



Funded by  
the European Union



WORLD BANK GROUP

# ROSC

## REPORT ON THE OBSERVANCE OF STANDARDS AND CODES



ACCOUNTING  
AND AUDITING

**GEORGIA**

2022

**June 2023**

© 2023 The World Bank  
1818 H Street NW,  
Washington DC 20433  
Telephone: 202-473-1000;  
Internet: [www.worldbank.org](http://www.worldbank.org)

Some rights reserved.

This work is a product of the staff of The World Bank. The findings, interpretations, and conclusions expressed in this work do not necessarily reflect the views of the Executive Directors of The World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work. The boundaries, colors, denominations, and other information shown on any map in this work do not imply any judgment on the part of The World Bank concerning the legal status of any territory or the endorsement or acceptance of such boundaries.

This publication has been produced with the assistance of the European Union. Its contents are the sole responsibility of the World Bank Group and do not necessarily reflect the views of the European Union.

### **Rights and Permissions**

The material in this work is subject to copyright. Because the World Bank encourages dissemination of its knowledge, this work may be reproduced, in whole or in part, for noncommercial purposes as long as full attribution to this work is given.

All queries on rights and licenses, including subsidiary rights, should be addressed to World Bank Publications, The World Bank Group, 1818 H Street NW, Washington, DC 20433, USA; fax: 202-522-2625; e-mail: [pubrights@worldbank.org](mailto:pubrights@worldbank.org).




# TABLE OF CONTENTS



<b>Abbreviations</b> .....	<b>2</b>
<b>Preface</b> .....	<b>5</b>
<b>Acknowledgements</b> .....	<b>6</b>
<b>Executive Summary</b> .....	<b>7</b>
<b>I. Introduction</b> .....	<b>16</b>
<b>II. Assessment</b> .....	<b>20</b>
A. Accounting & Auditing Standards .....	20
B. Institutional Framework for Corporate Financial Reporting .....	22
1. <i>General Financial Reporting Requirements</i> .....	23
2. <i>Listed Companies</i> .....	28
3. <i>Banking Sector</i> .....	37
4. <i>Microfinance Sector</i> .....	48
5. <i>Insurance Sector</i> .....	52
6. <i>State-Owned Enterprises</i> .....	60
7. <i>The Accountancy Profession</i> .....	64
8. <i>Professional Education and Training</i> .....	70
9. <i>Audit Regulation, Quality Assurance, and Public Oversight</i> .....	75
10. <i>Setting Accounting and Auditing Standards</i> .....	82
C. Observed Financial Reporting Practices and Perceptions .....	83
<b>III. Main Changes since the Previous ROSC A&amp;A Assessment</b> .....	<b>97</b>
<b>IV. Recommendations</b> .....	<b>99</b>
<b>Annex A. Progress on ROSC 2015 Recommendations</b> .....	<b>107</b>



# ABBREVIATIONS

<b>ACCA</b>	Association of Chartered Certified Accountants
<b>AFS</b>	Annual Financial Statements
<b>AGM</b>	Annual General Meeting
<b>AML</b>	Anti-Money Laundering
<b>BSD</b>	Bank Supervisory Department
<b>CGCCB</b>	Corporate Governance Code for Commercial Banks
<b>CGCI</b>	Corporate Governance Code for Issuers of Public Securities
<b>CGCSOE</b>	Corporate Governance Code for SOEs
<b>CPD</b>	Continuing Professional Development
<b>CPF</b>	Country Partnership Framework
<b>CTF</b>	Countering Terrorist Financing
<b>EC</b>	European Commission
<b>EFRAG</b>	European Financial Reporting Advisory Group
<b>ESRS</b>	European Sustainability Reporting Standards
<b>EU</b>	European Union
<b>FRMU</b>	Fiscal Risk Management Unit
<b>GAAP</b>	Generally Accepted Accounting Principles
<b>GEL</b>	Georgian lari (currency)
<b>GDP</b>	Gross Domestic Product
<b>GFAAFM</b>	Georgian Federation of Accountants, Auditors, and Financial Managers
<b>GFPAA</b>	Georgian Federation of Professional Accountants and Auditors
<b>GSE</b>	Georgian Stock Exchange
<b>HEI</b>	Higher Educational Institution
<b>I&amp;D</b>	Investigation and Discipline

<b>IAASB</b>	International Auditing and Assurance Standards Board
<b>IAESB</b>	International Accounting Education Standards Board
<b>IASB</b>	International Accounting Standards Board
<b>IES</b>	International Education Standards
<b>IESBA</b>	International Ethics Standards Board for Accountants
<b>IFAC</b>	International Federation of Accountants
<b>IFIAR</b>	International Forum of Independent Audit Regulators
<b>IFRS</b>	International Financial Reporting Standards Accounting Standards
<b>IFRS for SMEs</b>	International Financial Reporting Standards for Small and Medium-sized Entities Accounting Standard
<b>IMF</b>	International Monetary Fund
<b>ISA</b>	International Standards on Auditing
<b>ISQC</b>	International Standard on Quality Control
<b>ISQM</b>	International Standards on Quality Management
<b>ISSSG</b>	Insurance State Supervision Service of Georgia
<b>IT</b>	Information Technology
<b>JSC</b>	Joint Stock Company
<b>LIE</b>	Loan Issuing Entity
<b>LLC</b>	Limited Liability Company
<b>MD&amp;A</b>	Management Discussion and Analysis
<b>MFI</b>	Microfinance Institution
<b>MoE</b>	Ministry of Education
<b>MoESD</b>	Ministry of Economy and Sustainable Development
<b>MoF</b>	Ministry of Finance
<b>NBFI</b>	Non-Banking Financial Institutions
<b>NBG</b>	National Bank of Georgia
<b>NCEQE</b>	National Center for Educational Quality Enhancement
<b>NISD</b>	Non-banking Institutions Supervision Department
<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>PAO</b>	Professional Accountancy Organization

<b>PIE</b>	Public Interest Entity
<b>QA</b>	Quality Assurance
<b>REPORTAL</b>	Public Depository of Financial Statements
<b>ROSC A&amp;A</b>	Report on the Observance of Standards and Codes in Accounting and Auditing
<b>SAO</b>	State Audit Office
<b>SARAS</b>	Service for Accounting, Reporting, and Auditing Supervision
<b>SME</b>	Small or Medium Enterprise
<b>SMO</b>	Statement of Membership Obligations
<b>SMP</b>	Small or Medium Size Practice
<b>SOE</b>	State-Owned Enterprise
<b>US\$</b>	United States dollar (currency)

## Exchange rates

- \* 1 US\$ = 3.0976 GEL (31 December 2021); 1 US\$ = 2.7020 GEL (31 December 2022)
- \* 1 euro = 3.5040 GEL (31 December 2021); 1 euro = 2.8844 GEL (31 December 2022)



# PREFACE

Reports on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A) assess financial reporting and auditing standards, institutions, and practices in participating countries. These reports form part of a joint initiative implemented by the World Bank and the International Monetary Fund to review the quality of implementation of internationally recognized standards and principles in 12 key areas (the ROSC program) with a view to promoting financial and economic stability.

This report provides an assessment of financial reporting and auditing requirements and practices within the corporate sector in Georgia and sets forth

areas for consideration for improving the institutional environment for accounting and auditing. The ROSC A&A uses international benchmarks of good practice governing financial reporting and auditing in the assessment, including International Financial Reporting Standards and International Standards on Auditing. This report updates an earlier assessment which was published in 2015 and was undertaken following a formal request from the Government of Georgia.

The report was conducted as part of the European Union funded Georgia Financial Inclusion and Accountability project.



# ACKNOWLEDGEMENTS

The ROSC A&A was conducted during July-December, 2022 at the request of the Georgian Government. All findings reflect this period of the review.<sup>1</sup> The World Bank team was led by Garik Sergeyan (Senior Financial Management Specialist) and included Irina Gordeladze (Extended Term Consultant), Natalia Konovalenko (Extended Term Consultant), Michael Wells (Consultant), Darrel Scott (Consultant), and Jon Hooper (Consultant). The team worked under the supervision of Daniel Boyce (Governance Practice Manager).

The review was conducted through a participatory process involving various in-country stakeholders, including the Georgian Service for Accounting, Reporting and Auditing Supervision (SARAS), the Ministry of Finance, the National Bank of Georgia, the Insurance State Supervision Service of Georgia, the National Center for Educational Quality Enhancement, professional accountancy organizations, auditing firms, academia, and other business communities. The ROSC A&A team would particularly like to thank David Mchedlidze, the Head of Georgian Service for Accounting, Reporting and Auditing Supervision for the strong leadership of this initiative within the Georgian Government.

The team gratefully acknowledges Sebastian Molineus (The World Bank Country Director for South Caucasus) for his guidance and support.

The report also benefited from the comments of peer reviewers: Andrei Busuioc (Senior Financial Management Specialist), Haocong Ren (Senior Financial Sector Economist) and Mai Thi Phuong Tran (Senior Financial Management Specialist).

<sup>1</sup> The review of financial statements is based on the financial statements that were available to the reviewers in September 2022.





# EXECUTIVE SUMMARY



## Background

1. In the decade prior to the COVID-19 pandemic, Georgia's economy was the second-fastest growing in the Europe and Central Asia region. The average economic growth rate was 5.2 percent in per capita terms during 2010-2019. When Georgia moved to upper-middle income status in 2019, the gross domestic product (GDP) per capita was US\$ 4,773. As the pandemic hit, Georgia, reliant on tourism, experienced one of the largest GDP drops in the Europe and Central Asia region (6.8 percent decline in 2020). The economy has recovered strongly from COVID-19 and has shown resilience against the impacts of the Russia's invasion of Ukraine. In 2021, the economy rebounded strongly (10.4 percent growth), driven by the recovery of consumptions and exports, and GDP surpassed its 2019 level, with growth estimated to have averaged double-digits during the first ten months of 2022.

2. Georgia's future aspirations are ambitious, anchored in the objective of closer integration with the European Union (EU). Georgia intends to further open markets and invest in connectivity to boost exports. European integration is the cornerstone of this ambitious outlook. Building on the 2014 Association Agreement with the EU, Georgia has been approximating its institutions and policies with those of the EU and in March 2022 submitted a formal application for EU membership. In June 2022, the European Council discussed the application and stated its readiness to grant Georgia EU candidate status once the priorities set out in the European Commission's opinion on its EU membership application are addressed.

3. The capital market is at an initial stage of development, with two stock exchanges authorized to operate in Georgia. The Georgian Stock Exchange (GSE) is the only currently active exchange (established in 1999) and is the holding company of the Tbilisi Stock Exchange (not active at the time of the assessment). Neither exchange is affiliated with any networks of other exchanges. The eight listed equities are all domestic companies and had a total market capitalization of Georgian lari (GEL) 2,384 million at the end of 2021. The 23 listed non-equity instruments comprised 15 corporate bonds, seven international financial institution bonds and one global depository note. The market capitalization of the bonds was GEL 1,759 million at year-end 2021. The banking sector accounts for over 90 percent of total financial institution assets in Georgia and is growing both in scope and scale. The microfinance sector in Georgia is robust. It represents 76 percent of total loans in the non-banking financial institutions sector, which itself constitutes 3.4 percent of the overall financial sector as at the end of 2021. The insurance sector has been growing rapidly from a small base, with total premiums in the year ended 31 December 2021 of GEL 773 million, accounting for 1.3 percent of GDP. The state-owned enterprise (SOE) sector still plays a critical role in the economy. The SOE portfolio has been reduced from 1,315 entities in 2009 to 316 entities in 2021. With more than 196,000<sup>2</sup> established businesses, micro, small and medium enterprises accounted for around 62 percent of employment, and around 51 percent of total exports. They are a crucial part of the economy as at the end of 2021.

<sup>2</sup> Including individual entrepreneurs.

## ■ Linkage of this Report to the Georgia's Reform Agenda

4. This Report on the Observance of Standards and Codes Accounting and Auditing (ROSC A&A) seeks to assist the further development of the financial reporting institutional framework in Georgia. Strengthening corporate financial reporting and auditing is aligned with the Georgia Development Strategy Vision 2030, which features fostering investment activities and improving access to finance for small and medium enterprises (SME) among its objectives. The Strategy outlines the importance of a proper financial reporting system for the growth and development of SMEs. At the same time, the Strategy envisages the assurance of audit quality through monitoring of auditors' quality control systems.

5. The World Bank Country Partnership Framework (CPF) for Georgia 2019-2023 included as an indicator "enhanced transparent financial reporting by SMEs",<sup>3</sup> among others. The CPF program is also supporting improvement in the governance and financial reporting of SOEs. Weak corporate governance is listed as one of the investment climate deficiencies and includes inadequate corporate transparency, related to information disclosure about ownership structures and inefficient corporate boards.

## ■ Georgia Report on the Observance of Standards and Codes, Accounting and Auditing 2022

6. This ROSC A&A report assesses the progress in improving the institutional framework for accounting and auditing since the previous ROSC A&A in 2015. It analyzes the accounting frameworks for reporting by public interest entities (PIEs), listed companies, the banking, microfinance, and insurance sectors, SOEs, and SMEs. The current report seeks to support the ongoing development of the financial reporting institutional

framework in line with the Georgia Development Strategy Vision 2030. Improved corporate financial reporting can strengthen corporate governance, improve transparency, and raise the quality of financial information, thereby encouraging a more active and dynamic private sector as an engine for economic growth, making Georgia more attractive to investors.

7. This assessment was conducted at the request of the Government of Georgia to provide institutional recommendations on the country's accounting, financial reporting, and auditing reform agenda. The data and information used for the review were gathered from ROSC A&A 2.0 diagnostic questionnaires completed by stakeholders; by reviewing related documents; and through interviews with the main stakeholders from regulators, professional accountancy organizations (PAOs), auditing firms, the financial analyst community, banks, and academia. The ROSC A&A 2.0 approach uses a series of indicators to establish a baseline. This is the first time this approach is being used for the Georgia ROSC report. The report summarizes key findings, identifies gaps, and makes recommendations for consideration by the authorities to improve alignment with international standards and good practice.

## ■ Progress since the 2015 ROSC A&A Report and Progress on the Key 2015 ROSC A&A Recommendations

### Achievements since the 2015 ROSC A&A Report

8. Since the 2015 ROSC A&A report, the most significant achievement in this field was the enactment and subsequent implementation of the Law of Georgia on Accounting, Reporting, and Audit in 2016. This Law brought Georgian legislation in this area almost in line with EU legislation,<sup>4</sup> and addressed almost all of the recommendations in the 2015 ROSC A&A report.

<sup>3</sup> The CPF indicator (baseline: 0 [2016] and Target: 500 [2022]) was overachieved as of December 2022 with more than 4400 SMEs publishing their reports on the SARAS REPORTAL.

<sup>4</sup> Refer to transposition tables under the following links: <https://www.saras.gov.ge/Content/files/Transposition-table-audit-directive.pdf> and <https://www.saras.gov.ge/Content/files/Transposition-table-accounting-directive.pdf>

**9. The Law on Accounting, Reporting, and Audit determines the legal grounds for keeping company accounts in Georgia.** It does so in accordance with internationally recognized standards for preparing and submitting financial statements, management reports, and statements with regard to payments made to the State, as well as for carrying out professional certification, and audit activities including quality assurance. It also determines the legal grounds for exercising state supervision over these fields and for imposing sanctions as appropriate.<sup>5</sup>

**10. The Service for Accounting, Reporting, and Auditing Supervision (SARAS) has led effective implementation of the Law and many improvements in the quality of corporate financial reporting, accounting, and audit in Georgia.** The establishment of SARAS, as a result of the Law, was a significant achievement. Efficient dialogue was established with the main stakeholders including business societies, peer agencies, non-governmental sector, international organizations, and academia. SARAS's role in enhancing corporate transparency and quality assurance has been appreciated by society. In the meantime, further steps are needed to enhance the quality of monitoring and enforcement activities, as well as to improve the dispute resolution mechanism.

**11. Other notable achievements since 2015 are the establishment of the web based Public Depository of Financial Statements (REPORTAL)<sup>6</sup> for publication of annual financial statements (AFS) as well as the creation of the register of auditors.** The well-established and promoted reporting portal has enabled an unprecedented level of corporate transparency, with up to 100 institutional users of digital financial information, including financial services, credit rating agencies, financial analysts, research, regulators, and other sectors.

**12. Despite some resource limitations, SARAS continues to successfully fulfil its obligation to translate and adopt newly released international standards, being among the fastest adopters of**

**new International Financial Reporting Standards Accounting Standards (IFRS) around the world.** An online glossary of vocabulary for IFRS/ International Standards on Auditing (ISA) terms has been developed and is regularly updated.<sup>7</sup>

**13. Since the 2015 ROSC A&A, the transparency of the profession has increased significantly through well-administered registries of auditors, audit firms, and certified accountants.** Audit quality monitoring, performed in line with good practices and covering almost 90 percent of the market volume, has enhanced trust in the audit oversight function and the audit profession.

**14. Professional certification and continuous development processes have been standardized, made transparent, and are well-monitored.** SARAS has coordinated the availability of key supplementary materials, continuing professional development (CPD) and other training, and seminars on a wide range of topics for auditors and accountants, with the help of donors and PAOs.

## Remaining areas for improvement from the 2015 ROSC

**15. The following recommendations from the 2015 ROSC A&A have yet to be fully addressed, though each was considered by relevant stakeholders and some actions have been taken to implement the recommendation, as detailed below:**

- \* The 2015 ROSC A&A recommended that the definitions of PIEs and large/medium/small/micro enterprises be made consistent across Georgian legislation. The definitions of entities for corporate reporting purposes in the Law on Accounting, Reporting, and Audit are in line with international good practices. There remain some inconsistencies with the equivalent definitions in the Tax Code. However, the impact on corporate reporting in general is not significant.

<sup>5</sup> Law of Georgia on Accounting, Reporting, and Audit, Article 1.

<sup>6</sup> <https://reportal.ge>

<sup>7</sup> <https://www.saras.gov.ge/translate>

- \* Donor-supported activities have addressed two recommendations relating to improving university education and curricula in the field of accounting and audit. Major progress has been made, including the establishment of a recommended curriculum for accounting and audit education for universities and the provision of learning materials. These activities are ongoing, so the 2015 recommendations continue to be relevant.

16. These two areas are covered in the recommendations of this report, which are summarized below.

**Table 1.** Summary of ROSC A&A ratings

Performance Indicators	Georgia Rating <sup>8</sup>	Maximum Rating
<b>1. Financial Reporting and Auditing Standards<sup>9</sup></b>	<b>4</b>	<b>4</b>
A.1. Financial reporting standards	4	4
B.1. Auditing standards	4	4
<b>2. Commercial Enterprises (including SMEs)</b>	<b>4</b>	<b>4</b>
A.1. Simplified financial reporting	4	4
A.2. Exemptions to perform statutory audits	4	4
<b>3. Financial Reporting and Auditing of Listed Companies</b>	<b>3.1</b>	<b>4</b>
A. Financial reporting and auditing requirements for listed companies	3.3	4
B. Monitoring and enforcement of the financial reporting requirements of listed companies	2.8	4
<b>4. Financial Reporting and Auditing for Banks</b>	<b>3.1</b>	<b>4</b>
A. Financial reporting and auditing requirements for banks	3	4
B. Monitoring and enforcement of the financial reporting requirements of banks	3.2	4
<b>5. Financial Reporting and Auditing for Insurance Companies</b>	<b>2.9</b>	<b>4</b>
A. Financial reporting and auditing requirements for insurance companies	3	4

<sup>8</sup> ROSC A&A Rating Criteria: 1 = Minimum rating; criteria for “2” rating not met; 2 = Initial steps taken towards alignment with international good practice; however, significant gaps exist; 3 = Some alignment with international good practice; however, gaps remain; 4 = Substantial alignment with international good practice.

<sup>9</sup> This performance indicator relates to the adoption of international standards, performance indicators 2 to 6 relate to implementation and application of those standards.

## 2022 ROSC A&A Assessment – Ratings and Recommendations

17. An overall assessment of key accounting and auditing performance indicators is provided in Table 1, which confirms the remaining challenges. The recommendations in Table 2 are derived from the detailed findings of the report in the body of the report below.

Performance Indicators	Georgia Rating <sup>8</sup>	Maximum Rating
B. Monitoring and enforcement of the financial reporting requirements of insurance companies	2.8	4
<b>6. Accountancy Profession</b>	<b>Partially Adopted</b>	<b>Adopted</b>
A. International Education Standards	Partially Adopted	Adopted
B. Code of ethics for professional accountants	Adopted	Adopted
C. Investigative and disciplinary system	Partially Adopted	Adopted
<b>7. Audit Public Oversight</b>	<b>3.9</b>	<b>4</b>
A. Audit oversight system	3.8	4
B. Audit quality assurance	4	4
C. Audit quality investigations and sanctions	4	4

**Table 2.** Summary of recommended areas for consideration<sup>10</sup>

#	Recommendations	Responsible	Dependencies	Deadline
<b>Regulatory and Institutional Framework</b>				
1	<p>The establishment of SARAS and its progress in implementing the requirements of the Law has been a very great achievement and is a credit to all involved. SARAS should continue enhancing its capacity and funding to be fully sustainable and independent of external donor support and address its operational challenges; including its ability to attract and retain highly qualified staff and consultants to ensure the quality of its monitoring and enforcement activities. Additionally, consideration should be given to enhancing the composition, capacity and competencies of the SARAS board to increase its effectiveness in areas such as dispute resolution and adopting regulations.</p> <p>SARAS should also consider the need for a dispute resolution mechanism with paid independent audit experts to address disputes arising from auditor registration and inspections.</p>	Government of Georgia, Ministry of Finance (MoF), SARAS	Amendments of law and regulations	Medium term

<sup>10</sup> For detailed recommendations refer to **Section IV. Recommendations** below.

#	Recommendations	Responsible	Dependencies	Deadline
2	<p>In line with Georgia's efforts to achieve EU membership candidate status and to enhance the country's overall capacity to uphold the membership obligations, SARAS and legislators should continue efforts to further align with EU legislation in the areas of accounting, financial reporting, and auditing. Particularly, further alignment is required for:</p> <ul style="list-style-type: none"> <li>* introducing in the law of the definition of "key audit partner".</li> <li>* including in the auditor registration requirements the disclosures of audit firm's office locations and about the network.</li> <li>* covering by law the mechanism for possible delegation of tasks by SARAS to other bodies.</li> <li>* introducing in law the definition and the description of the auditor's annual transparency report.</li> </ul>	SARAS	Amendments of law and regulations	Short term
3	The publication requirements for PIE financial statements and management reports should be further enhanced and harmonized.	National Bank of Georgia (NBG), Insurance State Supervision Service of Georgia (ISSSG), MoF, SARAS	Amendments of law and regulations	Short to medium term
4	Systematic collaboration between all sectoral regulators and external auditors of regulated entities should be established or enhanced.	NBG, ISSSG	Amendments of regulations	Short term
5	Financial reporting requirements for microfinance enterprises should be reevaluated for proportionality considering existing and potential sources of funding.	NBG, SARAS	Amendments of law and regulations	Short term
6	A consolidated Code of Corporate Governance covering all PIEs should be issued, and laws and regulations updated to ensure its effective enforcement for PIEs.	NBG, ISSSG, MoF, SARAS	Amendments of law and regulations	Medium term

#	Recommendations	Responsible	Dependencies	Deadline
7	A Country Action Plan for sustainability reporting should be developed and introduced to meet the increasing demand from investors and institutions for insights into the sustainability effects of new and existing projects and activities.	SARAS, MoF	Introduction of law and regulations implementing the Country Action Plan.	Short term
8	The framework SOE law and supporting secondary regulations should be adopted in line the Comprehensive SOE Reform Strategy 2023-2026 and the Corporate Governance Code for State-Owned Enterprises (CGCSOE) should be implemented and enforced without further delay starting with the three pilot SOEs. Respective capacity building should be provided to the SOEs to implement the CGCSOE.	Government of Georgia	Amendments of law and regulations	Short Term
9	The establishment of audit committees in SOEs should be expedited.	MoF, Ministry of Economy and Sustainable Development (MoESD)		Short term
10	SOE reporting requirements should be strengthened. Particularly: <ul style="list-style-type: none"> <li>* SOE aggregate reporting and the disclosure of SOE portfolio information should be enhanced.</li> <li>* SOEs' management reports should be strengthened to include: a Corporate Governance report; information on the remuneration of SOE board members; information about financial assistance from the state; information on the costs and funding arrangements pertaining to the fulfillment of public service obligations; and a public statement of the SOE's objectives and their fulfilment.</li> <li>* Prominent disclosure of SOE public service obligations and/or quasi-fiscal activities and obligations in the financial statements should be required.</li> </ul>	MoF, SARAS	Amendments of law and regulations	Short Term

### Monitoring and Enforcement of Financial Reporting

11	Existing regulators' monitoring of general purpose AFS against applicable financial reporting standards should be enhanced. This will help to address the gap that was found to exist between the applicable legislative requirements and actual practice indicated by the non-compliance found in the review of IFRS financial statements in Section C.	SARAS	SARAS resources / budget	Short term
----	--	-------	--------------------------	------------

#	Recommendations	Responsible	Dependencies	Deadline
12	Regulations should explicitly provide for graduated sanctions to facilitate enforcement of financial reporting requirements.	SARAS	Amendments of law and regulations	Medium term
13	Systematic collaboration between SARAS and sector regulators with responsibility for reviewing IFRS compliance should be improved and extended.	SARAS, NBG, ISSSG, other regulators	Extend and improve the Memorandum of understanding	Short term
14	The annual publications of regulators that perform IFRS reviews should detail material findings of those reviews on an aggregated and anonymous basis, and findings of all regulators should be consolidated and included in the SARAS report.	SARAS, NBG, ISSSG, other regulators	Memorandum of understanding	Short term
15	Implementation of the eXtensible Business Reporting Language (XBRL) <sup>11</sup> standard should be considered for financial reporting in Georgia.	SARAS, MoF	Amendments of law and regulations	Medium term

#### Audit Oversight and Quality Assurance

16	SARAS should be given a wider range of graduated sanctions on auditors and audit firms in cases of misconduct or non-compliance with standards and registration requirements. The gap between the maximum fine and the ultimate sanction (deregistration) is large. A greater range of graduated sanctions on auditors for misconduct would help to regulate the market more effectively.	SARAS	Amendments of law and regulations	Medium term
----	---	-------	-----------------------------------	-------------

#### Accountancy Profession

17	The Georgian Federation of Professional Accountants and Auditors (GFPAA) should continue to make progress in complying with all the requirements of the International Federation of Accountants' (IFAC) Statements of Membership Obligations (SMO). Once IFAC's assessment of GFPAA's 2022 SMO Action Plan is complete, GFPAA should work on addressing any areas of non-compliance or partial compliance identified by IFAC.	GFPAA	GFPAA regulations	Medium term
18	GFPAA should work to address any recommendations made by SARAS as part of SARAS' oversight of the PAO processes and its process for ongoing approval of the GFPAA's certification.	GFPAA	GFPAA regulations	Medium term

<sup>11</sup> <https://www.xbrl.org/>



#	Recommendations	Responsible	Dependencies	Deadline
<b>Accounting Education</b>				
19	An educational standard for accountancy degrees at higher educational institutions (HEI) should be developed in line with the International Education Standards (IES) issued by the International Accounting Education Standards Board (IAESB) supported by IFAC, and good international practice, with involvement of universities, SARAS, and PAOs.	Ministry of Education (MoE), National Center for Educational Quality Enhancement (NCEQE), Universities	National education standard, regulations, universities' curricula	Short term
20	Audit and accounting should be considered to be added to the list of regulated professions in the Law on Education.	SARAS, MoE, NCEQE	Amendments of law and regulations	Medium term
21	University curricula should be aligned with a model curriculum and PAOs' curricula, aiming to promote recognition of university degrees by PAOs and SARAS.	MoE, Universities	Universities' curricula	Short to medium term
22	Assessment practices should be aligned with IES across universities to expedite recognition by PAOs and SARAS.	MoE, Universities	Amendments of regulations	Short to medium term
<b>Setting Auditing Standards</b>				
23	SARAS should be ready and prepared to adopt the forthcoming International Auditing and Assurance Standards Board (IAASB) standard on the audit of less-complex entities when it becomes extant, and to assist auditors with implementing the standard.	SARAS	Amendments of regulations	Medium term



# I. INTRODUCTION

## ■ Country Background

18. Georgia has an established record of reforms that has contributed to economic success. With an average economic growth rate of 5.2 percent in per capita terms during 2010-2019, Georgia was the second-fastest growing economy in the Europe and Central Asia region and among the fastest globally. As a result, GDP per capita (at constant 2015 US\$) increased from US\$ 3,100 in 2010 to US\$ 4,773 in 2019, the year in which Georgia moved to upper-middle income status. The poverty rate (measured using the national poverty line) declined from 37.3 percent at the start of the previous decade to 17.5 percent in 2021. These accomplishments have been supported by a sound macroeconomic framework, with a fiscal rule, inflation-targeting monetary policy, and robust financial sector regulation. An attractive

business environment has been established, with strong performance on almost all international measures of investment climate, and governance has been improving, with one of the lowest perceived corruption levels in the Europe and Central Asia region.

