

c) Representative body of LSG in agreement with the Government of Georgia

d) Property tax rate is defined by the Tax Code.

45. Municipal property is divided into:

a) Own and complementary property
b) Own and basic (non-alienated) property
c) Own and non-own property
d) Basic (non-alienated) property and complementary property

46. Right or Wrong:

Municipality is entitled within the scope of its authority and in accordance with the Georgian legislation to establish Joint Stock Company, Limited Liability Company, Non-Entrepreneurial (Non-commercial) Legal the LSG.

Right ----, Wrong -----

47. Disposal of municipal property means:

a) Privatization, transfer with the right to use, transfer with the right to manage to the LEPL of municipality, free of charge transfer with the right to use/in ownership in cases determined by the Law and complying with the defined rules;
b) Only privatization and transfer with the right to use;
c) Free of charge transfer only to municipal LEPL, in cases determined by the Law and complying with the defined rules;
d) Privatization, transfer with the right to use, transfer with the right to manage and write off.

48. Spending institutions being funded from the budgets of local self-governing bodies shall submit accounting reports to the local financing authorities:

a) Not later than March 1 from completion of reporting year
a) Not later than April 1 from completion of reporting year
c) Within the terms defined by the local self-governing body
d) Quarterly, within 10 working days after completion of the quarter.

49. Annual balance of LEPL is audited by:

a) Financial authority;
b) State control authority;
c) Internal audit service;
d) An independent auditor appointed by the state control authority.

50. Right or Wrong:

As per the Budget Code, regulations defined for LEPL apply to the budget process relations of N(N)LE, inter alia accounting of financial-economic activity, reporting and balance preparation.

Right ----, Wrong -----

Answers

Question	Test 1		Test 2	
1	C		right	
2	C		C	
3	right		A	
4	wrong		C	
5	A		right	
6	wrong		right	
7	C		D	
8	C		wrong	
9	right		D	
10	right		D	
11	C		wrong	
12	B		C	
13	C		wrong	
14	wrong		A	
15	right		B	
16	B		right	
17	C		D	
18	right		right	
19	C		B	
20	right		D	
21	C		C	
22	A		B	
23	wrong		A	
24	B		C	
25	C		B	
26	C		A	
27	wrong		C	
28	right		D	
29	A		B	
30	right		right	
31	B		B	
32	C		D	
33	C		A	
34	right		A	
35	C		D	

Question	Test 1		Test 2	
36	A		A	
37	right		right	
38	wrong		C	
39	right		A	
40	right		A	
41	C		C	
42	right		D	
43	C		C	
44	right		B	
45	A		D	
46	A		wrong	
47	right		A	
48	right		C	
49	right		D	
50	C		right	