19. The economy recovered strongly from COVID-19 and has shown resilience against the impacts of the Russia's invasion of Ukraine. As the pandemic hit, Georgia, reliant on tourism, experienced one of the largest GDP drops in the Europe and Central Asia region (6.8 percent decline in 2020). Authorities took advantage of the room created by prudent economic policies to respond to the crisis in a timely manner, mitigating its impacts on lives and livelihoods. As a result, poverty increased by just 1.8 percentage points, to 21.3 percent in 2020. In 2021, the economy rebounded strongly (10.4 percent growth), driven by

the recovery of consumptions and exports, and GDP surpassed its 2019 level. Despite the fact that Russia and Ukraine together account for about a quarter of exports, remittances, and tourism inflows, the Georgian economy is significantly more diversified than other countries in the Caucasus and Central Asia and has shown significant resilience to Russia's invasion of Ukraine and associated sanctions on Russia, with growth estimated to have averaged double-digits during the first ten months of 2022.

**20. Georgia's future aspirations are equally ambitious, anchored in the objective of closer integration with the EU.** Georgia intends to further open markets and invest in connectivity to boost exports. European integration is the cornerstone of this ambitious outlook. Building on the 2014 Association Agreement with the EU, Georgia has been approximating its institutions and policies with those of the EU and in March 2022 submitted a formal application for EU membership. In June 2022, the European Council discussed the application and stated its readiness to grant Georgia EU candidate status once the priorities set out in the European Commission's opinion on its EU membership application are addressed.

**21. The financial sector in Georgia is highly concentrated.** The banking sector accounts for over 90 percent of total financial institution assets in Georgia. It includes 14 commercial banks, 36 microfinance organizations, 18 insurers, and 5 pension funds.<sup>12</sup> Pension funds, smaller banks, and non-bank financial institutions are relatively minor participants in the financial sector. The overall legal and institutional framework is adequate. The banking sector remains healthy.

**22. Capital market development in Georgia has been given significant policy attention in the recent years.** The GSE, established in 1999, operates the

only active regulated exchange platform in Georgia, as well as its own clearing and settlement facilities. Listed securities, best bids and offers, transaction prices, and trading volumes are published daily on the GSE website. The local bond market has grown in popularity and now lists securities in local and foreign currencies issued by local companies and international financial organizations. The number of issuers has grown in recent years, spurred mainly by the bond issuers, while market capitalization has declined in recent years. There are no derivative contracts listed on the GSE. Prominent developments include recent legislative initiatives to support market development, the strengthening of capital market supervisory capacity at the NBG and the launch of the primary dealer system, tax reform on financial instruments and transactions, the introduction of a funded pension scheme, and the preparation of capital market development plan by the MOESD. None-the-less, capital market listings remain static and trading activity is extremely muted (for example, only nineteen trades occurred in the stock market in calendar year 2022).<sup>13</sup> A well-developed domestic capital markets could contribute to Georgia's sustainable economic growth.

**23. The SOE sector still plays a critical role in the economy.** The SOE portfolio has been reduced from 1,315 entities in 2009 to 316 entities in 2021; of these, 154 are owned by the central government and 162 by local authorities.<sup>14</sup> In addition, these SOEs control an additional 96 subsidiaries. SOEs remain present not only in strategic sectors such as utilities but also in commercial sectors such as transportation, manufacturing, and construction. In 2020, SOEs employed approximately 60,000 workers, accounting for about 5 percent of formal jobs.<sup>15</sup> Over the past decade, the Government has taken concrete steps to address SOE challenges, focusing on improving their fiscal transparency. Despite these steps, progress remains limited.

<sup>12</sup> NBG Annual Report, 2022.

<sup>13</sup> GSE Website

<sup>14</sup> Comprehensive SOE Reform Strategy for 2023-2026.

<sup>15</sup> This number includes all central-level SOEs, including with minority stake, and municipal enterprises with 25 percent or more state ownership and with an annual turnover exceeding GEL 200,000 or with annual payroll exceeding GEL 15,000.

## ■ Linkage of this Report to the Georgia's Reform Agenda

**24. This ROSC A&A seeks to assist with the further development of the financial reporting institutional framework in Georgia.** High quality financial reporting contributes to promoting private sector growth by allowing investors to evaluate corporate prospects and make informed investment decisions, thus contributing to attracting foreign direct investment.

**25. Strengthening corporate financial reporting and auditing is aligned with the Georgia Development Strategy Vision 2030 which features fostering investment activities and improving access to finance for SMEs as objectives, among others.** The Strategy outlines the importance of a proper financial reporting system for the growth and development of SMEs. At the same time, the Strategy envisages assurance of audit quality through monitoring auditors' quality control systems.

**26. The World Bank CPF for Georgia 2019-2023 included as an indicator "enhanced transparent financial reporting by SMEs".** The CPF program is also supporting the improvement in governance and financial reporting of SOEs. Weak corporate governance is listed as one of the investment climate deficiencies, including inadequate corporate transparency related inefficient corporate boards and to information disclosure about ownership structure. The CPF anticipates that improvements will be made to increase the independence of corporate boards and enhance the protection of minority shareholders.

**27. High quality accounting, auditing, and disclosure in publicly available financial statements enables improved transparency and accountability.** These financial statements are particularly important in creating a level playing field for investors and in helping to foster the environment necessary for both financial sector and capital market development by attracting institutional investors. They also help to

encourage enterprises to operate within the formal economy, thereby making it easier to ensure they are paying the appropriate level of taxation and contributing to improved fiscal sustainability. Publicly available, high quality corporate financial reporting that is reliable, accurate, and comparable will promote increased confidence and trust by investors, lenders, and creditors.

**28. The objective of achieving the United Nations Sustainable Development Goals requires good corporate financial reporting.** The achievement of the Goals relies on dramatically increased public spending, which in turn needs to be funded by improved tax administration and a broader and deeper tax base. Corporate financial reporting quality and transparency help to improve corporates' access to capital and lowers the cost of capital, thus enabling the economic growth that broadens and deepens the tax base thus boosting the country's tax revenues. The increased transparency might also contribute towards strengthening the tax administration system that could potentially reduce tax evasion.

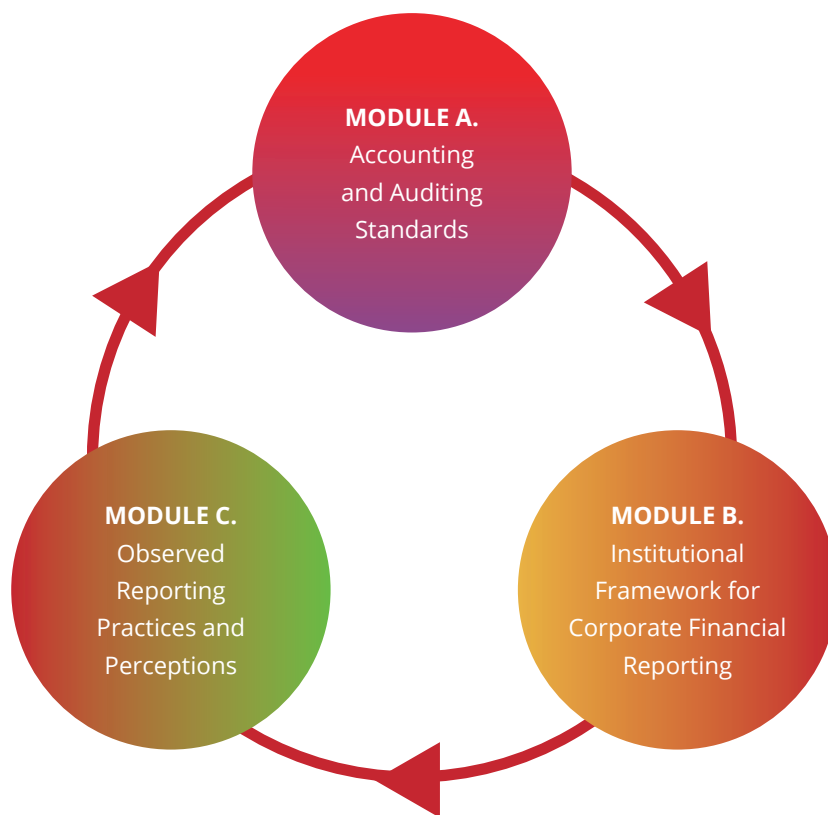
**29. This assessment was conducted at the request of the Government of Georgia and builds on the previous ROSC A&A in 2015.** Following the recommendations in the ROSC A&A 2015, Georgia implemented comprehensive reforms of the corporate financial reporting and audit frameworks and processes starting in 2016. The next stage should build on these earlier achievements to complete implementation of the remaining activities and address new recommendations. See **Annex A** for a summary of progress on ROSC A&A 2015 recommendations. The data and other information used for the review were gathered using the revised ROSC A&A 2.0 diagnostic (see **Figure 1**). Practices were then benchmarked against international standards and good practices to provide the basis for the policy recommendations included in **Section IV. Key Findings and Areas for Consideration**. The recommendations are intended to assist the promotion of:

- i. private sector led growth through increased regulatory and market efficiency;

- ii. development of the financial and capital markets; and
- iii. improved accountability and transparency (including sustainability reporting). Increasing the

degree of alignment with international standards and good practices for corporate financial reporting is a key driver of improvement of the overall standard of corporate governance.

**Figure 1.** ROSC A&A 2.0 Assessment Methodology





## II. ASSESSMENT

### **A. Accounting & Auditing Standards**

30. This section assesses the extent to which the national accounting and auditing standards follow international benchmarks – IFRS or the IFRS for SMEs accounting standards and ISA and International Standard on Quality Control (ISQC)<sup>16</sup> for auditing. The quality of national standards and how they are applied in practice impacts on the reliability and comparability of financial information for users, especially current or potential investors, lenders, and creditors. The national standard setting process is reviewed in **Section II.B.10 Setting Accounting and Auditing Standards**. The application of national standards is reviewed in **Section II.C Observed Financial Reporting Practices and Perceptions**.

### Accounting Standards Gap

31. Accounting standards provide the basis on which entities prepare their general-purpose financial statements. They include both general and specific requirements that must be followed by preparers of financial statements when: (i) determining the scope and format of the financial statements; (ii) establishing and applying their entity-specific accounting policies for the different types of transactions they enter into and the circumstances and events that the reporting entity is subject to; and (iii) determining the extent of disclosures presented in the notes to the financial statements.

32. The Law on Accounting, Reporting, and Audit<sup>17</sup> mandates the full adoption of IFRS by PIEs and large entities, and the IFRS for SMEs by medium and

<sup>16</sup> Replaced by International Standards on Quality Management (ISQM) 1 and 2 in December 2020, effective from December 15, 2022.

<sup>17</sup> Law on Accounting, Reporting, and Audit, dated June 8, 2016.

small businesses in the country. Details are provided below in **Section II.B.1. General Financial Reporting Requirements**.

## Auditing Standards Gap

**33. Auditing standards provide a basis for auditors to follow when they conduct their audits and provide their audit opinions.** The auditor gives their opinion as to whether or not the financial statements present fairly (or give a true and fair view of), in all material respects, the financial position and the financial performance of the company in accordance with the applicable financial reporting standards.

**34. The Law on Accounting, Reporting, and Audit mandates the full adoption of ISA.** The Law states that audits in Georgia are conducted in compliance with the ISA (specifying the ISA adopted by the IAASB or its successor in title). Considering the development by IAASB of a new separate standard for audits of financial statements of less complex entities, the approval of which is expected by December 2023, SARAS should be prepared for its adoption in Georgia, with necessary changes in the respective laws and regulations.

**35. The Law was amended in December 2022 to adopt ISQM 1 and 2.** The Law states that an auditor/audit firm shall be obliged to have proper policies and procedures for its quality management system in accordance with ISQM 1 and 2.<sup>18</sup>

## Performance Indicators – Financial reporting and auditing standards

**36. The overall rating attributed to Georgia under the performance indicator “Financial Reporting and Auditing Standards” is 4, as both sub-indicators are assessed with the highest possible score.**

### Sub-indicator A. Financial reporting standards

A.1. Financial reporting standards	
Georgia Rating	4 Adoption of IFRS and the IFRS for SMEs without modification is fully mandated by Law, except for microenterprises, which conforms with IFRS Foundation advice for the adoption of IFRS.
Rating Criteria	1 Criteria for “2” rating not met.
	2 A majority of adopted standards align or converge with IFRS.
	3 Most adopted standards align or converge with IFRS.
	4 All adopted standards align with IFRS.

### Sub-indicator B. Auditing standards

B.1. Auditing standards	
Georgia Rating	4 Adoption of ISA and ISQC1, now superseded by ISQMs 1 and 2, without modification is fully mandated by Law.
Rating Criteria	1 Criteria for “2” rating not met.
	2 A majority of adopted standards align or converge with ISA and ISQC.
	3 Most adopted standards align or converge with ISA and ISQC.
	4 All adopted standards align with ISA and ISQC.

<sup>18</sup> ISQM 1 and 2 were adopted by the IAASB and replaced the International Standard on Quality Control (ISQC1) as of 15 December 2022.

## **B. Institutional Framework for Corporate Financial Reporting**

**37. The key regulator in the institutional framework for corporate financial reporting in Georgia is SARAS.** The Law on Accounting, Reporting, and Audit specifies that SARAS is responsible for a unified policy of introducing IFRS and exercising control over their application. SARAS is a subordinated agency under the MoF, which ensures state supervision of accounting, reporting, and auditing in accordance with the Georgian legislation. The functions, structure, and management of SARAS is set out in a Decree.<sup>19</sup> When fulfilling its functions, SARAS acts on behalf of the state and is funded by the state budget.

**38. SARAS enforces the mandatory international standards relevant to corporate reporting, monitors compliance with the financial reporting standards, and determines the rules for and conducts the monitoring of auditors' quality control system and compliance with auditing standards.** SARAS is also responsible for: (i) putting into effect the mandatory international standards and other norms provided for by the law; (ii) translation and publication of those standards; (iii) creating and managing the system for submission and publication of financial statements (REPORTAL); (iii) defining the financial reporting standards for enterprises of the fourth category (microenterprises) and for non-commercial entities; (iv) assisting in the development of educational programs in the field of accounting, auditing, and financial reporting in accordance with IFRS/the IFRS for SMEs; (v) conducting monitoring of auditors' quality; and (vi) cooperating with PAOs and conducting regular consultations in order to improve the accounting system.

**39. The governing body of SARAS is the Accounting, Reporting, and Auditing board.** The board is authorized to: (a) review drafts of normative acts defined under the Law of Georgia on Accounting, Reporting, and Audit; (b) submit proposals to the

Head of SARAS on amendments to the normative acts; (c) provide consultations to the Minister of Finance with respect to the candidacy of the Head of the Service and submit the board's position in the form of a recommendation; (d) review appeals related to decisions made by SARAS on accounting, reporting, and auditing issues; and (e) perform other activities provided under the Law.

**40. The composition of the board is defined under the Law of Georgia on Accounting, Reporting, and Audit.** The board consists of seven members. All board members shall be non-practitioners who are qualified professionals, experienced and competent in the areas of accounting and reporting, audit, economics, finance, business administration, or law, with at least seven years of experience in one of the above fields. According to the Law, a non-practitioner is any person who, for at least three successive years prior to appointment as a member of the board, has not carried out auditing (service), has not held voting rights in an audit firm, has not been employed by an audit firm, and has not been a member of the management or supervisory body of an audit firm, or otherwise associated with it.

**41. The board consists of one member from each of the MoF, the board of the NBG, the MoESD, the State Insurance Supervision Service of Georgia; and one member each nominated from professional organizations, from business associations, and from an academic institution.** According to the Law, the process of board member selection shall be independent and transparent.

**42. At the board's discretion, SARAS staff and other invited persons may attend the board meeting.** Such persons shall not take part in the decision-making process.

**43. The Law stipulates that a board member shall not take part in a review or resolution of an issue if there is a conflict of interest with respect to the dispute.** A person whose case is being reviewed shall be entitled to request the recusal of a respective board member, if the latter has a personal interest in

<sup>19</sup> Decree of the Minister of Finance of Georgia No 223 On Approving the Regulation of the Service for Accounting, Reporting and Auditing Supervision (SARAS) dated September 14, 2016.



the issue being reviewed. A member of the board, as well as his/her family members, shall not be entitled to hold stock or capital shares, or voting rights, in an audit firm that is subject to supervision by SARAS.

**44. Participation on the board requires considerable time and personal resources but the members of the board/chairman are not compensated.** This can lead to challenges in gaining quorum for board meetings. Changes to board members can often lead to delays of the activities of the board. In some cases, the board has been unable to meet for a number of months due to the process of staffing the board. As a result, it is often not possible to review complaints submitted to SARAS within a year of submission.

**45. During 2021, 33 complaints were submitted to the board, of which only 16 complaints were able to be considered during 2021.** In 2022, 31 complaints were submitted to the board of which only 24 were considered in 2022. The complaints unattended during a calendar year are carried over to the next year.

**46. It is particularly challenging for the board to consider complicated technical issues relating to audit quality control inspections where the auditor subject to the review is in dispute with SARAS.** The non-payment of board members restricts available time and resources, and not all board members have detailed technical knowledge of audit matters. The majority of the board members have no specific experience in audit or preparation of IFRS financial reports, particularly those board members that represent state institutions. In addition, the board members representing the state institutions have limited availability to participate in the dispute resolution processes and in some cases the discussions of the complaints by the board are significantly delayed. The above factors significantly limit the effectiveness of the SARAS board to fulfill its mandate. SARAS should consider if there is a need to enhance the composition, capacity and competencies of the SARAS board to increase its effectiveness. It should also consider establishing a dispute resolution

mechanism with paid independent audit experts to resolve this challenge.

**47. SARAS has recently added supervision of aspects of the regulation of anti-money laundering (AML) to its responsibilities.** It is preparing for a program of AML inspections. It is also preparing for the challenge of establishing a comprehensive register of accountants and accountant firms.

**48. In addition to SARAS, commercial banks, microfinance institutions, and listed companies are supervised by the NBG, while the insurance industry is supervised by the ISSSG.** The primary focus is on compliance with prudential reporting requirements as well as with submission of both prudential and annual financial reports. Further details are provided below in relevant sections for each of the above industries. This report describes general regulatory, supervisory and enforcement powers of the financial regulators, as defined in law and regulations in Georgia. However, an assessment has not been performed on the detailed implementation and application of those legal powers, other than as evidenced in the external reports of regulators themselves and the quality of annual financial statements produced. Other reports produced by the World Bank do provide assessments of implementation and application.<sup>20</sup>

## 1. General Financial Reporting Requirements

### Commercial Enterprises (including SMEs)

**49. The Law on Entrepreneurs<sup>21</sup> defines that business activities in Georgia may be carried out by an individual entrepreneur (as a natural person) or a company (as a legal person).** The company can be established as a general partnership, a limited partnership, a limited liability company (LLC), a joint-stock company (JSC), or a cooperative.

<sup>20</sup> Financial Sector Assessment Program : Technical Note on Capital Market Development <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099840203012223862/p175014035c7470db0908e08f6202817c09>

Georgia - Financial Sector Assessment Program : Technical Note on Selected Issues in Banking Supervision <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099840003012224721/p175014039b1870910b7590127ef9a58031>

<sup>21</sup> The Law of Georgia on Entrepreneurs, dated August 2, 2021

50. There is a good progress with aligning Georgia's legislation with the EU relevant requirements in accounting, financial reporting and auditing, while further alignment is still needed. The areas for further alignment, particularly, should include (i) introducing in the law of the definition of "key audit partner"; (ii) including in the auditor registration requirements the disclosures of audit firm's office locations and about the network ; (iii) covering by law the mechanism for possible delegation of tasks by SARAS to other bodies; and (iv) introducing in law the definition and the description of the auditor's annual transparency report.

51. PIEs are defined in the Law on Accounting, Reporting, and Audit and, for financial reporting purposes, all commercial entities are classified into four categories based on their volume of total assets, total revenue, and the average number of persons employed. The categories' definitions are broadly in line with the approach and limits set in the EU directives.

52. An entity is categorized as a fourth category enterprise if its indicators, at the end of the reporting period, met at least two criteria out of the following: (1) the total value of assets does not exceed GEL 1 million;<sup>22</sup> (2) the revenue does not exceed GEL 2 million;<sup>23</sup> and (3) the average number of persons employed during the reporting period did not exceed ten.

53. An entity which is not an enterprise of the fourth category is categorized as a third category enterprise if its indicators, at the end of the reporting period, met at least two criteria out of the following: (1) the total value of assets does not exceed GEL 10 million;<sup>24</sup> (2) the revenue does not exceed GEL 20 million; and (3) the average number of persons employed during the reporting period did not exceed 50.

54. An entity which is not an enterprise of the third or the fourth category is categorized as a second category enterprise if its indicators, at the end of the reporting period, met at least two criteria out of the following: (1) the total value of assets does not exceed GEL 20 million;<sup>25</sup> (2) the revenue does not exceed GEL 50 million; and (3) the average number of persons employed during the reporting period did not exceed 250.

55. An entity is categorized as a first category enterprise if at the end of the reporting period it met at least two criteria out of the following: (1) the total value of assets exceeded GEL 50 million;<sup>26</sup> (2) the revenue exceeded GEL 100 million;<sup>27</sup> and (3) the average number of persons employed during the reporting period exceeded 250.

56. A PIE is defined as (1) an accountable enterprise whose securities are admitted to trading on a stock exchange in accordance with the Law on Securities Market,<sup>28</sup> (2) a commercial bank, in accordance with the Law on the NBG,<sup>29</sup> (3) a microfinance organization, in accordance with the Law on Microfinance Organizations,<sup>30</sup> (4) an insurer, in accordance with the Law on Insurance,<sup>31</sup> (5) a founder of a non-state pension scheme, in accordance with the Law on the Provision of Non-state Pensions and Non-state Pensions Insurance,<sup>32</sup> (6) an investment fund, in accordance with the Law on Investment Funds,<sup>33</sup> and (7) a person defined as a PIE by SARAS on the basis of the criteria approved by the Government of Georgia (except for the NBG), which are first and second category SOEs. The above PIE definition is overall in line with the EU definition of PIEs in Directive 2013/34/ EU.

<sup>22</sup> Around €346.7 thousand (as per the exchange rate on 31 December 2022)

<sup>23</sup> Around €693.5 thousand (as per the exchange rate on 31 December 2022)

<sup>24</sup> Around €3.5 million (as per the exchange rate on 31 December 2022)

<sup>25</sup> Around €6.9 million (as per the exchange rate on 31 December 2022)

<sup>26</sup> Around €17.3 million (as per the exchange rate on 31 December 2022)

<sup>27</sup> Around €34.7million (as per the exchange rate on 31 December 2022)

<sup>28</sup> Law of Georgia on Securities Market, no. 1745,1998 (latest update in 2022)

<sup>29</sup> Organic Law of Georgia on the NBG, no. 1676, 2009 (Last update in 2022)

<sup>30</sup> Law of Georgia on Microfinance Organizations, no 3482, 2006 (last update in 2022)

<sup>31</sup> Law of Georgia on Insurance, no 690, 1997 (last update in 2022)

<sup>32</sup> Law of Georgia on the Provision of Non-state Pensions and Non-state Pensions Insurance, no. 1679, 1998 (last update in 2022).

<sup>33</sup> Law of Georgia on Investment Funds, no. 6805, 2020 (last update in 2022).

**Table 3.** Numbers of entities within each financial reporting category

Category	Number of active entities (as of December 2022)	Number of entities that submitted annual reports to SARAS	Number of annual reports published on REPORTAL	Compliance rate
PIEs	135	126	126	93%
First	135	111	108	83%
Second	643	545	535	85%
Third	4,757	4,384	4,191	92%
Fourth	91,753	69,901	69,817	76%
Total	97,423	75,067	74,777	77%

Source: SARAS

## Accounting and Reporting Requirements

**57. The accounting framework requires full adoption of IFRS and the IFRS for SMEs without modifications.**<sup>34</sup> The full adoption of IFRS was introduced by a law in 2000, and adoption of the IFRS for SMEs in 2012. The criteria for enterprises to adopt IFRS, the IFRS for SMEs, or simplified rules established by the Government of Georgia are clearly defined in the current Law on Accounting, Reporting, and Audit. The Law specifies that the effective (English) edition of the above standards can be used. PIEs and enterprises (and groups) of the first category are required to carry out accounting and financial reporting in accordance with IFRS. Enterprises (and groups) of the second and third categories are required to carry out accounting and financial reporting in accordance with the IFRS for SMEs, but they can apply IFRS instead. Enterprises of the fourth category are required to carry out accounting and financial reporting in accordance with the simplified standards established by SARAS — national generally accepted accounting principles (GAAP) — but they can apply IFRS or the IFRS for SMEs instead. Consolidation of the financial statements is required for groups of the first, second, and third

categories. Fourth category groups are not required to prepare consolidated financial statements. If an entity/group does not meet at least two criteria out of the three provided above by the end of two consecutive reporting periods, the size category of the entity/group shall be changed, and the requirements established for the relevant category shall be applied. There is some simplification of financial reporting requirements by entity (and group) categories, particularly, with regards to second and third category of entities (and groups) applying the IFRS for SMEs, and fourth category of entities using national GAAP. Further financial reporting simplifications are needed to meet the equivalent EU requirements, in line with Georgia's commitment under the Association Agreement to approximate its institutions and policies with those of the EU.

**58. The Law on Accounting, Reporting, and Audit requires PIEs and first, second, third, and fourth category entities, other than SOEs to submit for publication their AFS (including consolidated statements), management reports (including a consolidated report),<sup>35</sup> reports on payments to the State (as defined by the law),<sup>36</sup> and audit reports**

<sup>34</sup> Except for microenterprises.

<sup>35</sup> Management reports are required only for PIEs and first and second category entities and should include a) a review of activities; b) a corporate governance report (only for entities, whose securities are admitted to trading on a stock exchange in accordance with the Law on Securities Market.); and c) a non-financial statement for PIEs with over 500 employees.

<sup>36</sup> Annual report on payments to the state are required only for PIEs and first category entities, whose activities involve the use of subsoil (including oil and gas extraction) or timber harvesting in a natural forest. The report should reflect payments made to the state in cash or in kind, in the form of profit tax, license and natural resources fees, regulation fees for the use of natural resources, royalties, dividends, bonuses determined by the Law on Oil and Gas, or rent and concession fees, if a one-off payment or total of payments exceeds GEL 100,000 during the reporting period.

no later than October 1 of the year following the reporting period or not later than nine months from the end of the reporting period in case the reporting period of an entity does not coincide with the calendar year. SOEs are required to submit their audited AFS by July of the year following the reporting period. Listed companies, commercial banks, insurance, and microfinance entities are subject to additional requirements by their regulators on the frequency of financial reports and disclosures, as discussed in detail in the next sections of this report. The reports are submitted to SARAS through the REPORTAL public reporting electronic portal, which should ensure that the submitted reports are publicly available within one month after their submission. The REPORTAL is administered by SARAS, which verifies that financial statements are filed on time,<sup>37</sup> consolidation requirements are met, statements have been audited where required, and there is compliance with the requirements of the applicable standards as well as filing procedures. It was noted that some PIEs operating in regulated sectors are required to provide audited annual reports to their regulators at a date earlier than they are required to publish those annual reports on REPORTAL. With this consideration, the ROSC assessment recommends that the date for publication of PIEs' annual reports in REPORTAL and elsewhere be aligned more closely with the requirements by regulators for earlier finalization of those annual reports.

**59. The use of publicly available financial information could be significantly enhanced via introduction of digital reporting, which would also improve the data quality and make it comparable across different jurisdictions.** This would also help to comply with the requirements of EU Directive 2022/2464 to introduce a single electronic format for PIEs. A feasibility study on implementation of the XBRL<sup>38</sup> standard was conducted in 2022 with the support of the World Bank STAREP project.<sup>39</sup> This concluded that the XBRL standard could be considered for financial reporting in Georgia. It would enrich SARAS' REPORTAL database, which would increase its usage by various stakeholders, allowing

time and cost savings, a faster review and evaluation process, more reliable and accurate handling of data, and improved analysis and decision-making. As a digital reporting standard, XBRL makes reporting more harmonized, enables more efficient use of the reports, and facilitates comparability of the reports. The XBRL standard enables using common technical (digital) formats and thus facilitates data comparability via information harmonization (standardization), at the same time improving the quality and reliability of information submitted by the entities. Implementation of the XBRL standard would have a number of expected benefits for a wide range of users of financial/non-financial (sustainability) information, including improved regulatory compliance if other state bodies also participate in XBRL implementation.

### Auditing Requirements

**60. The Law on Accounting, Reporting, and Audit has a statutory audit requirement for PIEs and first and second category entities/groups' AFS, while entities in the third and the fourth categories are exempted from having their AFS audited.** The Law requires that audits are conducted in compliance with the ISA issued by the IAASB or its successor in title. The Law specifies that the effective (English) edition of the standards can be used.

**61. External auditors of PIEs are appointed by the entities' shareholders general meetings based on the recommendations of audit committees.**<sup>40</sup> The Law requires that an engagement for PIE audits may be concluded for no less than two years and no longer than ten years. In case of winning a public tender conducted upon a decision of the PIE's shareholders meeting, the engagement can be extended for another ten-year period. After the expiry of the above periods, a subsequent engagement with the same auditor may not be concluded within a four-year period. The auditor is required to ensure the internal rotation of engagement partners and key personnel in respect of each PIE that it serves, at least once in seven years.

<sup>37</sup> Apart from separate monitoring and enforcement of the non-submission by other relevant regulators (such as NBG for banks, listed companies, ISSSG for insurance, etc.)

<sup>38</sup> <https://www.xbrl.org/>

<sup>39</sup> <https://cfr.worldbank.org/programs/starep>

<sup>40</sup> The Law of Georgia on Entrepreneurs, Article 57(7)

## Corporate Governance

**62. The Law on Entrepreneurs specifies that the governing bodies of a company are a general meeting, a management body (board of directors), and a supervisory board, if the establishment of the latter is provided by a law or a statute.** The Law requires holding a shareholders' annual general meeting (AGM) at least once a year, no later than within six months after drawing up the annual balance sheet.

**63. There are three separate corporate governance codes in Georgia: Corporate Governance Code for Commercial Banks (CGCCB),<sup>41</sup> Corporate Governance Code for the Issuers of Public Securities (CGCI),<sup>42</sup> and CGCSOE.<sup>43</sup>** The requirements of the banking code are mandatory for all commercial banks.<sup>44</sup> Listed companies and SOEs should follow the "comply or explain" principle.<sup>45,46</sup> The Law on Commercial Banks specifies that the supervisory board retains primary responsibility for corporate governance of a commercial bank.<sup>47</sup> The CGCCB also specifies that the supervisory board retains primary responsibility for corporate governance of commercial banks.<sup>48</sup> At least one-third of a commercial bank's supervisory board members, but no less than two, should be independent members. Similarly, the CGCSOE specifies that the supervisory board is responsible for the corporate governance of the enterprise.<sup>49</sup> All members of the SOE's supervisory board should be independent.

**64. The EU audit directive specifies that a majority of members of audit committee shall be independent of the of audit entity, while the Law of Georgia on Entrepreneurs requires that an audit committee, with at least one independent member, should be established within a supervisory board of a PIE.<sup>50</sup>** The law further specifies that for PIEs with no supervisory board, an independent audit committee shall be established, the members of which shall be independent

persons elected by the AGM. A member of the audit committee shall have competence in the field of activities of the undertaking. At least one member of the audit committee shall have competence in accounting and/or auditing, which is in line with the respective requirement of the EU audit directive. The Law also specifies that the audit committee shall supervise the financial reporting process, make recommendations for ensuring the accuracy of financial information, and for the auditor/audit firm to be appointed by the AGM. The audit committee also presents to the supervisory board or AGM the results of the audit, the effect of the audit on the veracity of the financial statements, and the involvement of the audit committee in that process. While the Law does not have a specific requirement for external auditors to attend the shareholders' AGM, such a requirement is specified in the CGCI.<sup>51</sup>

## Performance Indicators – General Financial Reporting Requirements

**65. The attributed rating is 4, which equals the simple mean of the rating criteria comprising sub-indicators A.1-A.2 below (i.e.,  $4 = (4+4)/2$ ).**

*Sub-indicator A. General financial reporting requirements*

A.1. Simplified financial reporting	
Georgia Rating	<b>4</b>
	Financial reporting simplifications are clearly differentiated by size of entities and groups and differentiation is based on at least 3 criteria. Definitions and values for turnover, total assets, and number of employees are clear. Classification is clear on when an entity should move from one classification category to another.

<sup>41</sup> Decree (No. 215/04 dated September 26, 2018) of the NBG President.

<sup>42</sup> Decree N172/04 of December 7, 2021 of the President of the NBG "On approval of Corporate Governance Code for the Issuers of Public Securities".

<sup>43</sup> Decree #1618 of the Government of Georgia, September 8, 2021.

<sup>44</sup> CGCCB, Article 1.2

<sup>45</sup> CGCI, Article 2.4

<sup>46</sup> Decree of the Government of Georgia on Approval of Corporate Governance Code for State-owned Enterprises, Article 3.F

<sup>47</sup> The Law of Georgia on Commercial Bank activities, Article 14.1

<sup>48</sup> CGCCB, Article 3.1

<sup>49</sup> CGCSOE, Article 3.2

<sup>50</sup> The Law of Georgia on Entrepreneurs, Article 57

<sup>51</sup> CGCI, Article 22.6

A.1. Simplified financial reporting		
Rating Criteria	1	Criteria for '2' rating not met.
	2	Financial reporting simplifications exist in the legal framework, and these are based on an entity's legal form.
	3	Financial reporting simplifications differ for some categories of entities and groups, differentiated by size and differentiation is based on 1-2 criteria.
	4	Financial reporting simplifications are clearly differentiated by size of entities and groups and differentiation is based on at least 3 criteria.

A.2. Exemptions to perform statutory audits		
Georgia Rating	4	Auditing exemptions are clearly differentiated by size of entities and groups and differentiation is based on at least 3 criteria. Definitions and values for turnover, total assets, and number of employees are clear. Classification is clear on when an entity should move from one classification category to another.
Rating Criteria	1	Criteria for '2' rating not met.
	2	Auditing exemptions exist in the legal framework, and these are based on an entity's legal form.
	3	Auditing exemptions differ for some categories of entities and groups, differentiated by size and differentiation is based on 1-2 criteria.
	4	Auditing exemptions are clearly differentiated by size of entities and groups and differentiation is based on at least 3 criteria.

## 2. Listed Companies

### Overview of the Securities and Exchange Market

66. There are currently two stock exchanges authorized to operate in Georgia. The GSE<sup>52</sup> is the only currently active exchange (established in 1999)<sup>53</sup> and is the holding company of the Tbilisi Stock Exchange (TSE).<sup>54</sup> Neither exchange is affiliated with any networks of other exchanges. The TSE is designed as a fully electronic exchange. It is GSE's intent that companies currently listed on the GSE will be migrated to the TSE over time.

67. There are three listing segments of the GSE: A listing, B listing, and Admitted to Trading. The A and B segments both require an issuer to have submitted audited reports for at least two prior years before being admitted to the Exchange. The GSE also reviews credit ratings and the entity's experience in its main business activity. None of these requirements are applied to entity's applying for the Admitted to Trading category. Thirteen securities were listed in the A section (twelve bonds and one equity listing), eighteen in the B section (fifteen bonds and three equity listings) and four in the Admitted to Trading section (all equity listings).<sup>55</sup>

68. The eight listed equities were all domestic companies and had a total market capitalization of GEL 2,290 million at quarter end March 2023.<sup>56</sup> Two entities listed on the exchange were dual listed. There were no listed companies owned or controlled by the state, and no listed subsidiaries of international holding companies. The trading volumes for the 12 months ended 31 December 2022 comprised 19 trades of a total of 1,253,978 shares and a value of GEL 13,619.<sup>57</sup> The 27 listed non-equity instruments comprised 19 corporates bonds, seven International Financial Institution bonds and one Global depository note. Fifteen trades in US\$ denominated bonds were recorded in the year ended 31 December 2022, with value of US\$ 2,444,612.<sup>58</sup>

<sup>52</sup> <https://gse.ge> 19 June 2023

<sup>53</sup> The Law of Georgia on Securities Market

<sup>54</sup> Not active at the time of the assessment

<sup>55</sup> GSE, December 31, 2021

<sup>56</sup> <https://www.gse.ge/capitalizations>

<sup>57</sup> <https://www.gse.ge/en/trades>

<sup>58</sup> <https://www.gse.ge/en/trades>

69. The securities market in Georgia is regulated by the Law on Securities Market. NBG is the regulator responsible for all financial system supervision other than for the insurance sector. The functions and duties of NBG are determined by the Constitution and by the Law on the NBG. In accordance with the Constitution,<sup>59</sup> NBG is responsible for the implementation of monetary policy to ensure price stability as well as for the stable operation of the financial sector. The securities market regulations also include the GSE Listing Rules<sup>60</sup> and the CGCI.<sup>61</sup>

70. The supervisory powers of NBG for capital market participants are set out in the Law on the NBG.<sup>62</sup> The scope of the Law includes brokerage companies, securities registrars, stock exchanges, central and specialized depositories, asset management companies, investment funds, and reporting companies. NBG is empowered to issue decrees, regulations, and guidelines and to impose sanctions on capital market participants.

71. The Law on Securities Market<sup>63</sup> details further specific requirements for securities market supervision and appropriate sanctions. NBG is entitled to apply escalating sanctions against the regulated participants of the securities market and/or against a member of their managing bodies (supervisory board or directors) depending on the seriousness of such violation. These sanctions range from the issue of written warnings to the revocation of licenses and includes fines and the discontinuance or suspension of transactions.

### Financial reporting requirements for listed companies

72. PIEs, which include all listed entities, are required by the Law of Georgia on Accounting, Reporting, and Audit to submit to SARAS for publication their AFS, including management reports and audit reports,

no later than October 1 of the year following the reporting period. These reports must be prepared in accordance with IFRS. The mechanism for publicly disclosing financial reports is the SARAS REPORTAL system.

73. However, listed companies are required by the Law of Georgia on Securities Markets to publish their AFS earlier than the general requirements. They must file their AFS with the NBG by May 15 in the year immediately following the company's December year-end.<sup>64</sup> They must also publish the financial statements by this earlier date on the SARAS REPORTAL system.

74. The financial statements of selected listed companies were reviewed as part of the observed financial reporting practices and perceptions. The review concludes that non-bank GSE-listed institutions reviewed likely did not comply with at least some significant aspects of IFRS accounting standards. For details see **Section C. Observed Financial Reporting Practices and Perceptions** of this report.

75. Listed companies are required to submit management reports. An annual management report should be prepared and reviewed by an auditor in accordance with rules determined for PIEs.<sup>65</sup> The management report must contain an activities review, a corporate governance report, and a non-financial statement. In addition, the management report of a listed company should contain information about the participation of members of the management body in the capital of the company.

76. Semi-annual financial reports (interim reports) are also required to be prepared by the listed company in accordance with IFRS.<sup>66</sup> Interim reports must be published through the SARAS REPORTAL system no later than August 15 of each year. A review by auditors is not required. An interim management report must accompany the interim report and should cover at least the first six months of the financial year. It must contain description and analysis of important

<sup>59</sup> The Constitution of Georgia. Article 68.

<sup>60</sup> Approved by the GSE Supervisory Board on October 4, 2018 (with last update on November 18, 2021).

<sup>61</sup> Approved on December 7, 2021, by Decree (N172/04) of the NBG President.

<sup>62</sup> Organic Law of Georgia on the NBG. Article 48.

<sup>63</sup> The Law of Georgia on Security Markets. Article 55<sup>1</sup>.

<sup>64</sup> The Law of Georgia on Securities Markets, Article 11.2

<sup>65</sup> The Law of Georgia on Accounting, Reporting, and Audit and Decree No181/04 of October 7, 2020, of the Governor of the NBG on the Approval of the Rule Regarding Disclosure Requirements in Relation to the Information About Issuers and Appointing Registrar to the Issuer. Article 3.4.

<sup>66</sup> The Law of Georgia on Securities Markets and Decree No181/04 of October 7, 2020, of the Governor of the NBG on the Approval of the Rule Regarding Disclosure Requirements in Relation to the Information About Issuers and Appointing Registrar to the Issuer.

events of the first six months, including their impact on the interim report and a comprehensive overview of the issuer's main key risks and challenges for the remaining six months of the financial year.

**77. NBG oversees the compliance of listed companies with the requirement to publish annual and interim reports through the REPORTAL system (see paragraph 58).** NBG relies on SARAS for the review of the content of annual reports. Any non-compliance is reported by SARAS to NBG to determine and carry out appropriate remedial or sanctioning measures (typically warnings, instructions, or fines). NBG checks the published interim reports with the requirements established by the law applying a risk-based approach.

**78. NBG operates independently from the government and commercial sector.**<sup>67</sup> Legislative, executive, and other bodies are not entitled to interfere in its activities except in cases prescribed by the Georgian constitution.

**79. The corporate reporting requirements for listed companies are well aligned with the general financial reporting framework administered by SARAS.** This is due to formalized inter-agency co-operation (one window principle) that largely unites the reporting system within Georgia.

## Statutory audit and other forms of independent assurance

**80. The AFS of issuers of public securities are required to be audited by the auditor of PIEs (see paragraph 60).**<sup>68</sup> The adoption of international standards is ensured by SARAS within six months after their renewal.<sup>69</sup> The Listing Rules of the GSE require that issuers whose securities are admitted to trading

submit an audited AFS to the stock exchange.<sup>70</sup>

**81. SARAS approves audit firms that are permitted to perform the audit of PIEs (including listed entities) based on both quantitative and qualitative criteria.**<sup>71</sup>

The process includes in-depth inspection of audit firms' processes on a regular basis. NBG relies on the SARAS process to identify and regulate auditors, who are permitted to perform audits on PIEs, and does not have a process of its own. An auditor of a PIE must have more than 15 years' audit experience. Auditors and audit firms approved for the audit of PIEs are published on the SARAS website.<sup>72</sup>

**82. Audit firms of PIEs (including listed entities) in Georgia are rotated.**<sup>73</sup> Audit partners are required to be rotated every seven years which is in line with the EU Audit Regulation requirement. Audit firms are required to be rotated every 10 years. If an incumbent audit firm wins a public tender, conditional on decision of the meeting of the partners/shareholders, a 10-year period may be extended for an additional 10 years. The law also established a mandatory cooling off period of four years.

**83. There are no explicit restrictions on the non-audit services which audit firms are allowed to provide to their audit client.** General independence rules apply, and auditor must be independent from the entity to which it provides audit services.

**84. There are no specific requirements for listed entities governing the appointment and termination of auditors.** The AGM of a PIE is entitled to make a decision on the appointment or withdrawal from an agreement concluded with an auditor, based on the recommendation of the audit committee.<sup>74</sup> There are no special provisions indicating the rights of boards of directors regarding the appointment/termination of auditors.<sup>75</sup>

<sup>67</sup> The Organic Law of Georgia on the NBG, Article 4.2

<sup>68</sup> Decree No181/04 of October 7, 2020, of the Governor of the NBG "On the approval of the rule regarding disclosure requirements in relation to the information about issuers and appointing registrar to the issuer", Article 3.2

<sup>69</sup> The Law of Georgia on Accounting, Reporting, and Audit: Article 1, Article 2.1, and Article 14

<sup>70</sup> GSE Listing Rules, Article 7

<sup>71</sup> [https://www.saras.gov.ge/Content/files/11-09-2018/Rule\\_for\\_Performing\\_Quality\\_Control\\_System\\_Monitoring\\_2018.07.26\\_ENG.pdf](https://www.saras.gov.ge/Content/files/11-09-2018/Rule_for_Performing_Quality_Control_System_Monitoring_2018.07.26_ENG.pdf)

<sup>72</sup> [www.saras.gov.ge/en/Companies](http://www.saras.gov.ge/en/Companies)

<sup>73</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 16.15

<sup>74</sup> The Law of Georgia on Entrepreneurs, Article 57.7 and Article 58.1

<sup>75</sup> The CGCI (refer paragraph 100 below), article 9, introduces requirements for the audit committee to evaluate and make recommendations the Board or shareholders on the appointment/reappointment of external auditors. The required evaluation includes annually reviewing external auditor independence.



**85. SARAS must be notified of the resignation or termination of the auditor.** Appropriate substantiation must be provided for the decision. There is no requirement for resignation or termination to be reported to NBG. However, the change of the auditor must be publicly disclosed by the issuer through its website, the website of the GSE, or through other appropriate means.<sup>76</sup>

## Audit committees

**86. PIEs are required to establish an audit committee within the supervisory board.**<sup>77</sup> The Law on Securities Market includes an identical requirement and further requires that the audit committee be charged with controlling the authenticity of the issuer AFS, the efficiency of its internal control system, and the independence of its internal audit function (if applicable).<sup>78</sup> It also requires that the audit committee manages the relationship with, and legal observance by, the external auditor.

**87. An audit committee of a PIE must be comprised of members of the supervisory board and at least one independent member.**<sup>79</sup> An independent member is defined as a person with no legal and/or economic relations with the undertaking, who holds no shares in the undertaking, and receives no remuneration or other economic benefits from the undertaking, other than the remuneration determined for membership of the supervisory board and/or the audit committee. A member of the audit committee must be competent in the field of activities of the undertaking. At least one member of the audit committee must be competent in accounting and/or auditing.<sup>80</sup> Audit committee members, including the chair, must have an ability to analyze financial statements and have financial education or relevant financial experience.<sup>81</sup> In addition, the Securities

Law requires that the audit committee chair be an independent person as defined.<sup>82</sup> CGCI prohibits a former partner or director of the current auditor from being a member of the audit committee if the person still has any type of financial interest at the auditor or within 12 months of leaving positions as partner or director of the auditor.<sup>83</sup>

**88. An audit committee is required to supervise the financial reporting process and the annual audit.**<sup>84</sup>

The supervisory responsibilities are met in part based on the opinions provided in a quality control system monitoring report. The CGCI states that the audit committee shall be responsible for determining the policy of internal audit and reporting, as well as monitoring the process of preparing financial and non-financial reports.

**89. The audit committee is accountable to the supervisory board.** An audit committee must submit information about the results of the audit conducted, the effect of the audit on the veracity of the financial statements, and the involvement of the audit committee in that process to the supervisory board<sup>85</sup> of a PIE.<sup>86</sup> A listed company must implement a policy of communication and information disclosure with shareholders and potential shareholders. Shareholders must be able to obtain information from the supervisory board and board of directors.<sup>87</sup> This is intended to ensure that shareholders have access to material information regarding the company.

## Filing/publication of financial statements

**90. Listed companies are required to publish annually a fully audited and IFRS compliant AFS and a management report.** The AFS information is required to be published as a part of its annual and semi-annual financial report on the SARAS REPORTAL

<sup>76</sup> Decree No180/04 of October 7, 2020, of the Governor of the NBG "On the approval of the rule regarding insider dealing, the unlawful disclosure of insider information and market manipulation", Article 7.1

<sup>77</sup> The Law of Georgia on Entrepreneurs, Article 57.1

<sup>78</sup> The Law of Georgia on Securities Market, Article 9.1

<sup>79</sup> The Law of Georgia on Entrepreneurs, Article 57.1

<sup>80</sup> The Law of Georgia on Entrepreneurs, Article 57.3

<sup>81</sup> Corporate Governance Code, Article 9.4

<sup>82</sup> The Law of Georgia on Securities Market, Article 91.1

<sup>83</sup> CGCI, Article 9.6

<sup>84</sup> The Law of Georgia on Entrepreneurs, Article 57.5(a) and (b)

<sup>85</sup> The Law of Georgia on Securities Market requires that an entity has a supervisory board

<sup>86</sup> The Law of Georgia on Entrepreneurs, Article 57.3

<sup>87</sup> CGCI, Article 22.4

system. Both annual and semi-annual reports must be IFRS compliant, however only the annual report must be audited. The AFS must be published by May 15 and the interim report by August 15 each year.<sup>88</sup> The management reports must be filed on the REPORTAL system.<sup>89</sup> The EU Transparency Directive specifies that an issuer shall make public its annual financial report (including the management report) at the latest four months after the end of each financial year and shall ensure that it remains publicly available for at least five years. Additionally, the issuer of shares or debt securities shall make public a half-yearly financial report covering the first six months of the financial year as soon as possible after the end of the relevant period, but at the latest two months thereafter. The issuer shall ensure that the half-yearly financial report (including an interim management report) remains available to the public for at least five years.

**91. Listed companies are required to disclose specified material information relating to financial reporting on an ongoing and non-selective basis.** Changes of the auditor as well as other material changes related to their activities must be publicly disclosed by the issuer through its website or the website of the GSE, or through other appropriate means without undue delay. These data, as a part of insider information, must be disclosed by the issuer in such a way that it is possible for the public to fully and correctly evaluate this information on a timely basis.<sup>90</sup>

**92. Information published on the REPORTAL system is available free of charge.** Listed entities are required to publish their AFS on their own website or in a print publication, however, there is no explicit requirement for the financial statements to be made widely available.<sup>91</sup>

## Monitoring and enforcement – financial reporting

**93. The Capital Market Supervision Department – Corporate Finance Division (CFD) is responsible for reviewing the financial statements of listed**

**companies.** CFD has two full time staff with financial reporting expertise. CFD verifies that each listed company has submitted the required financial and management reports, and that those reports include information relating to the auditor, the notes to the financial statement, a statement of compliance with IFRS, and the statements and signature(s) of responsible persons.

**94. CFD relies on SARAS for the review of compliance with IFRS. SARAS reviews the contents of listed companies' AFSs and refers cases of non-compliance to CFD for further sanctioning and enforcement purposes.** SARAS has a formal process for reviewing financial statement compliance with IFRS. This is a relatively new process and is still being developed. SARAS selects financial statements for review using a risk-based methodology. SARAS publishes a report of its findings from the review of financial statements.<sup>92</sup> The capacity and ability of SARAS to perform the reviews of compliance with IFRS is discussed elsewhere in this report but appears to be significantly under-resourced. SARAS has challenges recruiting and retaining staff for the IFRS review process because of structural difficulties in paying market related remuneration.

**95. CFD relies on SARAS to perform oversight on auditors of listed entities.** Accredited firms providing audit services and auditors are obliged to cooperate with SARAS in having the firms' audit quality control system inspected. The capacity and ability of SARAS to perform these reviews is discussed elsewhere in this report, but in general appears good. SARAS communicates with NBG on the outcome of the engagement quality control review. Applications to be accredited as auditors of PIEs include mainly quantitative criteria (years of experience, professional body membership, audit license).

**96. The enforcement of financial reporting requirements is clearly provided in the securities law and in regulations.** In response to violations of financial reporting requirements, NBG may:<sup>93</sup> (i) request that the violating person take necessary measures to ensure that their activities are in

<sup>88</sup> The Law of Georgia on Securities Market, Article 11.3(a)

<sup>89</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 7

<sup>90</sup> Decree No180/04 of October 7, 2020, of the Governor of the NBG "On the approval of the rule regarding Insider dealing, the unlawful disclosure of insider information and market manipulation", Article 7.1 and Annex 1, Point "D"

<sup>91</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 9(5)

<sup>92</sup> <https://saras.gov.ge/en/News/Detail/2614> "Non-compliances identified as a result of reviewing annual reports"

<sup>93</sup> The Law of Georgia on Securities Market, Article 55.2

compliance within the time limits set by NBG; (ii) suspend the sale of, or transactions in, securities; (iii) suspend the violating party from participating in the securities market for a certain period; and (iv) impose liability on the violating person under a legal act of NBG. A refusal to provide an explanation to NBG is regarded as a refusal by a witness to give evidence in administrative proceedings and providing incorrect information when giving an explanation to NBG is regarded as giving false evidence by a witness in administrative proceedings, for which the person may be held criminally liable.<sup>94</sup> The violation of the regulations of securities markets committed in aggravated circumstances may also give rise to criminal liability.<sup>95</sup>

**97. CFD may apply sanctions for the violation of reporting requirements, considering its seriousness and the potential risk,<sup>96</sup> including providing a written warning, and introducing special measures or a directive requiring a participant to stop violating and/or take measures to rectify the violations within a specified period.** NBG may also impose monetary fines or take specified action against individuals or corporates.<sup>97</sup> SARAS may refer any identified non-compliance with IFRS to the NBG for further action. However, because this is a relatively new process, no sanctions have yet been applied.

**98. No specific supervisory measures are triggered if a listed company receives anything other than an unmodified audit opinion.** However, the NBG may consider sanctions considering the seriousness and the potential risk of the violation.

**99. Law and regulations do not require CFD to hold regular meetings with auditors.** Auditors are not required to report on matters which they believe may be of material significance to the functions of the securities market regulator (e.g., breaches of securities or other laws). CFD does not have the power to

approve and/or dismiss auditors of listed companies and cannot require the production of any documents from the auditor.

## Corporate Governance

**100. The CGCI entered into force on January 1, 2022.<sup>98</sup>** It is based on a “comply or explain an alternative” approach. The submission of the Corporate Governance report to NBG is obligatory.<sup>99</sup> Companies are obliged to submit the first Corporate Governance report under the CGCI code in 2024, simultaneously with the publication of their 2023 financial statements. There are no explicit requirements with respect to financial reporting practices in the CGCI. The CGCI significantly supplements and enhances existing corporate governance reporting requirements included in the accounting and security market laws but does not replace them.

## Performance Indicators – Financial reporting and Auditing of Listed Companies

**101. The overall rating attributed to Georgia under the performance indicator “Financial Reporting and Auditing of Listed Companies” is 3.1 out of 4, which equals the simple mean of the rating criteria comprising sub-indicators A and B below (3.1=(3.3+2.8)/2).**

*Sub-indicator A. Financial reporting and auditing requirements for listed companies.*

**102. The attributed rating is 3.3, which equals the simple mean of the rating criteria comprising sub-indicators A.1-A.3 below (i.e., 3.3 = (4+3+3)/3).**

<sup>94</sup> The Law of Georgia on Securities Market, Article 55.21

<sup>95</sup> Pursuant to Paragraph 3, Article 55 of The Law of Georgia on Securities Market

<sup>96</sup> The Law of Georgia on Securities Market, Article 551

<sup>97</sup> Examples of sanctions imposed include fines and warnings for violation of reporting requirements (2021: 7 fines, 2 warnings) and warnings and directives in regard interim reports (2021: 20 warnings or directives).

<sup>98</sup> Decree N172/04 of December 7, 2021 of the President of the NBG “On approval of Corporate Governance Code for the Issuers of Public Securities”

<sup>99</sup> Decree N172/04 of December 7, 2021 of the President of the NBG “On approval of Corporate Governance Code for the Issuers of Public Securities”, Article 2.9

### A.1. Financial reporting requirements for listed companies

<b>Georgia Rating</b>	<b>4</b>	Listed companies are required to prepare IFRS compliant legal entity consolidated AFS. Listed companies are also required to prepare interim (semi-annual) financial statements. Listed companies are required to prepare management reports.
<b>Rating Criteria</b>	1	Criteria for "2" rating not met.
	2	Listed companies are required to prepare legal entity financial statements on an annual basis, in accordance with prescribed financial reporting standards.
	3	In addition to requirements under "2": Listed companies are required to prepare a management report (or management discussion and analysis – MD&A). Listed companies are required to apply IFRS for consolidated AFS.
	4	In addition to requirements under "3": Listed companies are required to prepare interim consolidated financial statements and to publish a statement on corporate governance.

### A.2. Audit requirements for listed companies

<b>Georgia Rating</b>	<b>3</b>	The AFS is required to be audited, and auditors must separately attest to accompanying material including management report. The Accounting Law requires PIEs (the PIE definition in the law includes listed companies) to have audit committees. The Securities Market Law read with the CGCI specifies that the audit committee must consist of members of the supervisory board, and the chair of the audit committee must be an independent director. The Law also specifies that the members of the audit committee should have appropriate experience in finance and accounting. The audit committee should be composed of board members who are not members of the executive body of the company or its controlled organizations. The majority of the audit committee members should be independent directors. Interim consolidated financial statements of listed companies are not required to be reviewed by auditors.
<b>Rating Criteria</b>	1	Criteria for "2" rating not met.
	2	The legal entity and consolidated financial statements of listed companies are subject to annual statutory audits. Shareholders (at the AGM) or board of directors (i.e., a governance body independent of management) are legally responsible for the appointment and dismissal of auditors of listed companies.
	3	In addition to requirements under "2": The auditor's report is required to attest whether the management report (MD&A) and other financial information have been read for consistency with financial statements. Listed companies are required to form an audit committee. At least one member of the audit committee is required to be an independent director. At least one member is required to have recent and relevant financial or auditing experience.
	4	In addition to requirements under "3": Interim consolidated financial statements of listed companies are required to be reviewed by auditors. The audit committee comprises only independent directors. At least one member is required to have recent and relevant financial reporting or auditing experience. Auditors of listed companies are required to be appointed by shareholders at the AGM (if applicable) or by the board of directors on the recommendation of the audit committee.

### A.3. Timeliness and public disclosure of financial reports for listed companies

Georgia Rating	3	<p>Interested parties, regardless of purpose, have access to published AFSs, management reports, and audit reports through the REPORTAL Depository. The AFSs are published before May 15 of the year following the reporting year.</p> <p>Companies are required to publish AFSs on their own website, or in a print publication. However, there are no requirements to disclose information on the activities of regulated securities market entities using mass media.</p> <p>There is no requirement for the AFS and the management report to be published simultaneously other than on REPORTAL.</p>
	Rating Criteria	1
2		<p>Listed companies are required to make legal entity and consolidated financial statements publicly available, although this may be in an abridged or incomplete form.</p> <p>Legal requirements are such that access to financial statements is limited or costly.</p> <p>The deadline for publication of annual reports of listed companies is no later than 9 months after reporting date.</p>
3		<p>In addition to requirements under "2":</p> <p>The audit opinion is also made publicly available.</p> <p>Legal requirements are such that financial statements are disseminated broadly, but there are limitations such as cost and ease of searchability.</p> <p>The deadline for publication of annual reports of listed companies is no later than 6 months after reporting date.</p>
4		<p>Listed companies are required to make the full sets of legal entity and consolidated financial statements publicly available. The audit report is also made publicly available.</p> <p>Listed companies are also required to publicly disclose the interim financial statements, with accompanying management discussion and analysis.</p> <p>Legal requirements are such that financial statements are readily searchable and accessible, at low or no cost.</p> <p>The deadline for publication of annual reports of listed companies is no later than 4 months after reporting date.</p>

Sub-indicator B. Monitoring and enforcement of the financial reporting requirements of listed companies.

103. The attributed rating is 2.8, which equals the simple mean of the rating criteria comprising sub-indicators B.1-B.4 below (i.e.,  $2.8 = (3+3+2+3)/4$ ).

B.1. Review of the listed company's annual financial statements		
Georgia Rating	<p>3</p> <p>The minimum procedures set by CFD include review of whether all components of the required submission have been published.</p> <p>CFD outsources the review of compliance with financial reporting standards to SARAS. The volume of financial information submitted by all companies to SARAS is significant, and SARAS has only limited resources to deal with it, which currently restricts the extent of monitoring and enforcement activities. Considering the procedures implemented by SARAS are in place, the requirements for this rating are considered to be met with minor limitations.</p>	
Rating Criteria	1	Criteria for "2" rating not met.
	2	Review of the AFS by the securities market regulator has <b>significant limitations</b> .
	3	Review of the AFS by the securities market regulator has <b>minor limitations</b> .
	4	Review of the AFS by the securities market regulator is <b>fully adequate</b> .

B.2. Communication with external auditors of listed companies		
Georgia Rating	<p>3</p> <p>CFD is not empowered to require, and does not have, regular meetings with external auditors of listed companies. Auditors are not required to inform the regulator ex-ante if they do not intend to issue a 'clean' (i.e., unmodified) audit opinion. CFD does not have the power to require production of any documents from the auditor.</p> <p>However, auditors are included in communication between SARAS and the issuer in regard non-compliance with IFRS.</p> <p>Auditors are also regulated by SARAS, which has a regular and robust inspection routine. Auditors may only be appointed by a listed company if they are on a SARAS approved list. Considering the auditor communication, oversight and approval processes of SARAS are in place, the requirements for this rating are considered to be met with minor limitations.</p>	
Rating Criteria	1	Criteria for "2" rating not met.
	2	Communication between the securities market regulator and external auditors of listed companies has <b>significant limitations</b> .
	3	Communication between the securities market regulator and external auditors of listed companies has <b>minor limitations</b> .
	4	Communication between the securities market regulator and external auditors of listed companies is <b>fully adequate</b> .

B.3. Reporting on the review of financial reporting of listed companies		
Georgia Rating	2	NBG prepares an annual report on its activities, published on its website. The report provides a summary of recent supervision activities. The quality of financial reporting and auditing of listed companies' sector is not distinctly reported in the annual report, although IFRS relevant topics are included. SARAS does perform a limited review of compliance with IFRS in listed companies (complementary function). SARAS annually publishes IFRS deficiencies detected through its reviews on an anonymized basis.
	Rating Criteria	<p>1 Criteria for "2" rating not met.</p> <p>2 Reporting by the securities market regulator on review of the financial statements of listed companies has <b>significant limitations</b>.</p> <p>3 Reporting by the securities market regulator on review of the financial statements of listed companies has <b>minor limitations</b>.</p> <p>4 Reporting by the securities market regulator on review of the financial statements of listed companies is <b>fully adequate</b>.</p>

B.4. Supervisory measures and sanctions for listed companies		
Georgia Rating	3	The legislation provides sufficient and robust measures and sanctions for listed companies' non-compliance with the requirements of accounting, financial reporting, and auditing, including compliance with IFRS. However, the compliance supervision is not yet fully monitored and enforced due to the limited SARAS capacity and the relative newness of the process.

B.4. Supervisory measures and sanctions for listed companies		
Rating Criteria	1	Criteria for "2" rating not met.
	2	Supervisory measures and sanctions that can be imposed by the securities market regulator have <b>significant limitations</b> .
	3	Supervisory measures and sanctions that can be imposed by the securities market regulator have <b>minor limitations</b> .
	4	Supervisory measures and sanctions that can be imposed by the securities market regulator are <b>fully adequate</b> .

### 3. Banking Sector

#### Overview of the banking sector<sup>100</sup>

104. Georgia's banking system is growing both in scope and scale.<sup>101</sup> Total assets were GEL70.3 billion<sup>102</sup> (US\$ 26.0 billion) on 31 December 2022, compared to GEL 60.6 billion (US\$ 19.6 billion)<sup>103</sup> on December 31, 2021,<sup>104</sup> an increase of 16.0 percent. The total assets of banks in Georgia comprise a significant element of foreign currency denominated instruments, with the foreign currency component being GEL 33.4 billion in 2022, 47.5 percent of total assets (2021: 49.5 percent of total assets). Total assets were significantly above the level of GEL 47.2 billion achieved in 2019 immediately before the start of the pandemic. Total loans of the banking sector, excluding interbank loans, increased from GEL 43.1 billion in 2021 to GEL 45.2 billion in 2022, an increase of 4.9 percent. Like total assets, total lending was significantly exposed to foreign currency. In 2022, outstanding local currency loans were GEL 24.6 billion (GEL 21.2 billion in 2021) and foreign currency loans were US\$ 7.5 billion (GEL 20.2 billion), up from US\$ 7.1 billion in 2021 (GEL 22.0 billion).

<sup>100</sup> For the purposes of this report, the banking sector section incorporates only the commercial banks.

<sup>101</sup> NBG Financial Sector Review, January 2023.

<sup>102</sup> *Assets and liabilities of Commercial Banks*, <https://nbg.gov.ge/en/statistics/statistics-data>

<sup>103</sup> Based on the exchange rate as at 31 December 2021 and 31 December 2022, NBG Financial Sector Review, September 2022.

<sup>104</sup> For the remainder of this section references to 2022, 2021, 2020, and 2019 mean at December 31 of that year unless otherwise specified.

**Table 4.** Breakdown of deposits by sector

Liability structure	December 2022 (% share)	December 2021 (% share)
Deposits from banks	2.9	1.5
Current and demand deposits	45.7	41.1
Term deposits	26.7	29.4
Accrued interest and dividends	0.5	0,5
Borrowed funds	19.6	20.7
Other liabilities	4.6	6.8
<b>Total</b>	<b>100</b>	<b>100</b>

Source: NBG - Assets and Liabilities of Commercial Banks, December 2022

**105. Bank deposits are keeping growing at a faster than the growth of assets.**<sup>105</sup> Total deposits in the banking sector, excluding interbank deposits, increased from GEL 37.2 billion in 2021 to GEL 44.3 billion in 2022, an increase of 19.1 percent. Like lending, the deposits of banks rose considerably above their pre-pandemic level of GEL 26.2 billion in 2019. In excess of 50 percent of deposits were in foreign currencies. Total liabilities of the sector increased from GEL 52.8 billion to GEL 61.1 billion in 2022. GEL 33.3 billion of total liabilities were in foreign currencies in 2022 (2021: GEL 31.3 billion). The Georgian currency strengthened against the US\$ from 3.10 in 2021 to 2.70 in 2022, understating the extent of growth when measured in GEL.

**106. The banking sector remains small in overall terms.** Total credit advanced relative to GDP was 73.1 percent as of December 2022, compared to 76.7 percent in 2021, 82.6 percent in 2020 and 69.4 percent in 2019. In 2022, Georgia's banking system consisted of 14 commercial banks, 13 of which were foreign controlled. Three Georgian banks were listed on the GSE, two of which had parent entities listed on the London Stock Exchange.

**107. The quality of the sector has remained sound.** Applying regulatory standards, 4.1 percent of loans were categorized as non-performing (substandard, doubtful, or loss) in 2022 (2021: 5.2 percent). The provision raised against gross nonperforming loans (coverage) was 42 percent in 2022 (2021: 42.0 percent).

**Table 5.** Lending growth by sector

Sector	December 2022		December 2021	
	Billion GEL	% share	Billion GEL	% share
Industry	3,964	8.8	5,034	11.7
Agriculture	1,004	2.2	932	2.2
Trade	4,383	9.7	4,004	9.3
Construction	3,648	8.1	3,049	7.1
Services	7,563	16.7	7,624	17.7



Sector	December 2022		December 2021	
	Billion GEL	% share	Billion GEL	% share
Mortgage	14,717	32.5	13,771	31.9
Consumer	7,683	17.0	6,224	14.4
<b>Total</b>		<b>100.0</b>		<b>100.0</b>

Source: NBG - Loans to the National Economy, December 2022

**108. The banking sector's average primary capital adequacy at the end of 2022 was 17.1 percent (2021: 15.6 percent).**<sup>106</sup> This compares to the statutory minimum average requirement of 13.2 percent (2021: 13 percent). The average total regulatory capital ratio was 20.2 percent (2021: 19.6 percent) compared to an average required ratio of 16.8 percent (2021: 17.5 percent). The NBG Financial Sector Review concludes that this level of capital adequacy is adequate considering the Basel III capital adequacy framework.<sup>107</sup> From 1 January 2023, commercial banks must adhere to the requirements applying IFRS-based numbers and approaches. The restated average total capital ratio applying IFRS for December 2022 was 21.6 percent against a required capital ratio of 19.2 percent.

## Banking regulator

**109. The structure of the NBG is provided by law.**<sup>108</sup> It was established 1991 as the National Bank of the Republic of Georgia.<sup>109</sup> The independence of NBG is guaranteed by the Constitution<sup>110</sup> and by law. Its duties and responsibilities are mandated by law.<sup>111</sup> The primary task of the NBG is to ensure price stability.

In addition, the NBG should ensure the stability and transparency of the financial system and promote sustainable growth of the national economy.

**110. The governance structure of the NBG is established by law.**<sup>112</sup> The governing body of the NBG is its nine-member supervisory board. The members can be Georgian nationals or foreign citizens with a reputation of integrity and who are recognized as professionals in economics, finance, or any other relevant field (maximum of two). The chair of the board is the NBG Governor. In addition to the chair, the board has three vice governors. Members are elected for seven-year terms upon nomination by the President of Georgia and following a majority vote in parliament. The Governor is appointed by the President of Georgia following nomination by the board. The vice-presidents are appointed and dismissed by the board following nomination by the Governor.

**111. The Bank Supervisory Department (BSD) of the NBG is the sole regulator of the banking sector in Georgia.**<sup>113</sup> As the regulating authority, BSD has the authority to license, delicense, regulate, and supervise banks. The Georgian economy and banking sector are significantly dollarized, although the NBG has issued

<sup>106</sup> NBG Annual report 2022

<sup>107</sup> NBG Financial Sector review, September 2022

<sup>108</sup> Organic Law of Georgia on NBG, 2009

<sup>109</sup> Established by decision of the Supreme Council of Georgia after the collapse of the Soviet Union

<sup>110</sup> Paragraph 3, Article 68.

<sup>111</sup> The Organic Law of Georgia on the NBG (2009) replaced the Law of Georgia on the National Bank of Georgia (1995).

<sup>112</sup> The Organic Law of Georgia on the NBG. Chapter II.

<sup>113</sup> Legal provisions with reference to supervisory powers of the NBG are provided by the Constitution (Article 68), the Organic Law of Georgia on the NBG (Chapter VIII), as well as by the Law on Commercial Banks and other relevant legal acts/by-laws (which can also be found on the website of the NBG). Also, by the Organic Law, the NBG has been empowered with a mandate to execute supervision of banking groups (so-called consolidated supervision). The power of NBG to set and enforce minimum prudential standards for banks and banking groups are stated in the Organic Law of Georgia on the NBG and in the Law on Commercial Banks (Article 21).

several policies in an effort to wean the economy off the US dollar and reinstate the lari as the dominant currency.

**112. BSD supervises and regulates commercial banks in accordance with risk-based principles.** Applying a risk-based supervisory approach, BSD identifies and mitigates potential risks that may impede the functioning of the financial system. This requires timely identification of risks to the banking sector or individual banks and mitigating those risks. Applying this approach means focusing on the risks that pose the greatest danger to the financial sector stability. An assessment of bank risks and their potential impact drives the design of supervisory action including the allocation of resources.

**113. The BSD has wide supervisory powers.** The BSD's responsibility for commercial banks includes the issuance and revocation of licenses, inspection and regulation, the issuance of written instructions, and the imposition of additional requirements, restrictions, supervisory measures, and sanctions. Supervisors undertake both on-site and off-site work, perform all necessary steps and activities to identify and assess risks of the banks, and elaborate relevant supervisory actions. However, the BSD has limited responsibilities for supervising financial reporting of banks (see paragraph 135 and 136 below).

**114. The BSD also has wide enforcement authority.** The Law on Commercial Banks defines sanctions with varying levels of severity, depending on the significance of violations and any actual or potential risks the violations pose to the assets of the bank. The law provides a list of actions that BSD should undertake when violations are identified. NBG regulations define the amounts of monetary penalties that can be imposed on commercial banks and their administrators for violations.<sup>114</sup>

**115. NBG prepares an annual report on its activities that is published on its website.** The report is in both Georgian and English.<sup>115</sup> The report discusses the outlook, targets, monetary policies, recent

developments, and achievements as well as a brief summary of recent supervision activities. The main reported findings focus on capital adequacy and prudential reporting, internal controls, governance, and lending. The report highlights the role NBG and BSD play in promoting application of quality financial reporting including updates to reporting templates. Although the development of quality IFRS reporting is discussed in the report, the report does not deal with IFRS shortcomings or noncompliance.

### Financial reporting requirements for commercial banks

**116. Banks are required to comply with IFRS for general purpose financial statements.**<sup>116</sup> Banks are as defined PIEs (see paragraph 56 above). They have been required to report in accordance with IFRS since 2017.<sup>117</sup>

**117. The law requires the application of the full and current version of IFRS, as issued by the International Accounting Standards Board (IASB). Consolidated financial statements must be based on IFRS and if some parts do not comply with IFRS, this must be disclosed in the financial statements.** The financial statements of commercial banks were reviewed as part of the observed financial reporting practices and perceptions. The review concludes that most banks likely complied with IFRS, but that there were areas of non-compliance identified. For details see **Section C. Observed Financial Reporting Practices and Perceptions** of this report.

**118. Prudential reporting is currently based on previous national GAAP.** Considerable effort has been devoted to transitioning the prudential reporting to IFRS. Starting from January 2023, banks will be required to submit regulatory reports which are in compliance with IFRS. In accordance with the supervision strategy of BSD for 2020-2022, the approximation of supervisory reports to IFRS is one of the most important priorities.<sup>118</sup> BSD continues

<sup>114</sup> Order of the President of the NBG, №242/01, 2009 Regulation for Determining and Imposing Fines on Commercial Banks and their Administrators.

<sup>115</sup> <https://nbg.gov.ge/en/publications/annual-reports>

<sup>116</sup> IFRS Jurisdictional Profiles.

<sup>117</sup> Order of the President of the NBG Regarding the Rules of Mandatory Audit of Consolidated Financial Statements and Explanatory Notes to the Financial Statements of the Commercial Banks.

<sup>118</sup> NBG Annual Report 2020.

working on transitioning supervision from the national GAAP to IFRS. BSD has worked on transferring banks' regulatory reporting to the IFRS framework through EU standards (FINREP/COREP<sup>119</sup> forms). Banks are required to disclose significant differences between IFRS and prudential reporting in their annual public prudential (pillar 3 reports).

**119. Banks are required to submit annual audited financial statements to BSD and make them available to the public.** Banks are required to submit preliminary financial statements to BSD on March 1 in the year immediately following their December year-end.<sup>120</sup> They are required to publish their audited financial statements on their own website by May 15.<sup>121</sup> Banks, like other entities in Georgia, are required to submit audited financial statements to SARAS by no later than October 1.<sup>122</sup>

**120. Banks are required to publish management reports. The Law on Accounting, Reporting, and Audit requires that a management report be prepared and published each year.** The report should include a general business overview, a corporate governance statement, a risk management policy overview, the number of employees, and other relevant information. The management report requirement is not included in the specific financial reporting requirements for banks, and consequently is only subject to the timeline set by SARAS (October 1).

**121. Although banks are required to prepare regular prudential financial reports for the NBG, banks that are not listed on the debt or equity markets are not required to prepare or publish public IFRS compliant interim financial reports.** Preparation of IFRS compliant interim financial reports by all banks would be in line with the good practice.

## Statutory audit and other forms of independent assurance

**122. Banks and financial institutions are required to have their AFS audited.** An order of NBG,<sup>123</sup> as well as the Law on Accounting, Reporting, and Audit, establishes the requirement for the audit of bank financial statements. The AFS of banks are required to be audited by an authorized auditor of PIEs (see paragraph 60).

**123. SARAS is responsible for regulating the audit profession.** Auditing standards for banks and financial institutions are set by SARAS. The full and current ISA as issued by the IAASB are adopted in Georgia. Further, the Law on Accounting, Reporting, and Audit empowers SARAS to set additional reporting and other requirements.

**124. SARAS approves audit firms who are permitted to perform the audit of PIEs (including banks) based on both quantitative and qualitative criteria.** The process includes in-depth inspection of audit firms' processes on a regular basis. The BSD relies on the SARAS process to identify and regulate auditors who are permitted to perform audits of banks and does not have a process of its own. An auditor of a financial institution must have more than 15 years' audit experience and five years of experience in the audit of financial institutions.<sup>124</sup>

**125. A bank and its auditor are required to notify SARAS in the event of the termination of an audit appointment.**<sup>125</sup> The notification requirement includes a requirement for substantiation of the termination.

**126. Audit firms of banks and financial institutions in Georgia are rotated.**<sup>126</sup> Audit partners are required to be rotated every seven years. This provision is in line with the EU audit regulation. Audit firms are required

<sup>119</sup> Financial Reporting/Common Reporting.

<sup>120</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, article 3, paragraph 1(a).

<sup>121</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, article 3, paragraph 1(c).

<sup>122</sup> The Law of Georgia on Accounting, Reporting, and Audit.

<sup>123</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, Article 3, paragraph (e).

<sup>124</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, Article 3, paragraph 1(ba) and 1(bb).

<sup>125</sup> The Law of Georgia on Entrepreneurs, Article 58.

<sup>126</sup> The Law of Georgia on Accounting, Reporting, and Audit, and Order of the President of the NBG regarding the Rules of Mandatory Audit of Consolidated Financial Statements and Explanatory Notes to the Financial Statements of the Commercial Banks.

to be rotated every 10 years. The law also requires a mandatory cooling off period of four years. Banks are required to hold a tender for audit.

**127. Audit firms are not allowed to provide specially prescribed services to their bank audit client.<sup>127</sup>**

A bank's auditor cannot provide services related to tax declarations and general tax consultation, legal services, represent the bank in negotiations, perform the internal audit function, or perform personnel search functions, among other listed functions. This provision is in line with the EU audit regulation. An auditor does not have the right to provide audit services to an entity if there is danger of conflict of interests or threats caused by financial, personal, business, labor, and/or other current or future relations.

**128. The law provides that shareholders appoint auditors.<sup>128</sup>** The audit committee is required to have a tender process for the appointment of an auditor. The committee recommends an auditor to the shareholders or the supervisory board. A shareholder vote on appointment of the external auditor is required to be held as the final step.

**129. The BSD does not unconditionally have the power to reject the appointment or terminate the appointment of an auditor.<sup>129</sup>** If the BSD determines that an audit was not performed according to ISA or has questions as to the independence and competence of the auditor, the BSD can require that the appointment of an auditor be terminated. The resignation or termination of the auditor must be reported to the BSD within 10 days.

## Audit committees

**130. The law and regulations require banks to have an audit committee.<sup>130</sup>** All banks, regardless of their size, complexity, and scope of activities, are required

to set up audit and risk management committees from among the members of the supervisory board. The chair of the audit committee must be independent and not be the chair of the supervisory board or any other committees.<sup>131</sup> The committee should comprise at least 3 members, the majority of which should be independent.<sup>132</sup> At least two members of an audit committee, including the chairperson, should have the ability to analyze financial statements, respective experience, or should have an education in finance.<sup>133</sup>

## Filing/publication of financial statements

**131. PIEs are required to file financial statements annually.** Banks, like other PIEs in Georgia, are required to submit audited financial statements to SARAS by no later than October 1 of each year for the preceding year. This requirement includes a full set of Georgian language, IFRS compliant financial statements and a management report. SARAS conducts certain validation checks on the information submitted and then the information is posted on REPORTAL.

**132. Banks are required by law and regulation to publish AFS.** In terms of these requirements, the audited financial statements of a bank, without accompanying management report, must be published by May 15 of each year.<sup>134</sup> These financial statements have to be published on the website of the bank and are also published on the website of the supervisor. There are no other requirements for dissemination of the financial statements.

## Monitoring and enforcement – financial reporting

**133. The Reporting Policy and Monitoring Division, a subdivision of the BSD is responsible for reviewing financial statements of banks and financial**

<sup>127</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 16.

<sup>128</sup> The Law of Georgia on Entrepreneurs, Article 57.7, CGCCB, Order 215/04.

<sup>129</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, Article 3, paragraph 1(b), 1(c) and 1(o).

<sup>130</sup> CGCCB, Order 215/04, the Law on Commercial Banks (Article 12 and Article 16) and the Law on Entrepreneurs (Article 57).

<sup>131</sup> CGCCB, Order 215/04, Article 7.1 and 7.6

<sup>132</sup> CGCCB, Order 215/04, Article 8.2

<sup>133</sup> CGCCB, Order 215/04, Article 8.3

<sup>134</sup> Order of the President of the NBG N284/04 on Regulation on Statutory Audits of Consolidated Financial Statements of Commercial Banks and the Disclosure of Information in the Notes to the Financial Statements, article 3, paragraph 1(e).

**institutions.** The dedicated unit has responsibility for reviewing the financial statements, specifically for confirming that IFRS financial reporting and disclosure requirements are followed. The Division also reviews auditor reports. The common year-end of banks in Georgia means that the timeline of the review is tight. The Division has four staff and focuses its initial activities on the key differences between accounting and prudential measures, and then on higher risk areas such as expected credit losses (measurement and disclosure). However, the objective is to fully review the financial statements before publication.

**134. SARAS has its own process for reviewing financial statement compliance with IFRS.** This is a relatively new process and is still being developed. SARAS selects financial statements for review based on a risk-based methodology. SARAS publishes a report of its findings from the review of financial statements.<sup>135</sup> The capacity and ability of SARAS to perform these reviews of compliance with IFRS is discussed elsewhere in this report. Given that bank financial statements are already subject to review by BSD, they are considered low-risk and are selected less frequently than would otherwise be the case. It appears from discussions that BSD places some reliance on the existence of the SARAS review process.

**135. Enforcement of financial reporting requirements is not clearly provided in BSD regulations.** The banking supervisor does not impose sanctions on non-compliant AFS although findings of non-compliance can raise questions on the competence of the auditor. This may in turn lead to the supervisor asking for a change of auditor. Auditors are not required to inform the banking supervisor if they intend to issue a qualified audit opinion. However, auditors are required to inform the BSD in the case of major events including an increase of risk to the going concern of the entity. The BSD does not take any supervisory measures if a bank receives anything other than an unmodified audit opinion. SARAS may refer identified non-compliance with IFRS to the NBG for further action. However, because this is a relatively new process, no sanctions have yet been applied.

**136. BSD relies on SARAS to perform oversight on auditors of banks and financial institutions.** Accredited firms providing audit services and auditors are obliged to cooperate with SARAS in having the firm's audit quality control system inspected. The details of the SARAS process are set out in **Section II. B.9. Audit regulation, quality assurance and public oversight** and the performance indicators in paragraph 314. The capacity and ability of SARAS to perform these reviews is discussed elsewhere in this report, but in general appears good. SARAS communicates with BSD on the outcome of the audit quality control review.

**137. Law and regulations have requirements for communication between the BSD and auditors.** External auditors are legally required to notify the NBG within 5 business days after identification of material adverse changes regarding the banks business or risks, among other matters. An internal BSD manual guides effective communication between auditors and the BSD.<sup>136</sup> In practice, meetings occur at least twice annually. The supervisor does not have the power to establish the scope of external audits but does require the production of the management letter and information regarding materiality.

## Corporate Governance

**138. All commercial banks and branches and subsidiaries of foreign banks operating in Georgia are required to comply with CGCCB.**<sup>137</sup> The CGCCB does not require or encourage further or different financial reporting practices in addition to those financial reporting requirements established by law or other regulations. In case of failure to fully comply with, or violation of, the Code, the bank may be exposed to administrative and corrective measures. The bank, its administrator, or the bank's holding company may be required to adjust the bank's corporate governance structure or may be subject to regulatory measures and/or sanctions (monetary fine) set by the Code or sanctions set under Article 30 of the Law on Commercial Banks.

<sup>135</sup> <https://saras.gov.ge/en/News/Detail/2614> "Non-compliances identified as a result of reviewing annual reports"

<sup>136</sup> Guidelines for Effective Communication between Audit Firms and the NBG.

<sup>137</sup> Order of the President of the NBG N215/04 on the Approval of the Corporate Governance Code for Commercial Banks.

## Performance Indicators – Financial Reporting and Auditing Requirements for Banks

139. The overall rating attributed to Georgia under the performance indicator “Financial Reporting and Auditing for Banks” is 3.1 out of 4, which equals the simple mean of the rating criteria comprising sub-indicators A and B below ( $3.2=(3+3.2)/2$ ).

*Sub-Indicator A. Financial reporting and auditing requirements for banks.*

140. The attributed rating is 3, which equals the simple mean of the rating criteria comprising sub-indicators A.1-A.3 below (i.e.  $3 = (3+3+3)/3$ ).

A.1. Financial reporting requirements for banks	
Georgia Rating	3 Banks prepare IFRS compliant AFS for both the legal and consolidated entity along with a separate management report. Banks in Georgia that are not listed on the debt or equity markets are not required to prepare or publish IFRS compliant interim financial statements
Rating Criteria	1 Criteria for “2” rating not met.
	2 Banks are required to prepare legal entity financial statements on an annual basis, in accordance with prescribed financial reporting standards.
	3 In addition to requirements under “2”: Banks are required to prepare a management report (or MD&A). Banks are required to apply IFRS for consolidated AFS.
	4 In addition to requirements under “3”: Banks are required to prepare interim consolidated IFRS compliant financial statements.

A.2. Audit requirements for banks	
Georgia Rating	3 The annual financial report is audited, and auditors attest to accompanying material, including the management report. Banks are required to form an audit committee of a minimum of three members, a majority of which must be independent. Refer to A.1. above, there is no requirement for unlisted banks to submit interim IFRS compliant financial statements and therefore there is no audit review.
Rating Criteria	1 Criteria for “2” rating not met.
	2 The legal entity and consolidated financial statements of banks are subject to annual statutory audits. Shareholders (at the AGM) or board of directors (i.e. a governance body independent of management) is legally responsible for the appointment and dismissal of auditors of banks.
	3 In addition to requirements under “2”: The auditor’s report is required to attest whether the management report (MD&A) and other financial information have been read for consistency with the financial statements. Banks are required to form an audit committee. At least one member of the audit committee is required to be an independent director. At least one member is required to have recent and relevant financial or auditing experience.
	4 In addition to requirements under “3”: Interim consolidated financial statements of banks are required to be reviewed by auditors. The audit committee comprises only independent directors. At least one member is required to have recent and relevant financial reporting or auditing experience. Auditors of banks are required to be appointed by shareholders at the AGM (if applicable) or by the board of directors on the recommendation of the audit committee.

### A.3. Timeliness and public disclosure of financial reports for banks

Georgia Rating	<b>3</b>	<p>All banks must publish their AFS, audited by an independent auditor by May 15 of the subsequent year (within four and a half months). The complete financial statements including audit report must be published on their website.</p> <p>The management report must be published with a separate audit report on the SARAS website by October 1.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	<p>Banks are required to make legal entity and consolidated financial statements publicly available, although this may be in an abridged or incomplete form.</p> <p>Legal requirements are such that access to financial statements is limited or costly.</p> <p>The deadline for publication of annual reports of banks is no later than nine months after the reporting date.</p>
	3	<p>In addition to requirements under "2":</p> <p>The audit opinion is made publicly available.</p> <p>Legal requirements are such that financial statements are disseminated broadly, but there are limitations such as cost and ease of searchability.</p> <p>The deadline for publication of annual reports of banks is no later than six months after the reporting date.</p>
	4	<p>Banks are required to make the full sets of legal entity and consolidated financial statements publicly available. The audit report is also made publicly available.</p> <p>Banks are required to publicly disclose the interim financial statements, with accompanying management discussion and analysis.</p> <p>Legal requirements are such that financial statements are readily searchable and accessible, at low or no cost.</p> <p>The deadline for publication of annual reports of banks is no later than four months after the reporting date.</p>

*Sub-Indicator B. Monitoring and enforcement of the financial reporting requirements of banks.*

**141. The attributed rating is 3.2, which equals the simple mean of the rating criteria comprising sub-indicators B.1-B.5 below (i.e.  $3.2 = (3+4+4+2+3)/5$ ).**

### B.1. Review of bank annual financial statements

Georgia Rating	<b>3</b>	<p>BSD is responsible for reviewing financial statements of banks and financial institutions. The review focuses on report adequacy, audit report, content of financial statements, and key findings of management letters. BSD also performs a limited review of financial statements for compliance with bank specific IFRSs. Enforcement of financial reporting requirements is not clearly provided in the regulations.</p> <p>SARAS also reviews bank financial statements for compliance with IFRS, although the risk is down weighted to reflect the review that has already occurred at BSD. SARAS communicates relevant findings to BSD.</p> <p>The volume of financial information submitted by all companies to SARAS is significant, and SARAS has only limited resources to deal with it, which currently restricts the extent of monitoring and enforcement activities.</p>
----------------	----------	---

### B.1. Review of bank annual financial statements

Rating Criteria	1	Criteria for "2" rating not met.
	2	Review of the AFS by the banking supervisor has <b>significant limitations</b> .
	3	Review of the AFS by the banking supervisor has <b>minor limitations</b> .
	4	Review of the AFS by the banking supervisor is <b>fully adequate</b> .

### B.2. Reconciliation requirements between equity and regulatory capital of banks

Georgia Rating	4	<p>Reconciliation requirements are fully adequate. Banks are required to prepare financial statements in accordance with IFRS. Banks are required to compile and publish a Basel Pillar III report which includes a reconciliation.</p> <p>The IFRS AFS and the Pillar III report are audited, publicly disclosed, and reviewed by NBG.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	Reconciliation requirements between equity and regulatory capital have <b>significant limitations</b> .
	3	Reconciliation requirements between equity and regulatory capital have <b>minor limitations</b> .
	4	Reconciliation requirements between equity and regulatory capital are <b>fully adequate</b> .

### B.3. Communication with external auditors about banks

Georgia Rating	4	<p>Law and regulations do not require NBG to hold regular meetings with auditors; however, an internal guidance manual does provide for bilateral meetings between NBG and auditors. Currently meetings typically take place twice a year.</p> <p>Audit firms are required to communicate to NBG if they intend to qualify the financial statements, and the NBG has access to the management report.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	Communication between the banking supervisor and external auditors of banks have <b>significant limitations</b> .
	3	Communication between the banking supervisor and external auditors of banks have <b>minor limitations</b> .
	4	Communication between the banking supervisor and external auditors of banks is <b>fully adequate</b> .



#### B.4. Reporting on the review of financial reporting of banks

Georgia Rating	<b>2</b>	<p>NBG prepares an annual report on its activities, published on its website. The report provides a summary of recent supervision activities. The quality of financial reporting and auditing of banking and financial sector is not distinctly reported in the annual report, although IFRS relevant topics are included.</p> <p>SARAS does perform a limited review of compliance with IFRS in banks (complementary function). SARAS annually publishes IFRS deficiencies detected through its reviews on an anonymized basis.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	Reporting by the banking supervisor on review of financial statements of banks have <b>significant limitations.</b>
	3	Reporting by the banking supervisor on review of financial statements of banks have <b>minor limitations.</b>
	4	Reporting by the banking supervisor on review of financial statements of banks is <b>fully adequate.</b>

#### B.5. Supervisory measures and sanctions for banks

Georgia Rating	<b>3</b>	<p>Supervisory measures or sanctions can be imposed by the bank supervisor for various elements of financial reporting. The supervisor can apply various measures (administrative, civil, criminal) on companies and/or directors for financial reporting.</p> <p>The measures/sanctions are sound with reasonable assurance that no material risks are left unaddressed.</p> <p>BSD in co-operation with SARAS does focus on compliance with IFRS, however the sanctions are not fully enforced due to limited resources and the newness of the process.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	Supervisory measures and sanctions that can be imposed by the banking supervisor have <b>significant limitations.</b>
	3	Supervisory measures and sanctions that can be imposed by the banking supervisor have <b>minor limitations.</b>
	4	Supervisory measures and sanctions that can be imposed by the banking supervisor are <b>fully adequate.</b>

## 4. Microfinance Sector

### Overview of the microfinance MFI sector

**142. Non-banking financial institutions (NBFIs) are defined by NBG.**<sup>138</sup> The definition includes microfinance institutions (MFIs), loan issuing entities (LIEs), currency exchange units, and credit unions. The NBFIs together constituted a 3.3 percent share of the overall financial sector assets as at December 31, 2022 (2021:3.4 percent).<sup>139</sup> In total, the sector is comprised of 36 MFIs, 176 LIEs, 511 currency exchange units, and one credit union. Within the sector, MFIs represent 75.8 percent of total loans. LIEs represent 24.0 percent of total loans. The sole credit union has loans of less than 0.1 percent of total loans and is not considered further.

**143. The focus of this section of the report is on MFIs.** There is a clear distinction in legal requirements that exist for MFIs and LIEs (the two dominant micro lending organizations). The former has been regulated under law since 2008,<sup>140</sup> with regulations issued to govern their prudential requirements, supervision, asset management, and financial statements. The latter has only been subject to regulation since 2018 and is poorly described with limited or no regulatory framework.<sup>141</sup> Both types of entity make loans to the general public, and both base their activities in large part on pawn or Lombard style loans.

**144. The distinction between LIEs and MFIs predominantly relates to their legal rights in raising funding.** Both are predominantly funded from professional and related party sources. However, legally, MFIs are entitled to raise loan funding from resident and non-resident legal and natural persons.<sup>142</sup> Commencing in 2013/4, NBG worked with MFIs to reduce their reliance on retail funding in the form of

loans or promissory notes.<sup>143</sup> As a consequence, funds attracted from private individuals decreased from 36.5 percent (5 447 individuals) in 2014 to 7.2 percent (437 individuals) in 2022. However, the enabling legislation for raising loans remains in place.

**145. The ROSC indicators used for microfinance entities are similar to those applied to banks.** As such, the indicators are established relative to the good practice for PIEs that have public accountability in large part because of their ability to attract funding from the general public. The intent of this good practice is to protect unsophisticated depositors and lenders to the industry by establishing appropriate levels of transparency and regulatory oversight. As set out in paragraph 144 above, although MFIs remain legally entitled to raise such funding, regulatory intervention has all but eliminated this practice. Consequently, the ROSC indicators are not considered appropriate to the industry in Georgia as currently operating. With consideration of the above the financial reporting requirements for microfinance enterprises should be reevaluated for proportionality considering existing and potential sources of funding.

**146. MFIs have grown through the pandemic period.**<sup>144</sup> Total loans were GEL 1.62 billion (US\$ 599.6 million)<sup>145</sup> as at 2022,<sup>146</sup> compared to GEL 1.36 billion (US\$ 439.0 million)<sup>147</sup> in 2021, an increase of 19.1 percent. The total lending of MFIs include a smaller element of foreign currency denominated instruments relative to the banking sector, with the foreign currency component of 2 percent in 2022 (2021: 4 percent).

**147. MFIs are predominantly funded by borrowing and retained capital.**<sup>148</sup> As a consequence of a change in requirements in 2018, there are no depositors in this sector.<sup>149</sup> Total borrowed funds, excluding subordinated loans, was GEL 1 011 million in 2022 (2021:

<sup>138</sup> NBG Annual report 2022

<sup>139</sup> NBG Annual Report 2022

<sup>140</sup> The Law of Georgia on Microfinance Organizations

<sup>141</sup> Order 217/045 of the President of the NBG on Loan Issuing Entities (2018)

<sup>142</sup> The Law of Georgia on Microfinance Organizations, article 4.1(f)

<sup>143</sup> NBG Annual report 2013, page 93

<sup>144</sup> NBG, consolidated data of microfinance organizations, December 2021, 2020, and 2019.

<sup>145</sup> Based on the exchange rate as at December 31, 2021, NBG Financial Sector Review, September 2022

<sup>146</sup> For the remainder of this section references to 2021, 2020, and 2019 mean at December 31 of that year unless otherwise specified.

<sup>147</sup> Based on the exchange rate as at December 31, 2020, NBG Financial Sector Review, September 2022

<sup>148</sup> NBG, consolidated data of microfinance organizations, December 2022, 2021, 2020, and 2019

<sup>149</sup> NBG Annual Report 2021 and 2022

GEL 901 million), an increase of 12.2 percent. GEL 369 million of the borrowing was from non-residential investors (2021: 393 million) a decrease caused in part by the Russia's invasion in Ukraine. Total funds borrowed from financial institutions were GEL 817 million in 2022 (2021: GEL 685 million), an increase of 19.3 percent. Funds borrowed from individuals amounted to GEL 173 million in 2022 (2021: GEL 190 million). Total capital including subordinated debt increased from GEL 607 million in 2021 to GEL 707 million in 2022, an increase of 16.5 percent.

**148. The MFI credit exposure is dominated by retail loans, in particular pawn shop loans.**<sup>150</sup> In 2022, 80 percent of loans were retail in nature (2021: 78 percent). The remaining 20 percent was advanced to legal entities or was related to trade and service or agricultural activities of individuals. In 2022, 48.6 percent of total loans were pawn shop loans (2021: 48.4 percent).

**149. The quality of the loan portfolio has improved.** The proportion of overdue loans has fallen from 8.0 percent in 2021 to 7.4 percent in 2022, and the non-performing loans from 5.9 percent to 5.5 percent. The provisions held against the total portfolio have also decreased year on year, from 6 percent to 5 percent.

**150. The quality of the sector has remained sound.**<sup>151</sup> The sector received significant support from the NBG in the form of a US\$ 200 million liquidity swap. This support was advanced in 2020 and continued through 2021 and is considered to have positively contributed to the sector's stability.

## Regulator

**151. The sector is regulated by the NBG.** The structure of the NBG and its governance are discussed in paragraph 109 to 110 above in **Section II. B.3. Banking sector.**

**152. Although MFIs and LIEs are organizationally very similar, their reporting and regulatory requirements are very different.** For the purposes of the remainder of this section, the focus is on MFIs, regulated by the Non-Banking Institutions Supervision Department (NISD) of the NBG. However, it is considered that if MFIs continue not to source funding from the general public, then the financial reporting requirements imposed on MFIs are likely be disproportionate to the level of their public interest.

**153. The NISD of the NBG is the sole regulator of MFIs in Georgia.** As the regulating authority, NISD has the authority to license, delicense, regulate, and supervise MFIs.

**154. The authority of the NISD is created by regulation.**<sup>152</sup> The NISD responsibility for MFIs includes the issuance and revocation of licenses, inspection and regulation, the issuance of written instructions, and the imposition of additional requirements, restrictions, supervisory measures, and sanctions. All the requirements in law and regulation, including prudential, regulatory reporting, and financial reporting requirements are subject to sanction. Supervisors undertake off-site work and perform all necessary steps and activities to identify and assess risks of the entities and relevant supervisory actions.

**155. The NISD also has some enforcement authority.**<sup>153</sup> The enforcement authority as defined in the legislation and regulations for MFIs is non-specific, simply noting that in case of violation of requirements, the NISD has the right to use measures and sanctions against the offender, including sanctions for non-submission of financial statements to SARAS (based on SARAS information).

**156. NBG prepares an annual report on its activities that is published on its website.** The report is in both Georgian and English.<sup>154</sup> The report discusses the outlook, targets, monetary policies, recent developments, and achievements as well as a brief

<sup>150</sup> NBG, consolidated data of microfinance organizations, December 2022, 2021, 2020, and 2019

<sup>151</sup> NBG, consolidated data of microfinance organizations, December 2022, 2021, 2020, and 2019

<sup>152</sup> Order No. 143/04 of the President of the NBG on Approval of Regulation on Supervision and Regulation of Microfinance Organization Activities. Order No. 19/04 of the President of the NBG on the Approval of the Form of Financial Reports, the Date of Submission and Accounting Rules to be Submitted by Microfinance Organizations to the NBG.

<sup>153</sup> Order No. 143/04 of the President of the NBG on Approval of Regulation on Supervision and Regulation of Microfinance Organization Activities, Article 7.

<sup>154</sup> <https://nbg.gov.ge/en/publications/annual-reports> The 2020 report is available in both English and Georgian. At 12/10/22, the 2021 report was only available in Georgian.

summary of recent supervision activities, including those as applied to NBFIs. Although the development of quality IFRS reporting is discussed in the report, the report does not deal with reporting short-comings or non-compliance.

### Financial reporting requirements for MFIs

**157. MFIs have been required to comply with IFRS for general purpose financial statements since 2017.**<sup>155</sup> MFIs are defined as PIEs (see paragraph 56 above). An order of the NBG also reaffirms this requirement.<sup>156</sup> The financial statements of selected MFIs were reviewed as part of the observed financial reporting practices and perceptions, see **Section C. Observed Financial Reporting Practices and Perceptions** of this report. That section concludes that most MFIs likely did not comply with IFRS.

**158. Georgian law requires the application of the full and current version of IFRS, as issued by the IASB.**<sup>157</sup> Consolidated financial statements must be based on IFRS standards and if some parts do not comply with IFRS, it has to be disclosed.

**159. Prudential reporting is currently based on previous national GAAP.**

**160. MFIs are required to publish AFS on their website by June 15.**<sup>158</sup> MFIs, like other entities in Georgia, are required to submit audited legal entity financial statements to SARAS by no later than October 1.<sup>159</sup>

**161. MFIs are required to publish management reports.** The Law on Accounting, Reporting, and Audit requires that a management report be prepared and published each year. The report should include a general business overview, a corporate governance

statement, a risk management policy overview, the number of employees, and other relevant information. The management report requirement is not included in the specific financial reporting requirements for MFIs, and consequently is only subject to the timeline set by SARAS (October 1).

**162. Although MFIs are required to prepare regular prudential financial reports for the NISD, MFIs that are not listed on the debt or equity markets are not required to prepare or publish public IFRS compliant interim financial reports.**

### Statutory audit and other forms of independent assurance

**163. MFIs are required to have their AFS audited.** An order of NBG,<sup>160</sup> as well as the Law on Accounting, Reporting, and Audit, establish the requirement for the audit of MFI financial statements. The AFS of MFIs are required to be audited by an auditor authorized to audit PIEs (see paragraph 60).

**164. SARAS is responsible for regulating the audit profession.** It approves audit firms who are permitted to perform the audit of PIEs (including MFIs) based on both quantitative and qualitative criteria.

**165. An MFI and its auditor are required to notify SARAS in the event of the termination of an audit appointment.**<sup>161</sup> The notification requirement includes a requirement for substantiation of the termination.

**166. Audit firms of MFIs in Georgia are rotated.**<sup>162</sup> Audit partners are required to be rotated every seven years. Audit firms are required to be rotated every ten years. The law also established a mandatory cooling-off period of four years.

<sup>155</sup> IFRS Jurisdictional Profiles.

<sup>156</sup> Order No. 19/04 of the President of the NBG on the Approval of the Form of Financial Reports, the Date of Submission and Accounting Rules to be Submitted by Microfinance Organizations to the NBG, Article 3.

<sup>157</sup> The Law of Georgia on Accounting, Reporting, and Audit.

<sup>158</sup> Order No. 19/04 of the President of the NBG on the Approval of the Form of Financial Reports, the Date of Submission and Accounting Rules to be Submitted by Microfinance Organizations to the NBG. Article 3(d).

<sup>159</sup> The Law of Georgia on Accounting, Reporting, and Audit.

<sup>160</sup> Order No. 19/04 of the President of the NBG on the Approval of the Form of Financial Reports, the Date of Submission and Accounting Rules to be Submitted by Microfinance Organizations to the NBG. Article 3.

<sup>161</sup> The Law of Georgia on Entrepreneurs. Article 58.

<sup>162</sup> The Law of Georgia on Accounting, Reporting, and Audit.

**167. Audit firms are not allowed to provide specially prescribed services to their MFI audit client.**<sup>163</sup>

An MFI auditor cannot provide services related to tax declarations and general tax consultation, legal services, represent the bank in negotiations, perform the internal audit function, or perform personnel search functions, among other listed functions. An auditor does not have the right to provide audit services to an entity if there is danger of conflict of interests or threats caused by financial, personal, business, labor, and/or other current or future relations.

**168. The law provides that the shareholders appoint auditors.**<sup>164</sup> The executive recommends an auditor to the shareholders or the supervisory board. A shareholder vote on the appointment of the external auditor is required to be held as the final step.

### Audit committees

**169. The Law on Entrepreneurs requires MFIs to have an audit committee.**<sup>165</sup> An audit committee must be established from members of the supervisory board for a PIE (which includes MFIs). The committee must be comprised of members of the supervisory board and must include at least one independent member. The audit committee is tasked with supervision of the financial reporting preparation process, as well as supervision of the performance of the audit of the financial reports. Members of the committee must be competent in the activities of the entity and at least one of the members must be competent in accounting or auditing. The committee must report to the supervisory board and the shareholders on a regular basis. In practice, not all MFIs have an audit committee.

### Filing/publication of financial statements

**170. PIEs are required to file financial statements annually.** MFIs, like other PIEs in Georgia, are required to submit audited financial statements to SARAS by

no later than October 1 of each year for the preceding year. This requirement includes a full set of Georgian language IFRS compliant financial statements and a management report. SARAS conducts certain validation checks on the information submitted, and then the information is posted on a public SARAS website.

### Monitoring and enforcement – financial reporting

**171. The NISD has no dedicated team with responsibility for reviewing financial statements.** The NISD reviews reconciliations of annual regulatory reports with IFRS financial statements after those financial statements have been published (June 15). The NISD requests the management letter from the auditors and reviews it. Otherwise, the NISD relies on the SARAS process.

**172. SARAS has a process for reviewing financial statement compliance with IFRS.** SARAS selects financial statements for review based on a risk-based methodology.<sup>166</sup> SARAS publishes a report of its findings from the review of financial statements. The capacity and ability of SARAS to perform these reviews of compliance with IFRS is discussed elsewhere in this report.

**173. The enforcement of financial reporting requirements is not provided for in the regulations.** The NISD does not impose sanctions for a noncompliant AFS. Auditors are not required to inform the NISD if they intend to issue a qualified audit opinion. The NISD does not take any supervisory measures if an MFI receives anything other than an unmodified audit opinion. SARAS may refer identified non-compliance with IFRS to the NBS for further action. However, because this is a relatively new process, no sanctions have yet been applied.

**174. NISD relies on SARAS to perform oversight on auditors of MFIs.** Accredited audit firms and auditors are obliged to cooperate with SARAS in having the firm's audit quality control system inspected. The

<sup>163</sup> The Law of Georgia on Accounting, Reporting, and Audit. Article 16.

<sup>164</sup> The Law of Georgia on Entrepreneurs, Article 57.7, CGCCB Banks, Order 215/04

<sup>165</sup> The Law of Georgia on Entrepreneurs, Article 57

<sup>166</sup> <https://saras.gov.ge/en/News/Detail/2614> "Non-compliances identified as a result of reviewing annual reports"

capacity and ability of SARAS to perform these reviews is discussed elsewhere in this report, but in general appears good. SARAS communicates with NISD on the outcome of the engagement quality control review.

**175. Law and regulations do not require NISD to hold regular meetings with auditors; and in practice meetings do not take place.**

### Corporate governance

**176. There is no code of corporate governance for MFIs.** Some aspects of corporate governance are prescribed in the Law of Georgia on Microfinance and Law of Georgia on Entrepreneurship.

## 5. Insurance Sector

### Overview of the insurance sector

**177. The insurance sector has been growing rapidly from a small base.**<sup>167</sup> Total written premiums in the year ended December 31, 2022,<sup>168</sup> of GEL 909 million were 1.46 percent of GDP. Premium income grew from GEL 773 million in 2021, a growth rate of 17.6 percent, and is 45.5 percent higher than pre-pandemic levels. The growth of premiums in 2020 was impacted by COVID-19 but was nonetheless 7 percent. Growth in premium income has more than doubled since 2017. Gross claims have increased by 91 percent over the same six-year period to GEL 475 million in 2022. While significant growth, this is consistent with general international trends for growing emerging markets.

**178. The insurance sector consists of 18 institutions.** All 18 insurers are composite insurers, although very little life business is written. There is no domestic reinsurance-only entity. Five insurers are foreign-owned and thirteen are domestically privately-owned. There are no state-owned insurers. One domestic

insurance company is listed on the GSE. There are also 17 registered insurance brokers supporting the industry.

**179. The insurance industry is evolving, although health products (41 percent of premiums) still dominate.**<sup>169</sup> Health products have grown consistently but are reducing as a share of the overall market (44.7 percent of market in 2017). Motor third party liability is the fastest growing sector over the last five years; however, this was caused by significant growth in 2018 as a consequence of changes in legislation.<sup>170</sup> Life business comprises only 8 percent of the market, but is the fastest growing segment, having grown from 5.6 percent in 2017.

**180. Access to reinsurance is also increasing with reinsurance premiums more the doubling over the last six years (GEL 97 million in 2017 to GEL 237 million in 2022).** In 2019, gross paid claims increased by GEL 76 million to GEL 533 million caused by major claims in the portfolios of two insurance entities. The effectiveness and robustness of those entities' reinsurance is credited with having saved the two insurers from bankruptcy.

**181. The quality of the sector has remained sound.**<sup>171</sup> The five largest insurers dominate the market, with a combined market share of 67 percent in 2022. Cash and cash equivalents are the biggest asset class on the balance sheets of insurers (35.8 percent), closely followed by insurance and reinsurance receivables (31.6 percent). On average, insurance companies exceed minimum capital requirements by 50 percent.

### Insurance regulator

**182. ISSSG was established by decree in 2013.**<sup>172</sup> ISSSG was the legal successor of the insurance supervisor previously housed in the NBG. The Service is independent and accountable directly to the Government of Georgia.

<sup>167</sup> Insurance Supervisor Insurance Market Statistics, December 2022.

<sup>168</sup> For the remainder of this section references to in 2022, 2021, 2020 and 2019 mean at December 31 of that year unless otherwise specified.

<sup>169</sup> Insurance Supervisors Annual Report 2018 to 2021.

<sup>170</sup> The Law of Georgia on Compulsory Civil Liability Insurance for owner of a motor vehicle registered in a foreign country.

<sup>171</sup> Insurance Supervisor Financial Indicators of Insurance Market, December 2022.

<sup>172</sup> Decree 102 i 2013 on the Establishment of LEPL State Insurance Supervision Service of Georgia and the attached Supervisory Board.

**183. Its responsibilities are established in the Law on Insurance.**<sup>173</sup> The statutory functions of the ISSSG include promoting the stability of the insurance market, protecting consumer rights, securing the financial solvency of insurance entities, and creating a competitive environment. The ISSSG is also responsible for supervising non-state pension schemes.

**184. The governance structure of the ISSSG is established by the law.**<sup>174</sup> A supervisory board with advisory power has a membership of seven and must include: the Chair of the Finance and Budget Committee of the Parliament; the Minister of Finance; the Minister of Economy and Stable Development; the Minister of Internally Displaced Persons from the Occupied Territories, Labor, Health and Social Affairs; the Minister of Environmental Protection and Agriculture and two experts from the non-governmental sector. The ISSSG is run by the head of the service, who is appointed for five years on the recommendation of the board and can be dismissed from office by the Government.

**185. ISSSG is the sole supervisor of the insurance sector in Georgia.**<sup>175</sup> As the supervisory authority, ISSSG has the authority to license, delicense, regulate, and supervise insurers and insurance brokers. Its authority also includes establishing procedures for determining and creating reserves, determining permitted assets, and defining assets/liability, liability/capital, and solvency ratios. ISSSG defines internal accounting requirements and prepares methodological and advisory documents on issues of insurance.

**186. ISSSG has wide supervisory powers.**<sup>176</sup> ISSSG has the right to request and receive information to fulfil its obligations. ISSSG develops and operates the supervisory reporting process, including the requirements for both regular and ad-hoc reports. These reports cover financial information and statistical data. The financial reports are based

on a combination of IFRS and specific regulatory requirements based on prudential and certain conservative approaches.

**187. The ISSSG also has wide enforcement authority.** The ISSSG may apply specific sanctions if the insurer has violated provisions of the Law on Insurance, including not complying with any instruction or procedure of the ISSSG. These violations include missing deadlines for submitting reports or submitting incorrect reports. The ISSSG can send written warnings, introduce special measures, impose pecuniary penalties, suspend the right to distribute profits, or suspend the right to perform insurance activities including the revocation of licenses.

**188. The ISSSG issues an annual report, which is publicly available.** The report is published on the official website of the ISSSG<sup>177</sup> and is sent to certain stakeholders. The report analyses the state of the industry and discusses changes and impending changes in the regulatory, legal, and competitive environment. It does not discuss financial reporting issues.

**189. The ISSSG is independently funded.**<sup>178</sup> The main source of funding is a supervisory fee calculated as 1 percent of annual earned premiums and 1 percent of an insurer's annual profit generated from long term life insurance.

## Financial reporting requirements for insurance organizations

**190. Insurers have been required to comply with IFRS for general purpose financial statements since 2017.** Large PIEs were required to adopt IFRS for the year ended December 31, 2017. An insurer is defined as a PIE in accordance with the Law on Insurance.

**191. The law requires the application of the full and current version of IFRS, as issued by the IASB.**<sup>179</sup>

<sup>173</sup> The Law of Georgia on Insurance.

<sup>174</sup> The Law of Georgia on Insurance, Article 19

<sup>175</sup> The ISSSG is constrained in its authority to regulate given its legal status as a supervisory body. This does not however impact its' ability to effectively supervise financial reporting requirements.

<sup>176</sup> The Law of Georgia on Insurance, Article 21.

<sup>177</sup> [www.insurance.gov.ge](http://www.insurance.gov.ge)

<sup>178</sup> The Law of Georgia on Insurance, Article 19.

<sup>179</sup> The Law of Georgia on Insurance, and the Law of Georgia on Accounting, Reporting, and Audit.

Consolidated financial statements must be based on IFRS standards and if some parts do not comply with IFRS, it has to be disclosed. Currently, insurance contracts are accounted and reported based on IFRS 4 *Insurance Contracts*, but IFRS 17 *Insurance Contracts* will be applied from 2023. The ISSSG has engaged with the industry to monitor and assist with the implementation of the new standard. The financial statements of selected insurance companies were reviewed as part of the observed financial reporting practices and perceptions. The review concluded that most insurers likely complied with IFRS, but areas of non-compliance were identified. For details see **Section C. Observed Financial Reporting Practices and Perceptions** of this report.

**192. Prudential reporting is currently based on a mixture of accounting frameworks.** The specific financial reporting requirements for regulatory purposes apply a more conservative approach to certain items, such as bad debt reserves, income from subrogation, incurred but not reported provision, and deferred acquisition costs. The other components are required to be accounted and reported in accordance with IFRS. Insurers are required to present a separate comparative table indicating the differences between regulatory reporting and IFRS and provide relevant explanations. There are also specific differences in revenue and expense recognition for tax purposes.

**193. Insurers are required to submit audited AFS to ISSSG and make them available to the public.** The Law on Insurance requires insurers to submit audited AFS to the ISSSG no later than April 15 each year.<sup>180</sup> Insurers are required to make the financial statements available on their own website by the same date. The ISSSG also publishes the AFS on its website. Insurers, like other entities in Georgia, are required to submit audited legal entity financial statements to SARAS by no later than October 1.<sup>181</sup>

**194. Insurers are required to publish management reports.** The Law on Accounting, Reporting, and Audit requires that a management report be prepared and published each year. The report should include a general business overview, a corporate governance

statement, a risk management policy overview, the number of employees, and other relevant information. The management report requirement is not included in the specific financial reporting requirements for insurers, and consequently is only subject to the timeline set by SARAS (October 1). The reports are also made available to ISSSG upon request.

**195. Although insurers are required to prepare regular prudential financial reports for the ISSSG, insurers that are not listed on debt or equity markets are not required to prepare or publish IFRS compliant interim financial reports.**

### Statutory audit and other forms of independent assurance

**196. Insurers are required to have their AFS audited.** It is required by the Law of Georgia on Insurance and the Law of Georgia on Accounting, Reporting, and Audit. The AFS of insurers are required to be audited by an auditor authorized to audit PIEs (see paragraph 60).

**197. SARAS is responsible for regulating the audit profession.** Auditing standards for insurers are set by SARAS. The full and current ISA as issued by IAASB are adopted in Georgia. Further, in terms of the Law on Accounting, Reporting, and Audit, SARAS is empowered to set additional reporting and other requirements.

**198. SARAS approves audit firms who are permitted to perform the audit of PIEs (including insurers) based on both quantitative and qualitative criteria.** The process includes in-depth inspection of audit firms' processes on a regular basis. ISSSG relies on the SARAS process to identify and regulate auditors who are permitted to perform audits on insurers and does not have a process of its own.

**199. An insurer and its auditor are required to notify SARAS in the event of the termination of an audit appointment.**<sup>182</sup> The notification requirement includes a requirement for substantiation of the termination.

<sup>180</sup> The Law of Georgia on Insurance, Article 14(3).

<sup>181</sup> The Law of Georgia on Accounting, Reporting, and Audit.

<sup>182</sup> Law of Georgia on Entrepreneurs, Article 58.



**200. Audit firms of insurers in Georgia are rotated.**<sup>183</sup>

Audit partners are required to be rotated every seven years. Audit firms are required to be rotated every 10 years. The law also established a mandatory cooling off period of four years. Insurers are required to hold tender for audit.

**201. Audit firms are not allowed to provide specially prescribed services to their insurance audit client.**<sup>184</sup>

An insurers' auditor cannot provide services related to tax declarations and general tax consultation, legal services, represent the insurer in negotiations, perform the internal audit function, or perform personnel search functions, among other listed functions. An auditor does not have the right to provide audit services to an entity if there is danger of conflict of interests or a threat caused by financial, personal, business, labor, and/or other current or future relations. This provision is in line with the EU audit regulation.

**202. The law provides that the shareholders appoint auditors.**<sup>185</sup>

The executive recommends an auditor to the shareholders or the supervisory board. A shareholder vote on appointment of the external auditor is required to be held as the final step.

**203. The ISSSG does not unconditionally have the power to reject the appointment or terminate the appointment of an auditor.** Insurers do not have to notify the ISSSG about the resignation or termination of an auditor. However, the information about the auditor is reflected in the monthly supervisory financial statements.

**Audit committees**

**204. The Law on Entrepreneurs requires insurers to have an audit committee.**<sup>186</sup> An audit committee must be established from members of the supervisory board for a PIE (which includes insurance companies). The committee must be comprised of members of the supervisory board and must include at least one independent member. The audit committee is tasked

with supervision of the financial reporting preparation process, as well as supervision of the performance of the audit of the financial reports. Members of the committee must be competent in the activities of the entity and at least one of the members must be competent in accounting or auditing. The committee must report to the supervisory board and the shareholders on a regular basis.

**205. The ISSSG has drafted amendments to the Law on Insurance on audit committees.** According to these amendments, insurers are required to have an audit committee consisting of at least 3 members, one being an independent member. Members will be required to have relevant experience in insurance and finance. The audit committee will be required to regularly report to the board of the insurance undertaking.

**Filing/publication of financial statements**

**206. Insurers are required to submit an audited AFS to ISSSG and publish it on their website by April 15.** Insurers, like other PIEs in Georgia, are required to submit audited financial statements to SARAS by no later than October 1 of each year for the preceding year. This requirement includes a full set of Georgian language IFRS compliant financial statements and a management report. SARAS conducts certain validation checks on the information submitted, and then the information is posted on REPORTAL. There are no further requirements for dissemination of the financial statements.

**Monitoring and enforcement – financial reporting**

**207. The Financial Reporting and Analysis Division, a subdivision of the ISSSG is responsible for reviewing financial statements of insurers.** The Financial Reporting and Analysis Division is a dedicated unit within the ISSSG Supervision Department responsible

<sup>183</sup> Law of Georgia on Accounting, Reporting, and Audit.

<sup>184</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 16.

<sup>185</sup> The Law of Georgia on Entrepreneurs, Article 57.7.

<sup>186</sup> The Law of Georgia on Entrepreneurs, Article 57.1.

for reviewing the financial statements of insurers, and specifically for confirming that financial reporting and disclosure requirements are met. The unit also reviews auditor reports. The common year-end of insurers in Georgia means that the timeline of review of financial statements is tight. The division has five staff members with IFRS expertise in insurance. The team focusses its initial activities on the key difference between accounting and prudential measures, and then on higher risk areas such as reserving. The objective is nonetheless to fully review the financial statements before publication. SARAS also has a complementary process for reviewing financial statement compliance with IFRS. SARAS publishes a report of its findings from the review of financial statements.

**208. Enforcement of financial reporting requirements is not clearly provided in the regulations.** If misleading information appears as a result of gross negligence or wrongful actions of the insurers, appropriate adjustments are required, and sanctions can be applied. Sanctions may include warnings, fines, suspension, or withdrawal of license, or in severe cases the issue might be informed to relevant criminal investigation bodies. Several previous cases of under-reserving, when revealed, triggered on-site inspections. SARAS may refer identified non-compliance with IFRS to the ISSSG for further action. However, because this is a relatively new process, no sanctions have yet been applied.

**209. ISSSG relies on SARAS to perform oversight on auditors of insurers (see paragraph 198).** The details of the SARAS process are set out in **Section II. B.9 Audit regulation, quality assurance and public oversight** of this report, and the performance indicators in paragraph 314.

**210. Law and regulations do not require ISSSG to hold regular meetings with auditors.** In practice, meetings are only taking place on an irregular basis for very specific reasons. The supervisor does not

have the power to establish or increase the scope of external audits. Preliminary notification by the auditor of the intent to issue a qualified report is also not required. For material matters or differences, appropriate adjustments in the supervisory financial statements are required or appropriate on-site inspections are initiated.

### Corporate governance

**211. There is no code of corporate governance for insurers.** Some issues of corporate governance are prescribed in either the Law on Insurance or Law on Entrepreneurs. Despite the absence of a corporate code, the Law on Insurance does provide for the ISSSG to impose specific sanctions for violation of the rules of corporate governance. New insurance legislation is being drafted that will address corporate governance issues according to European legislation. The new framework will include a wide range of improvements and increases in the capacity of ISSSG.

### Performance Indicators – Financial reporting and auditing for insurance companies

**212. The overall rating attributed under the performance indicator “Financial reporting and auditing for insurance companies” is 2.9 out of 4, which equals the simple mean of the rating criteria comprising sub-indicators A and B below ( $2.9 = (3.0+2.8)/2$ ).**

*Sub-Indicator A. Financial reporting and auditing requirements for insurance companies.*

**213. The attributed rating is 3, which equals the simple mean of the rating criteria comprising sub-indicators A.1-A.3 below (i.e.,  $3 = (3+3+3)/3$ ).**

### A.1. Financial reporting requirements for insurance companies

Georgia Rating	<b>3</b>	Insurance companies prepare IFRS compliant AFS for both the legal and consolidated entity, along with a separate management report. The management report is not required to be published at the same time as the financial statements. Insurance companies in Georgia that are not listed on the debt or equity markets are not required to prepare or publish IFRS compliant interim financial statements.
Rating Criteria	1	Criteria for "2" rating not met.
	2	Insurance companies are required to prepare legal entity financial statements on an annual basis, in accordance with prescribed financial reporting standards.
	3	In addition to requirements under "2": Insurance companies are required to prepare a management report (or MD&A). Insurance companies are required to apply IFRS for consolidated AFS.
	4	In addition to requirements under "3": Insurance companies are required to prepare IFRS compliant interim consolidated financial statements.

### A.2. Audit requirements for insurance companies

Georgia Rating	<b>3</b>	<p>The annual financial report is audited and auditors attest to accompanying material, including the management report. Insurance companies are required to form an audit committee of a minimum of three members, one of which must be independent. There are no regulations in place to ensure a member has recent relevant financial or auditing experience.</p> <p>Refer to comment A.1. above, there is no requirement for unlisted insurers to submit interim financial statements.</p> <p>Auditors are required to be appointed by shareholders and the appointment is subject to the express approval of the regulator.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	<p>The legal entity and consolidated financial statements of insurance companies are subject to annual statutory audits.</p> <p>Shareholders (at the AGM) or board of directors (i.e., a governance body independent of management) is legally responsible for the appointment and dismissal of auditors of insurance companies.</p>
	3	<p>In addition to requirements under "2":</p> <p>The auditor's report is required to attest whether the management report (or MD&amp;A) and other financial information in the annual report have been read for consistency with the financial statements. Insurance companies are required to form an audit committee.</p> <p>At least one member of the audit committee is required to be an independent director. At least one member is required to have recent and relevant financial or auditing experience.</p>
	4	<p>In addition to requirements under "3":</p> <p>Interim consolidated financial statements of insurance companies are required to be reviewed by the auditors.</p> <p>The audit committee comprises only independent directors. At least one member is required to have recent and relevant financial reporting or auditing experience.</p> <p>Auditors of insurance companies are required to be appointed by shareholders at the AGM (if applicable) or by the board of directors on the recommendation of the audit committee.</p>

<b>A.3. Timeliness and public disclosure of financial reports for insurance companies</b>	
<b>Georgia Rating</b>	<p><b>3</b></p> <p>All insurers must provide their AFS, audited by an independent auditor to the regulator by April 15. The complete financial statements including the audit report, but excluding the management report, must be published on their website by the same date. There is no requirement to disseminate financials statements more widely.</p> <p>The AFS and management report are published with a separate audit report on the SARAS website by October 1.</p>
<b>Rating Criteria</b>	<p>1</p> <p>Criteria for "2" rating not met.</p>
	<p>2</p> <p>Insurance companies are required to make legal entity and consolidated financial statements publicly available, although this may be in an abridged or incomplete form.</p> <p>Legal requirements are such that access to financial statements is limited or costly.</p> <p>The deadline for publication of annual reports of insurance companies is no later than nine months after the reporting date.</p>
	<p>3</p> <p>In addition to requirements under "2":</p> <p>The audit opinion is also made publicly available.</p> <p>Legal requirements are such that financial statements are disseminated broadly, but there are limitations such as cost and ease of searchability.</p> <p>The deadline for publication of annual reports of insurance companies is no later than six months after the reporting date.</p>
	<p>4</p> <p>Insurance companies are required to make the full sets of legal entity and consolidated financial statements publicly available. The auditor's report is also made publicly available.</p> <p>Insurance companies are also required to publicly disclose the interim financial statements, with accompanying management discussion and analysis.</p> <p>Legal requirements are such that financial statements are readily searchable and accessible, at low or no cost.</p> <p>The deadline for publication of annual reports of insurance companies is no later than four months after the reporting date.</p>

*Sub-Indicator B. Monitoring and enforcement of the financial reporting requirements of insurance companies.*

214. The attributed rating is 2.8, which equals the simple mean of the rating criteria comprising sub-indicators B.1-B.4 below (i.e.,  $2.8 = (3+3+2+3)/4$ ).

<b>B.1. Review of the insurance company's annual financial statements</b>	
<b>Georgia Rating</b>	<p><b>3</b></p> <p>There is a dedicated function to review financial statements excluding the management report. Financial statements are reviewed for prudential information content and for IFRS compliance.</p> <p>The regulator does not have authority to oblige amendment of the financial statements.</p> <p>SARAS also performs a complementary risk-weighted review of financial statements for compliance with IFRS. SARAS communicates relevant findings to ISSSG. The volume of financial information to be submitted by all companies to SARAS is significant and SARAS has only limited resources to deal with it, which currently restricts the extent of monitoring and enforcement activities.</p>

### B.1. Review of the insurance company's annual financial statements

Rating Criteria	1	Criteria for "2" rating not met.
	2	Review of the AFS by the insurance supervisor has <b>significant limitations</b> .
	3	Review of the AFS by the insurance supervisor has <b>minor limitations</b> .
	4	Review of the AFS by the insurance supervisor is <b>fully adequate</b> .

### B.2. Communication with external auditors on insurance companies

Georgia Rating	3	<p>Auditors are required to report significant risk and issues identified in their audit report. The auditor is not required to report directly to the regulator, and the regulator has no authority in regard to the appointment of the auditor.</p> <p>The supervisor meets auditors on an ad-hoc basis. There is limited assurance that no material risks are left unaddressed.</p> <p>However, auditors are included in communication between SARAS and the insurer in regard non-compliance with IFRS.</p> <p>Auditors are also regulated by SARAS, which has a regular and robust inspection routine. Auditors may only be appointed by a PIE if they are on a SARAS approved list.</p>
	1	Criteria for "2" rating not met.
	2	Communication between the insurance supervisor and external auditors of insurance companies have <b>significant limitations</b> .
	3	Communication between the insurance supervisor and external auditors of insurance companies have <b>minor limitations</b> .
Rating Criteria	4	Communication between the insurance supervisor and external auditors of insurance companies is <b>fully adequate</b> .

### B.3. Reporting on the review of financial reporting of insurance companies

Georgia Rating	2	<p>The supervisor prepares an annual report on its activities, which is published on its website, although there is no apparent legal obligation to do so.</p> <p>The report contains information on insurance sector operations, growth, liquidity, capital adequacy, and corporate governance, but does not focus on compliance with financial reporting requirements. SARAS performs a complementary review of compliance with IFRS in Insurers. SARAS published IFRS deficiencies that it detects through its reviews on an anonymized basis.</p>
	1	Criteria for "2" rating not met.
Rating Criteria	2	Reporting by the insurance supervisor on the review of financial statements of insurance companies has <b>significant limitations</b> .
	3	Reporting by the insurance supervisor on the review of financial statements of insurance companies has <b>minor limitations</b> .
	4	Reporting by the insurance supervisor on the review of financial statements of insurance companies is <b>fully adequate</b> .

#### B.4. Supervisory measures and sanctions

Georgia Rating	3	Supervisory measures or sanctions can be imposed by the insurance supervisor for various elements of financial reporting. The supervisor can apply various measures (administrative, civil, criminal) on companies and/or directors for financial reporting.  The measures/sanctions are sound with reasonable assurance that no material risks are left unaddressed.  The supervisor does focus on compliance with IFRS, however the sanctions available for non-compliance with IFRS requirements are limited.
	Rating Criteria	
	1	Criteria for “2” rating not met.
	2	Supervisory measures and sanctions that can be imposed by the insurance supervisor have <b>significant limitations</b> .
	3	Supervisory measures and sanctions that can be imposed by the insurance supervisor have <b>minor limitations</b> .
	4	Supervisory measures and sanctions that can be imposed by the insurance supervisor are <b>fully adequate</b> .

## 6. State-Owned Enterprises

### Overview of SOEs

**215. Georgia has been a pioneer of business environment reforms, yet the footprint of SOEs remains large.** The SOE portfolio has been reduced from 1,315 entities in 2009 to 316 entities in 2021; of these, 154 are owned by the central government and 162 by local authorities.<sup>187</sup> In addition, these SOEs control a further 96 subsidiaries. However,

SOEs remain present not only in strategic sectors such as utilities but also in commercial sectors such as transportation, manufacturing, and construction. In 2020, SOEs employed approximately 60,000 workers, accounting for about 5 percent of formal jobs. Over the past decade, the government has taken concrete steps to address SOE challenges, focusing on improving their fiscal transparency. Despite these steps, progress remains limited.

**216. Many SOEs are performing poorly, raising concerns about service delivery and posing fiscal risks.** SOEs often require subsidies and loans from the state budget, while their service delivery to citizens remains sub-optimal and their contribution to public finances in the form of taxes and dividends is below par. Between 2015–2021, SOEs received equity injections amounting to GEL 1.59 billion.<sup>188</sup> The injections were aimed at financing infrastructure projects and operational expenses. Despite these injections, SOE equity declined because of the devaluation of assets and wide-scale losses incurred by the SOEs (2021 was an exception). Due to the pandemic, the sector lost income of GEL 300 million. Although in 2021, for the first time, the profit of the sector significantly exceeded the losses, it was due mainly to exchange rate difference.

**217. Over the past decade, the Government has taken some concrete steps to address SOE challenges, focusing on improving fiscal transparency.** The main achievement of recent years is the strengthened fiscal oversight by the MoF and publication of a comprehensive annual Fiscal Risk Statement since 2017, containing a significant amount of information and analysis of SOEs’ performance and corporate governance. Significant steps were also taken to improve the MoF’s financial monitoring function of SOEs, and creation of a Fiscal Risk Management Unit responsible for compiling, assessing, and reporting performance information. A Comprehensive SOE Reform Strategy was adopted in December 2022.

**218. 48 large and medium SOEs were classified as PIEs and must comply with the relevant provisions of the Law on Accounting, Reporting, and Audit.**<sup>189</sup>

<sup>187</sup> Comprehensive SOE Reform Strategy for 2023-2026

<sup>188</sup> Ministry of Finance of Georgia, Fiscal Risk Analysis Document, 2021 - 5th Update, p.3.

<sup>189</sup> Ordinance of the Government of Georgia on Establishing Criteria for Designating Enterprise as a Public Interest Entity by the Service of Accounting, Reporting, and Audit Supervision (SARAS).

Since 2020, these companies must comply with the PIE provisions of the Law on Accounting, Reporting, and Audit, including IFRS-based accounting and financial reporting, preparation of a management report, and annual audit with full disclosure on the website of SARAS.

**219. The SOE categorization exercise was carried out by the MoF in 2020 with International Monetary Fund (IMF) assistance.** It classified all Georgian SOEs into: (i) public corporations (SOEs) or (ii) general government units, as per the IMF Government Finance Statistics Manual.<sup>190</sup> This classification is independent from the PIE designation in Georgian legislation. Under the new classification:

- \* 52 entities were defined as public corporations, which function as fully commercial entities or have a potential of transitioning into commercial enterprises, and
- \* 183 entities were defined as general government units, as they do not perform commercial activities

and permanently depend on government subsidies and other types of financial support.<sup>191</sup>

**220. Multiple government agencies currently own and supervise SOEs, which complicates the oversight arrangements, dilutes SOEs' public accountability, and induces conflict of interest between the ownership and policy-making functions of government.** These various agencies carry out the government's ownership functions with respect to their portfolio SOEs, meaning they make key decisions at both the strategic and operational level. These agencies establish policies, vote in shareholder meetings, and thus approve capital increases and changes to companies' charters. This creates complications in informed decision making. Concern about poor SOE financial performance and weak corporate governance standards and practices, especially in the case of those SOEs that deliver critical public services, has brought SOEs to the top of the government reform agenda.

**Table 6.** Largest SOEs in Georgia (sorted by total assets, thousands of GEL, 2021)

SOE Name	Legal Status	Sector	Total Assets	Total Employees
Partnership Fund	JSC	Other financial service activities, except insurance and pension funding	4,493,690	68*
Marabda-Kartsakhi Railway	LLC	Construction of railways and underground railways	1,849,788	81*
Georgian State Electrosystem	JSC	Transmission of electricity	1,490,336	1,531
United Water Supply Company of Georgia	LLC	Water collection, treatment, and supply	1,427,882	2,851
Tbilisi Transport Company	LLC	Urban and suburban passenger land transport	719,256	6,486
Engurhesi	LLC	Production of electricity	476,374	1,277
Georgian Gas Transportation Company	LLC	Transport via pipeline	204,834	839*

<sup>190</sup> IMF: Government Finance Statistics Manual 2014 (<https://www.imf.org/external/np/sta/gfsm/>)

<sup>191</sup> Fiscal Risk Statement, MoF.

SOE Name	Legal Status	Sector	Total Assets	Total Employees
Electricity System Commercial Operator	JSC	Distribution of electricity	149,778	76*
United Energy System Sakrusenergo	JSC	Transmission of electricity	146,975	288*
Georgian Post	LLC	Postal activities under universal service obligation	127,151	3,000
State Construction Company	LLC	Construction of roads and motorways	84,000	67*

\* Employment data for December 2019; Source: Fiscal Risks Analysis Document (2020) by MOF.

Source: Fiscal Risks Statement (2021) by MOF; Financial Statements for 2021.

## SOE regulations

**221. SOEs are entities of private law, incorporated as JSC or LLC.** The Law on Entrepreneurs is a foundational legislative framework for all types of legal entities, including SOEs.<sup>192</sup> In addition, SOEs are regulated by general norms of the Labor Code,<sup>193</sup> the Law on Rehabilitation and the Collective Satisfaction of Creditors' Claims,<sup>194</sup> and other laws applicable to private companies. Public procurement law applies to all state majority owned SOEs in Georgia. Several major SOEs are also subject to specific government orders on special procurement of goods and services that enables them to simplify some of the procurement procedures for goods and services essential for their business. Only one SOE – the Partnership Fund – is regulated by their own special law.<sup>195</sup>

**222. A comprehensive SOE Reform Strategy for 2023-2026 has been adopted by the government with donor support.**<sup>196</sup> The Strategy is based on the sectorization exercise, hence is mainly limited to PIEs that are public corporations. It outlines the basis for continued state ownership of SOEs. The SOE strategy is based on five pillars and specifies the Government's

rationale for continued SOE ownership, prioritizes SOE's orientation on commercially profitable activities, clarifies the principles of competitive neutrality for SOEs, proposes the MoF and MoESD as the joint ownership entities, and sets corporate governance requirements. The Strategy calls for a new SOE Framework Law to be developed and enacted to guide the reforms. For commercial SOEs that are PIEs, the strategy envisages implementation of the Organisation for Economic Co-operation and Development (OECD) Guidelines on the Corporate Governance of State-Owned Enterprises. The implementation of the Strategy will start with three pilot SOEs: JSC Georgian Railways, LLC United Georgian Airports, and LLC Georgian Gas Transportation Company.

## Financial reporting and independent audit requirements for SOEs

**223. Accounting, financial reporting, and audit practices in Georgia are advanced, requiring all entities — private and state-owned — to report and publicly disclose their financial information.** In accordance with the Law on Accounting, Reporting, and Audit and the Ordinance of the Government

<sup>192</sup> The Law of Georgia on Entrepreneurs.

<sup>193</sup> Labor Code of Georgia.

<sup>194</sup> The Law of Georgia on Rehabilitation and the Collective Satisfaction of Creditors' Claims.

<sup>195</sup> The Law of Georgia on a Joint Stock Company – Partnership Fund of Georgia

<sup>196</sup> [http://www.economy.ge/uploads/files/2017/reformebi/sacarmoebus\\_reforma/2\\_strategy.pdf](http://www.economy.ge/uploads/files/2017/reformebi/sacarmoebus_reforma/2_strategy.pdf)



of Georgia on Establishing Criteria for Designating Enterprise as a PIE by SARAS, large and medium SOEs attained PIE status in 2020. Hence, SOEs became subject to higher transparency standards and disclosure requirements, including IFRS-based accounting and financial reporting, preparation of management reporting, non-financial reporting, and annual audits with full disclosure on SARAS REPORTAL. Enforcement over noncompliance with reporting requirements is delegated to the respective sector regulating bodies (the Georgian National Energy and Water Supply Regulatory Commission and the Georgian National Communications Commission) who act based on information provided by SARAS. These bodies act in accordance with their regulations, which may stipulate different sizes of sanctions and timelines for enforcement.

**224. SOEs are also subject to additional specific legislation related to their oversight.** For example, SOEs are subject to the audit authority of the State Audit Office (SAO). SAO audits the financial and economic activities of SOEs where the state holds more than 50 percent of shares, unless the enterprise's securities are traded on a securities market, in which case SOEs are not subject to SAO audit.<sup>197</sup> However, due to low-capacity, SAO audits are often only performed once in several years. To ensure an additional layer of accountability, chief executive officers of 100 percent state-owned enterprises are required to file their asset declarations annually.<sup>198</sup>

**225. To achieve early availability of information on the financial results of SOEs, MoF introduced more stringent deadlines for their financial reporting.**<sup>199</sup> The new regulation requires SOEs that are PIEs to submit their audited AFS and other types of reports to the SARAS by July 1 of the year immediately following the reporting period, and unaudited financial and other types of reports by April 1. However, in practice, SOEs largely do not follow this requirement, as it fails to provide a mechanism of corresponding sanctions. Currently, 120 SOEs submit their reports

based on the provided templates to the MoF in addition to publishing them on REPORTAL. All of the SOEs' financial statements reviewed within the ROSC assessment likely did not comply with some significant aspects of IFRS accounting standards. For details see **Section C. Observed Financial Reporting Practices and Perceptions** of this report.

**226. Large or medium SOEs are required by the Law on Accounting, Reporting, and Audit to have their AFS audited.** Small-sized SOEs are not subject to mandatory annual audit. The law requires that all audits comply fully with ISA.

**227. An SOE performance monitoring system involving seven SOEs was adopted on June 10, 2022.**<sup>200</sup> Led by the MoF's Fiscal Risk Management Unit, it is aimed at ensuring the financial transparency of SOEs, reducing fiscal risks, and improving financial management standards. The monitoring does not include review of financial statements for compliance with IFRS - this task is being carried out by SARAS. The resolution<sup>201</sup> introduces a "statement of corporate intent" that is aimed to "define the financial and non-financial goals that need to be achieved within limited risks." This statement is a four-year plan to be submitted to the MoF and updated annually. Seven SOEs presented corporate intent statements to the MoF for the first time in October 2022. This clear goal setting is an important step forward in the SOE reform but, as this requirement is new, it is not yet tested for implementation effectiveness.

## Corporate Governance

**228. As PIEs, SOEs are required to have at least one independent board member and at least one board member competent in accounting and/or audit on its supervisory board.** PIEs with a supervisory board are required to establish an audit committee within it. SOEs that do not have supervisory boards are

<sup>197</sup> The Law of Georgia on State Audit Office, Article 17.2.i

<sup>198</sup> Resolution of the Government of Georgia on the Rules for Submitting the Declaration of Assets of an Official and Approval of the Job Register of the Officials Who Are Obligated to Fill in the Declaration of Assets, Article 20. #178, 03.04.13.

<sup>199</sup> Government of Georgia Decree N217 on Defining Timeframe of Reporting for State-Owned Enterprises of Public Interest and Their Daughter Companies, 11th February 2021

<sup>200</sup> Resolution of the Government of Georgia on Financial Oversight of the SOEs N1012.

<sup>201</sup> Ibid.

required to establish standalone audit committees staffed with independent members elected by the annual meeting of shareholders. However, SOEs are still in the process of establishing audit committees and have not achieved compliance with this legal requirement.

**229. CGCSOE was introduced in 2021, marking an important step in establishing a corporate governance framework for SOEs.** It sets basic corporate governance requirements and is also designed to be implemented on an “apply or explain an alternative” approach. The list of SOEs subject to the code had not been issued at the time of the ROSC A&A assessment so the CGCSOE was not yet implemented. Although, three SOEs were selected by the SOE Strategy to pilot the CGCSOE.

## 7. The Accountancy Profession

**230. Professional activity in the field of accounting and financial reporting in Georgia is not subject to licensing and certification by any legal requirement or through a national regulatory body; only auditors are regulated at the state level.** There is no legal requirement for accountants to be a member of a local PAO or to be certified, other than if the accountant wishes to register to perform audit services. Membership of a PAO is otherwise on a voluntary basis; however, PAOs do have requirements to qualify as a member.

**231. The Law on Accounting, Reporting, and Audit defines the criteria for certified accountants.** This is defined as a person who is certified by a professional organization of accountants and/or auditors in accordance with the professional certification standards established by SARAS and who maintains appropriate standards of CPD. SARAS has established and maintains the professional certification standards, which comply with the requirements of EU directives for auditors and with IES established by the IAESB, supported by IFAC. SARAS has to date recognized only the GFPAA qualification for this purpose.

**232. The SARAS process to recognize PAO qualifications includes confirming compliance with the requirements of IES.** The compliance of registered

auditors with the requirements of IES 8, which relates to the education of auditors, is confirmed through the audit firm monitoring process.

**233. The minimum entrance requirements for both certified accountants and to become a member of a PAO include holding a relevant degree and successfully completing professional certification.**

For an auditor, the practical experience is defined as at least three years of practical experience in the audit of financial statements under the supervision of an auditor. This is monitored by SARAS. For PAOs it is three years of experience in financial accounting and reporting, monitored by the PAO.

**234. GFPAA offers two professional certification programs under the local accountancy qualification.**

The full professional certification program consists of 13 modules (full qualification), grouped into 3 levels, and is based on the Association of Chartered Certified Accountants (ACCA) qualification curricula translated into the Georgian language. This leads to the qualification of a professional accountant. GFPAA also offers a certification program, consisting of 4 modules. A person who successfully passes exams on all 4 modules receives a certified accountant qualification. Since 2017, GFPAA is recognized by SARAS as a professional body entrusted with administering certifications, qualification exams, and CPD of their members. According to the law and SARAS regulation, these programs must be aligned with IES, EU Directives, and comply with the Professional Certification Standard and the Continuous Education Standard set by SARAS. GFPAA's certification program is based on the ACCA syllabus, and requires a three-year practical experience and final examination, which is administered by GFPAA. The certification program is updated as a minimum once in three years to incorporate changes in national legislation and international standards and syllabus updates. Assessments and CPD are conducted in accordance with the Professional Certification Standard and Continuous Education Standard. Compliance with SARAS requirements is confirmed on an annual basis. GFPAA, other professional organizations, and the Big 4 audit firms are jointly developing CPD programs, which are being reviewed and approved by SARAS, to achieve a unified approach to CPD programming.

**235. SARAS maintains a register of accountants which lists certified accountants in Georgia and indicates the nature of their qualification.**<sup>202</sup> This register is available to the public via the SARAS website and is intended to help members of the public and companies to find the right certified accountant to meet their requirements. There are approximately 900 certified accountants on the register. These include certified accountants holding GFPAA's recognized qualification, holders of recognized international qualifications, who have passed tests on local tax and law, and auditors who already held the previously recognized audit qualification prior to the introduction of the new Law on Accounting, Reporting, and Audit in 2016.

**236. The Law on Accounting, Reporting, and Audit was amended in December 2022 to bring all accountants and accounting firms providing professional services under the supervision of SARAS.** The Law was amended based on AML and countering terrorist financing (CTF) legislation. This amendment introduced the requirement for accountants and accounting firms providing professional services (mainly outsourced accountancy services) to join the SARAS register of accountants and for SARAS to be able to set CPD requirements for such accountants.

**237. Auditors must be certified accountants as defined in the law with the certification process administered by a PAO recognized for these purposes by SARAS.** Only one PAO - GFPAA - is recognized by SARAS for the provision of the professional certified accountant qualification exams for auditors. Following a detailed assessment process, SARAS has recognized GFPAA's professional certification process as compliant with SARAS' professional certification standards, which incorporate compliance with EU requirements and relevant IES requirements. This assessment also covers the quality and administration of examinations and the quality of teaching and learning materials.

**238. Auditors have to meet additional requirements in addition to certification, such as having suitable work experience, maintaining CPD, and holding professional indemnity insurance.**

## Professional Accountancy Organizations

**239. Other than for auditors, PAOs in Georgia set their own requirements for their members.** The two main PAOs (GFPAA and Georgian Federation of Accountants, Auditors and Financial Managers – GFAAFM) have different categories of membership (full, associate, etc.). All members are expected to have completed higher education and require a minimum period of relevant work experience (accounting, financial reporting, economics, etc.), which is assessed and monitored by the PAOs.

**240. GFPAA is the largest PAO in Georgia and is the only PAO that is a member of IFAC.** GFPAA was established in 1996 and gained full membership of IFAC in 2000. GFPAA full members must complete its professional qualification program. It has 5,893 members, of which 755 are full members holding a professional qualification and 5,138 are associate members.

**241. As part of its membership of IFAC, GFPAA periodically prepares a self-assessment of their compliance with the IFAC SMOs in the form of a SMO Action Plan.** GFPAA submitted an updated self-assessment in 2022 which is under consideration by IFAC. The latest assessment published by IFAC on its website analyses the 2019 self-assessment. A number of the actions from the IFAC assessment based on the 2019 Action Plan have been implemented and there are a few areas where actions are ongoing, including improving the investigation and discipline (I&D) scheme and its operation. Once IFAC's assessment of the 2022 Action Plan is complete, GFPAA will work on addressing any areas of non or partial compliance identified by IFAC.

**242. The other main PAO, the GFAAFM, unites small and medium audit practices.** Its members include 244 members certified as auditors under the previous audit certification program. It also has 110 non-certified members and 45 corporate members.

**243. GFAAFM has an agreement with a training provider to provide training for its members.** This covers various areas including tax, internal audit, and financial management.

<sup>202</sup> <https://www.saras.gov.ge/en/CertifiedAccountant>

**244. The profession in Georgia might benefit from consolidation of the PAOs.** This would bring economies of scale and increase the access of GFAAFM members to the greater resources of GFPAA. Such consolidation should be considered.

### International Education Standards

**245. Educational requirements for auditors are set by the Law on Accounting, Reporting, and Audit and further detailed by SARAS regulations and standards.** SARAS regulations and standards set out the required content and administration requirements for the certification of certified accountants and auditors. The certification standards fully implement the requirements of the IES set by the IAESB, supported by IFAC. Other requirements of the IES are implemented through ongoing requirements of audit registration, including work experience requirements and CPD.

**246. IFAC's latest assessment of compliance with IESs indicated "partial compliance", based on a self-assessment by GFPAA from 2019.** Subsequent improvements were noted by the ROSC team, such as alignment of university curricula with the

professional qualification and the publishing of a model professional accounting and audit curricula by SARAS. SARAS assesses that GFPAA's qualifications comply with IESs, but the IFAC rating is given below as required by the ROSC A&A process. IFAC are currently assessing an updated self-assessment by GFPAA submitted in 2022.

**247. The GFPAA's professional qualification has been in operation for more than 15 years and fully complies with the IES and EU requirements for audit qualifications, as confirmed by SARAS recognition.** It is available in the Georgian language and is well aligned with the professional qualification of ACCA. GFPAA has learning materials for each subject paper of the qualification which are regularly updated and of high quality. However, GFPAA has required donor assistance to maintain the materials due to insufficiency of necessary funds. GFPAA believes that the SARAS assessment process has imposed a requirement to update all materials on an unnecessarily frequent basis. Updating only those materials relevant to changes in standards etc. would be more appropriate and affordable. GFPAA also provides training on the subjects of the qualification. Income from education accounts for a significant proportion of GFPAA's income.

**Table 7.** PAO membership breakdown as of December 2022

Member Category	Female	Male	Total
<b>GFPAA</b>			
Full members	464	291	755
Associate members	3,618	1,520	5,138
<b>Total</b>	<b>4,082</b>	<b>1,811</b>	<b>5,893</b>
<i>Of which members in public practice:</i>	<i>146</i>	<i>172</i>	<i>318</i>
<b>GFAAFM</b>			
Certified auditor members	70	174	244
Non-certified members	73	37	110
<b>Total</b>	<b>143</b>	<b>211</b>	<b>354</b>

Source: GFPAA, GFAAFM

248. GFPAA has high success rates in its final exams. In the last three years, 1,530 candidates enrolled in the final examination, comprising 1,193 women and 337 men. In this period, the final examination was passed by 1,130 (73.8 percent) candidates, comprising 872 women and 275 men.

249. GFPAA works with universities and others to offer exemptions where appropriate for subject papers in its qualification. The program includes three stages of certification (levels 1, 2, and 3). Out of 13 modules of the program, an applicant can be exempted in 8 modules across levels 1 and 2. Exemptions at level 3 are not available. Exemptions can be granted following confirmation that similar knowledge has been obtained and appropriately examined in institutions recognized by GFPAA as adequate, according to an established procedure.

250. GFAAFM has an agreement with GFPAA whereby its students may undertake GFPAA's professional qualification exams.

### Code of Ethics for Professional Accountants

251. The Law on Accounting, Reporting, and Audit requires all auditors to comply with the IESBA *Code of Ethics for Professional Accountants*. The implementation of the Code of Professional Ethics shall be ensured by SARAS within six months of any revisions. A certified accountant and auditor/audit firm is also entitled to use the effective (English) version of the Code (IESBA Code).

252. Enforcement of auditors' compliance the IESBA Code of Ethics is the responsibility of SARAS. Audit inspections assess compliance, and any potential non-compliance is addressed by the investigation and disciplinary function of SARAS.

253. GFPAA requires all its members to comply with the IESBA Code of Ethics. GFPAA's Ethics and Disciplinary Committee ensures the investigation of any violation of the Code of Ethics by non-auditor GFPAA members.

254. GFAAFM requires all members to comply with the IESBA Code of Ethics. However, their enforcement mechanism has not been operational and has not considered any cases of potential misconduct.

### Investigation and Discipline System

255. SARAS is responsible for the I&D of auditors. This is in relation to potential professional misconduct relating to ethical and any other professional requirements. The sanctions available to SARAS are defined in the Law on Accounting, Reporting, and Audit and are different for: violations relating to AML/CTF law by an auditor or by a PAO; violations relating to audit requirements by an auditor or by a PAO.

256. According to the Law on Accounting, Reporting, and Audit, where a potential offence under the law is detected, SARAS investigates and determines whether such an offence has taken place. In the event of failure to fulfil financial reporting requirements, SARAS can impose monetary fines ranging from GEL 500 for microenterprises up to GEL 10,000 for PIEs. Any dispute of this finding can be reviewed by the SARAS board.

257. In cases of misconduct or non-compliance with standards and registration requirements by auditors, SARAS can impose fines of up to GEL 5,000 on an auditor or audit firm. The individual auditor concerned can appeal to the court at any time. In addition, SARAS has the power to remove the auditor from the register.

258. The gap between a maximum fine of GEL5,000 on auditors, which has a low deterrent effect, and deregistration, an ultimate sanction, is large. The effectiveness of regulation of auditors would be improved by the availability of a greater range of sanctions on auditors in cases of misconduct.

259. SARAS has instigated and successfully concluded a number of I&D cases concerning mostly issues relating to registration requirements. The system was shown to function overall well.

**260. GFPAA is responsible for the I&D procedures of its members.** Where misconduct is proven, GFPAA can apply the following disciplinary measures to a member:

- a. Reference/instruction - a written appeal to the respondent instructing them to stop or not to repeat the inappropriate behavior.
- b. Obligation - a written request to the defendant requiring them to stop or not to repeat the inappropriate behavior.
- c. Public warning - publication of a statement on the GFPAA website warning the respondent (may contain the content of a severe warning) to stop or not to repeat the inappropriate behavior;
- d. Suspension of membership - restriction of the use of the GFPAA member's name for a specified period (maximum three years) and publication of an announcement on the GFPAA website.
- e. Expulsion - canceling GFPAA membership and publishing an announcement about it on the GFPAA website.

GFPAA's Ethics and Disciplinary Committee has considered five cases of possible misconduct to date, of which two led to formal investigations and disciplinary measures.

**261. GFPAA's self-assessment of compliance with IFAC's SMO 6 requirements relating to I&D prepared in 2019 concluded that there were a number of minor areas where its compliance could be improved.** These included: establishment of a process for the independent review of complaints on which there was no follow-up; defining a process for

liaison with outside bodies on possible involvement in serious crimes and offences; and a regular review of implementation and effectiveness of the system and implementation of corrective actions.

**262. GFPAA's 2022 updated self-assessment (submitted to IFAC) notes that it now fully complies with SMO 6. IFAC is currently analyzing this assertion.** However, as the IFAC rating for SMO 6 compliance remains at 'partially adopted' at the time of this report, the rating for the ROSC concurs with the IFAC rating. GFAAFM has established an I&D process and I&D committee but has not considered any cases to date.

**263. The I&D function relating to auditors, implemented by SARAS, appears to be fully in compliance with international best practices and the principles of SMO 6, although SMO 6 relates to PAOs, not regulators.** GFPAA's I&D process appears to be close to compliant with SMO 6. It is not clear whether GFAAFM's process is compliant - it does not self-assess as it is not an IFAC member. However, the effectiveness of the I&D process correlates with the degree of public interest of those subject to the processes.

### Performance Indicators – Accountancy Profession<sup>203</sup>

**264. The overall rating attributed to Georgia under the performance indicator "Accountancy Profession" is Partially Adopted.**

<sup>203</sup> The performance indicator ratings for the Accountancy Profession section of the ROSC assessment are based on the ratings of the professional assessment of IFAC, most notably that of their Member Compliance Program. There are seven benchmarks used for the ratings as set forth under IFAC SMOs of which only three are used for ROSC: (1) SMO 2 - International Education Standards for Professional Accountants; (2) SMO 4 - Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA); and (3) SMO 6 - Investigation and Discipline.

International Education Standards		
Georgia Rating	<b>Partially Adopted<sup>204</sup></b>	<p>Educational requirements for the audit profession fully complying with the IES are set in law and are implemented by the state regulator. Educational requirements for professional accountants fully complying with the IES are set by the two PAOs.</p> <p>The CPD policies of both SARAS and the PAOs align with IES7 and provision is of high quality and widely available due to a partnership agreement between the PAOs and a leading Big 4 international accounting firm.</p>
Rating Criteria	Adopted	The requirements of the IES in their entirety in effect as of the time of the assessment have been adopted for all aspiring professional accountants and professional accountants as defined in the jurisdiction.
	Partially Adopted	<p>Requirements from an earlier version of IES have been adopted.</p> <p><i>or</i></p> <p>Some of the requirements of the IES in their entirety in effect as of the time of the assessment have been adopted for professional accountants.</p> <p><i>or</i></p> <p>The requirements of the IES in their entirety in effect as of the time of the assessment have been adopted for a segment of the profession.</p>
	Not Adopted	The requirements of the IES have not been adopted.

Code of Ethics for Professional Accountants		
Georgia Rating	<b>Adopted</b>	<p>The IESBA Code of Ethics for Professional Accountants is required for all auditors and professional accountants.</p> <p>Mechanisms for the enforcement of the code are in place for auditors (SARAS) and for professional accountants (POAs). The mechanism for one of the POAs has not been used in practice.</p>
Rating Criteria	Adopted	The Code of Ethics for Professional Accountants in effect as of the time of the assessment has been adopted for all professional accountants.
	Partially Adopted	<p>An earlier (2009 or later) version of the Code of Ethics for Professional Accountants has been adopted for all professional accountants.</p> <p><i>or</i></p> <p>Some requirements of the Code of Ethics for Professional Accountants in effect as of the time of the assessment have been adopted.</p> <p><i>or</i></p> <p>The Code of Ethics for Professional Accountants has been adopted for a segment of the profession.</p>
	Not Adopted	<p>The Code of Ethics for Professional Accountants has not been adopted.</p> <p><i>or</i></p> <p>A pre-2009 version of the Code of Ethics for Professional Accountants has been adopted.</p>

<sup>204</sup> At the time of this report, the IFAC rating for adoption of IES is 'Partially compliant'. Improvements in compliance were noted during this ROSC assessment but did not affect this grading, which must reflect the IFAC assessment.

Investigation and Discipline System		
Georgia Rating	<b>Partially Adopted</b>	<p>SARAS operates an I&amp;D system for auditors in accordance with the Law on Accounting, Reporting, and Audit. SMO 6 is a requirement for PAOs so is not relevant to regulators; however, SARAS' scheme complies with the concepts of IFAC's SMO 6.</p> <p>GFPAA self-assessed in 2019 that its compliance with SMO 6 could be improved, including independent review of complaints, which did not lead to investigation. In its updated self-assessment submitted to IFAC in 2022, GFPAA noted that it now fully complies with SMO 6. IFAC is currently assessing this assertion.</p> <p>GFAAFM has established an I&amp;D system, but it has not been active in practice. It has not been self-assessed for compliance with SMO 6 as GFAAFM does not aspire to IFAC membership.</p>
Rating Criteria	Adopted	An I&D system, incorporating all of the requirements of SMO 6, has been established and is operational for all professional accountants.
	Partially Adopted	<p>An I&amp;D system, incorporating all of the requirements of SMO 6, has been adopted and is operational for a segment of the profession.</p> <p><i>or</i></p> <p>An I&amp;D system for all professional accountants has been established and is operational but only incorporates some of the requirements of SMO 6.</p> <p><i>or</i></p> <p>An I&amp;D system, incorporating all of the requirements of SMO 6, has been established but is not yet operational.</p>
	Not Adopted	I&D system is not established

## 8. Professional Education and Training

**265. Professional accounting education in Georgia is defined by the Law of Georgia on Accounting, Reporting, and Audit, and by two Regulations issued by SARAS: the Professional Certification Standard and Continuous Education Standard.** The Professional Certification Standard (the Standard)<sup>205</sup> was issued in 2017 and last updated in December 2022, and determines the training disciplines for professional certification, as well as the procedure for conducting the examination process, exemption from exams, the documentation to be submitted for professional certification, and the procedure for issuing the certificate. The Standard complies with the requirements of EU Directives and IES.

**266. According to the Standard, professional certification of a candidate and the issuance of a certificate confirming the status of a certified accountant is carried out by a PAO.** The higher education considered in the Standard includes a bachelor's, master's, or doctorate academic degree or equivalent. The PAO grants the status of a certified accountant to a person who has a higher education and has completed a full certification program. The certification program should be recognized by SARAS, according to the rules it has established. The PAO is authorized to perform both the training and the assessment. Universities offering education degrees in accounting and audit who are willing to seek exemptions from a PAO as part of their accountancy professional education program should submit their education programs to SARAS for recognition, in line with the procedure set forth by SARAS in the Standard.

<sup>205</sup> Order of the Head of SARAS No. N-16 of September 25, 2017 On the Approval of the Professional Certification Standard and the Procedure for the Recognition of Certification Programs and Examination Process (<https://www.matsne.gov.ge/ka/document/view/3811685?publication=8>)



PAOs and other institutions carrying out educational activities (including recognized universities) are obliged to update the syllabus of certification programs/courses/separate disciplines (subjects) at least once in three years in accordance with the changes made in the legislation and other regulatory norms (standards).

**267. The Continuous Education Standard<sup>206</sup> sets the requirements for maintaining a certified accountant's qualification, defines the CPD program, and the legal grounds for its implementation and recognition.** The Standard was approved in 2017 and last updated in 2021. The CPD process is ensured by PAOs, who are responsible for monitoring the CPD of their member professional accountants and for keeping records. PAOs are required to have internal policies, systems, and procedures which ensure that requirements with respect to CPD of their member certified accountants are met. Recognition of CPD programs and evaluation of their compliance with the regulations is carried out by SARAS. SARAS keeps the register of recognized professional education programs and continuous education programs.

**268. As of the date of this ROSC review, two PAOs were recognized by SARAS and included on the professional education register.** GFPA was recognized for conducting professional certification, examinations, and CPD education and examination for accountants and auditors. GFAAFM was recognized for certification and CPD education for auditors, but not for administering examinations. No university education programs were recognized by SARAS for the purpose of professional accounting education as of December 31, 2022. However, graduates of universities offering education programs with an accounting concentration, were given a waiver for GFPA to provide them with exemptions on the first three (basic) exams of professional certification. The waiver has been renewed annually, as universities have not applied for full recognition.

**269. As of December 31, 2022, there were 62 HEIs registered in Georgia, 20 are state-funded and 42 are private.<sup>207</sup>** They comprise 33 universities, 20 teaching universities, 2 colleges, and 7 HEIs established by the Georgian Orthodox Church. Courses in accountancy and audit are offered by 28 of the HEIs (55 educational programs altogether). Two private universities, Caucasus University and Black Sea International University, offer stand-alone degree programs in accountancy.<sup>208</sup> Accountancy and audit courses are more commonly taught as a part of other higher education degree programs, such as: business administration (40 HEIs), law (18 HEIs), economics (17 HEIs), and finance (18 HEIs). In general, the accountancy profession is taught in the Georgian language, with eight programs taught in English.

**270. At the vocational education level, 32 vocational education providers (out of a total 80) can offer vocational education and training programs on accountancy.** Vocational accountancy programs are offered by 25 colleges and 7 universities (20 public and 12 private institutions). At vocational level, accountancy is taught as a stand-alone discipline. Successful completion of the program confers a fifth level (out of eight) vocational qualification with specialization in accounting, according to the National Qualification Framework.<sup>209</sup>

**271. The curricula for higher education programs, including accountancy, are compliant with general national education standards as confirmed through program accreditation, comprising Georgia's system of external quality assurance and institutional authorization.** Both processes are carried out by the NCEQE, a member of the European Association for Quality Assurance in Higher Education and the European Quality Assurance Register for Higher Education.<sup>210</sup> At the time of this ROSC A&A assessment, a new procedure for the development of occupational and educational standards was being developed. It is planned that the new educational standard for accounting and finance-related programs will be developed in 2024.

<sup>206</sup> Order of the Head of SARAS No. N-13 of August 18, 2017, on the Approval of Continuous Education Standard (<https://matsne.gov.ge/ka/document/view/3782102?publication=4>)

<sup>207</sup> Source: National Center for Educational Quality Enhancement <https://www.eqe.ge/en>

<sup>208</sup> Source: Education Management Information System, EMIS, 2022

<sup>209</sup> <https://eqe.ge/res/20191007105945NQFofGeorgia.pdf>

<sup>210</sup> The National Center for Educational Quality Enhancement <https://www.eqe.ge/en>

**272. At the vocational education level, Georgia has fully switched to modular programs since 2019.** Modular educational programs are based on educational standards, which are based on standards of the profession. Professional duties, tasks, and minimum requirements that must be met within a specific profession are reflected in the professional standards, developed with the involvement of employers.

**273. Individual universities/tertiary-level institutions have autonomy in developing curricula.** According to the Law of Georgia on Higher Education, the state ensures autonomy for HEIs and their main educational units in terms of determining and carrying out academic, financial, economic, and administrative activities independently. Provided that universities meet the general criteria, they are free to set their own rules and procedures for evaluating and revising curricula. In line with recently implemented education reform, new education standards are being developed for HEIs. The standard in the area of accounting and audit, to be introduced in 2024, will be developed with the involvement of HEIs and employers. In addition, NCEQE, responsible for development of education standards, has a memorandum of understanding with SARAS and is a member of the SARAS Committee on Initial and Continuous Professional Development.

**274. Obligatory and elective modules for vocational education and training programs are defined by the educational standard.** Institutions develop programs based on the educational standard and submit them for authorization to the NCEQE. Authorization is valid for six years after which there is a reauthorization procedure. Institutions are expected to make timely updates to their program to take account of any changes made to the applicable standards.

**275. Caucasus University, a private university based in Tbilisi, has been offering degree programs in accountancy for 21 years.** It was established in 2004 on the foundation of the Caucasus School of Business, which was established in 1998 in partnership with Georgia State University (Atlanta, U.S.). Admission to the university is on a competitive basis, considering the results of the unified national exams. The university offers an undergraduate 4-year full-time Bachelor's Program of Business Administration in Accountancy. Each year about 20 students are

enrolled. The program is taught in Georgian and English languages. The textbooks and learning materials are mostly available in Georgian, with part of the textbooks available also in English. At the time of the ROSC A&A assessment the program had 12 teaching staff, two full time and 10 part-time. Since January 1, 2019, the program has been accredited by ACCA for 5 exemptions.

**276. Black Sea International University is a private university offering degrees in accounting and audit for the last eight years.** The university has been engaged in educational and scientific activities since 1995. It is the first English-language educational institution in Georgia offering programs in both English and Georgian languages at all three levels of education. The University offers two undergraduate 4-year full-time bachelor's degree programs: a stand-alone program on accounting and audit and business administration with an accounting concentration. Each year around 50 students are enrolled from around 300 applicants. Approximately 65 percent are female students. The courses are taught in English and Georgian languages. The textbooks and learning materials are mostly available in Georgian with some in the English language. The accountancy curriculum is subject to review on a yearly basis. There are two full-time and nine part-time teaching staff involved in the accountancy programs, two are international staff. The majority of graduates are employed by local and international network audit and assurance companies. About 20 percent are employed by employers in the non-financial sector and SMEs, followed by non-governmental and public sector organizations, financial sector, and academia. Both programs are accredited for three exemptions from the first level of the GFPAA professional qualification, which is outlined in detail in para 285.

**277. Ivane Javakishvili Tbilisi State University offers business administration programs with accounting concentration.** The first national university in the Caucasus, opened in Georgia in 1918, it is the oldest and the biggest university in the country, with approximately 22,000 students studying in seven faculties. Accounting has been taught for more than 90 years. Currently, the university doesn't offer a stand-alone degree program on accounting. However, it offers an undergraduate four-year full-time Bachelor's Program of Business Administration and two-year

full-time Master's Program of Business Administration with an accounting concentration. Enrollment in the university, including educational programs of the Faculty of Economics and Business, takes place as a result of unified national exams. Mandatory subjects to be passed for the undergraduate programs in economics include Georgian language, foreign language, and mathematics. Enrollment in the business administration undergraduate program is very competitive. In 2022, the number of places announced for the business administration educational program was 700, while number of applicants was 4,560. About 15 percent of students follow the program with an accounting concentration. The proportion of female students is approximately 60 percent. The main sources of funding of the university include tuition fees, scientific-research grants and income from leases. The courses are taught in Georgian language. The textbooks and learning materials are mostly available in Georgian with some in the English language. Program curricula are reviewed on a yearly basis, or as needed following changes introduced to accounting and audit standards and regulations. At the time of this review there were 13 full-time and 3 part-time staff for the accounting concentration. The university's economic and business administration educational programs are accredited by the GFPAA for exemptions on the first four books of the professional qualification.

**278. Ilia State University offers finance and banking programs with significant accounting content.**

The university was founded in 2006 as a result of the merger of six different academic institutions. Each year around 250 students are enrolled for its bachelor's and master's degrees in finance and banking with significant accounting content. The courses are taught mostly in Georgian and English languages. The textbooks and learning materials are available in Georgian and English languages. The accountancy curriculum is subject to review twice per year. The finance and banking program is accredited for three exemptions from the GFPAA professional qualification.

**279. Batumi Shota Rustaveli State University offers an undergraduate business administration program with an accounting concentration.** The university was founded in 2002, based on educational institutions with an 80-year history. It has been offering accountancy programs for 21 years, however

since 2019 it does not offer a stand-alone degree on accountancy. The main disciplines are taught as part of an undergraduate business administration program with an accounting concentration. Each year around 40 students are enrolled from around 200 applicants. The proportion of male students is approximately 70 percent. The courses are taught in the Georgian language. Textbooks and learning materials are mostly available in Georgian, with some in English and Russian languages. The accountancy curriculum is subject to review on a yearly basis. There are six full-time and four part-time teaching staff involved in the accountancy programs. The majority of graduates are employed by local audit and assurance companies, and by employers in financial sector, followed by non-governmental and public sector organizations, and academia. The business administration program is accredited by GFPAA for exemptions on the first three books of professional qualification.

**280. Georgian Technical University offers an undergraduate business administration program with an accounting concentration.** It is a private university, based in Tbilisi. The business administration bachelor's degree program, which includes an accounting concentration, comprises 11 study courses (55 ECTS credits) and has been implemented since June 2012. Each year around 40-50 students are enrolled for the program. The university is funded from students' tuition fees. The courses are taught in Georgian language. Textbooks and learning materials are mostly available in Georgian. The accountancy curriculum is subject to review once every two to three years. There are six full-time and eight part-time teaching staff involved in the accountancy programs. The business administration program is accredited by GFPAA for exemptions on the first three books of the professional qualification.

**281. The University of Georgia teaches accountancy as part of the business administration program at bachelor and master levels.** Based in Tbilisi, it is one of the largest private universities in the country with more than 6,000 local and international students. The university has accredited programs at bachelor's, master's, and PhD levels in English and Georgian languages. In the bachelor's program students' enrollment is carried out according to the Georgian legislation based on the results of national examination. The university has been offering courses in accountancy for 17 years. Up to 15 students are

enrolled yearly for the business administration program with an accounting concentration. The main financial source of funding of the University of Georgia is the tuition fees paid by students (including grant funding for students enrolled by the state). In 2011, the University of Georgia received significant funding from American financial institutions (OPIC). The courses are taught mostly in Georgian and English languages. The textbooks and learning materials are available in Georgian and English languages. The accountancy curriculum is subject to review on a yearly basis. There are three full-time and seven part-time teaching staff involved in the accountancy programs, including three international staff. The majority of the graduates are employed by local audit and assurance companies, and by employers in the financial sector, followed by non-governmental and public sector organizations, and academia.

**282. Sukhumi State University offers a business administration program for bachelor's and master's degrees with an accounting concentration.** Based in Tbilisi, the university has been teaching accounting disciplines since 1978. There is no longer a stand-alone accountancy program, but bachelor and master level business administration programs have an accounting concentration. Around 100 students are enrolled yearly, with 30 students following the accountancy concentration. The courses are taught in English and Georgian languages. The textbooks and learning materials are mostly available in Georgian with some in the English language. The accountancy curriculum is subject to review as needed. There are six full-time teaching staff involved in the accountancy programs. About 30 percent of the graduates are employed in the financial sector, 15 percent in government bodies and other public sector organizations, followed by NGOs (12 percent), non-financial sector (10 percent), and local audit and assurance companies (8 percent). Both programs are accredited for three exemptions from the GFPAA professional qualification.

**283. University teaching, in general, needs more investment to improve the quality of learning materials and instructors' knowledge.** Salaries of lecturers in most universities/tertiary-level institutions in Georgia are non-competitive, particularly in state universities. Lecturers do not always keep up to date with developments in the profession and changes in international standards.

**284. Graduates of Georgian Universities can apply to GFPAA for exemptions.** Following a World Bank recommendation, GFPAA initiated cooperation with universities and the Ministry of Education to strengthen accountancy academic curricula and align university programs with relevant IES. By the time of the ROSC A&A review, GFPAA had signed memoranda of understanding with seven universities, aimed at aligning universities' curricula with GFPAA syllabuses and establishing cooperation in other aspects relating to integration of initial and professional education in the area of accounting and audit. The relevant university programs are accredited for exemptions on the first 3 to 4 exams of the GFPAA professional certification.

**285. Graduates of Georgian universities and students of GFPAA can apply to ACCA for exemptions.** As of December 2022, ACCA has a partner relationship with a number of institutions in Georgia. GFPAA is recognized as a key partner. The Ministry of Finance Academy in Georgia is an approved learning partner in Georgia. There are five approved employers and five accredited programs in the following education institutions: Bachelor of Business Administration in Accounting Program of Caucasus University (5 exemptions), Bachelor of Business Administration (concentration in finance) Program of Free University of Tbilisi (3 exemptions), Bachelor of Business Administration of Finances Program of Business and Technology University (6 exemptions), GFPAA Professional Certification Program (9 exemptions), and GFPAA Chief Accountant Qualification (3 exemptions). To apply for exemptions, students must provide documentary evidence in the form of an official letter confirming which exams have been passed at which dates. For the majority of the universities in Georgia, the maximum exemptions available are the first four exams for an accounting degree. In cases when the university has exemptions at GFPAA they still need to apply for ACCA exemptions separately. It is ACCA policy that exemptions are not awarded on the basis of other exemptions. As of the date of the ROSC review there were 152 ACCA members in Georgia, 810 future members in the process of qualifying, and 48 DipIFR certificate holders.

**286. The international donor community, including the EU and the World Bank, have been supporting the strengthening of accounting education in**

Georgia within a number of regional and in-country technical assistance programs, including the Strengthening Auditing and Reporting in the Countries of Eastern Partnership (STAREP) regional program,<sup>211</sup> the Public Sector Accounting and Reporting Program (PULSAR),<sup>212</sup> and the EU-World Bank joint Georgia Financial Inclusion and Accountability Technical Assistance Project.<sup>213</sup> The National Strategy for the improvement of accounting and auditing education in Georgia was developed in 2018 as part of the STAREP program, aiming to analyze the status of the accounting education in the country and its compliance with the Law on Accounting, Reporting, and Audit, as well as with EU Directives and IES. The key development areas identified included:

- a) promoting better synergy between accounting and auditing education at university and professional levels, aiming to improve the quality of and access to the profession;
- b) enhancing the role of the profession by promoting accounting and auditing education;
- and c) ensuring methodological support necessary to develop accounting and auditing education at university and professional level.

During regional and in-country discussions of the Strategy with key stakeholders it was widely recognized that an efficient accounting and auditing educational system aligned with international good practices contributes to the development of professional skills of accountants and auditors and increases the level of public trust in the quality and utility of the services provided.

**287. A benchmarking analysis in 2019 reviewed syllabuses, teaching, assessment, and governance in tertiary accounting education in Georgia.** Three leading universities offering degrees in accounting, Tbilisi State University, Black Sea International University, and Illia State university, took part in the assessment. The results of the analysis were discussed with key stakeholders involved in accounting education in Georgia, including SARAS, PAOs, and MoE. The results of the assessment were published in 2020 and an action plan for strengthening accounting education was developed. This included four priority areas: a) development of a model curriculum for training accountants aligned with IES and based on internationally recognized

programs and good practices; b) equipping accounting education institutions with high quality and up-to-date textbooks and learning materials in the Georgian language; c) development of unified examination procedures in line with regulatory requirements and good international practices; and d) promotion of universities' learning programs both in country (by the regulator and PAOs) and internationally. Analysis of various options for degree level accounting education curricula concluded that the GFPAA curriculum, used for professional certification and based on the ACCA qualification, is well positioned to be used for this purpose, especially given its recognition by SARAS and the availability of high quality and up-to-date learning materials in the Georgian language.

**288. Cooperation between GFPAA and leading Georgian universities offering accounting degrees is being strengthened, including within memoranda of understanding.** The aim is to promote integration of initial and professional accounting education and further recognition of HEIs' programs by SARAS. More than 1,000 copies of ACCA textbooks, translated into Georgian, were transferred to university signatories of a memorandum of understanding as part of the World Bank STAREP program and the EU-World Bank joint Georgia Financial Inclusion and Accountability Technical Assistance Project.

## 9. Audit Regulation, Quality Assurance, and Public Oversight

### Overview of regulation

**289. The system of audit and auditor regulation, quality assurance, and public oversight in Georgia has been assessed as largely compliant with the EU acquis.** As part of the EU's assessment of Georgia for possible candidate status for EU membership, the statutory framework for audit regulation, including quality assurance and public oversight, was assessed as largely compliant with the EU framework and legal requirements. Some areas for further improvement shared with SARAS, which will address them, included:

<sup>211</sup> <https://cfr.worldbank.org/programs/starep>

<sup>212</sup> <https://cfr.worldbank.org/programs/pulsar>

<sup>213</sup> <https://www.worldbank.org/en/news/press-release/2019/05/24/enhancing-financial-inclusion-and-accountability-in-georgia>

- \* The definition of “key audit partner” should be introduced in law.
- \* Requirements about the disclosure of audit firm’s office locations and about the network should be added to registration requirements.
- \* The mechanism for possible delegation of tasks by SARAS to other bodies should be covered by law.
- \* The definition and the description of the annual transparency report should be introduced in law.

**290. The system of regulation and oversight is well established and effective.** The World Bank has worked closely with SARAS, and its sponsor, the MoF since its establishment in 2016. SARAS has proven to be highly efficient and effective in implementing the requirements of the Law on Accounting, Reporting, and Audit. This includes establishing and operating audit quality assurance, establishing a unique company reporting portal, implementing an effective audit register, developing a microenterprise financial reporting standard, developing a financial reporting enforcement function, setting and enforcing educational requirements for auditors, and significant progress in all other areas.

**291. There were 438 registered auditors, including those working within audit firms, as of December 31, 2022.** There were 368 audit firms (267 firms and 101 sole practitioners) including 29 international network firms. 376 audit partners work within audit firms and 101 of the firms were sole practitioners (39 work as audit partners within audit firms and operate as sole practitioners at the same time). Nine hundred commercial entities were subject to the statutory audit requirement, including banks, listed companies, and others. As noted above, auditors must be certified accountants and meet other criteria including completing practical work experience and holding public indemnity insurance, as defined by the law.

**292. Only certain auditors are allowed to audit PIEs. Approval to audit PIEs is based on SARAS inspection results.** PIE audit approval is given only to a firm (sole practitioner auditors are not given such approval) which has high quality audit engagements and an effective firm-level quality management system. Within the PIE audit firm, approval is given specifically

to an auditor as the engagement partner for a high-quality engagement. Approval of both the firm and the auditor is granted until the next inspection.

**293. There is currently one common register for statutory and non-statutory auditors.** There is no separate register for PIE auditors, but audit firms authorized to audit PIEs can be easily identified by using a filter in the register.

**294. SARAS has plans to change the system from one common register to separate registers for statutory auditors and non-statutory auditors.** The statutory auditor register will still comprise PIE auditor and non-PIE auditor sections.

**295. Some auditors on the register may not provide audit services.** Some practitioners wish to be included on the register to be searchable by potential clients but provide mainly tax, accounting, and advisory services. Under SARAS’ plan to have separate registers for statutory and non-statutory auditors, auditors who do not do audits will be placed in the non-statutory register.

**296. Eighteen auditors had recognized foreign accountancy qualifications.** SARAS can recognize accountancy qualifications and register auditors who are members of organizations that are members of IFAC established in member states of the OECD or EU, after passing qualification tests in Georgian law and tax. SARAS had 18 such auditors on the register.

**297. There is no specified legal form for audit firms to be registered.** Audit firms are not required to be registered as a specific legal form of company, but in practice audit firms are mainly LLCs and individual practitioners. Audit firms are required to hold appropriate professional indemnity insurance for no less than GEL 100,000 for the purpose of compensating for possible material damage caused by the failure of the audit entity to fulfil audit services as required by the law.

**298. The provision of non-audit services and other possible conflicts of interest are regulated by the Law on Accounting, Reporting, and Audit.** As part of the quality assurance of auditors and audit firms, the design and implementation of the

firm's quality management system is assessed, including compliance with independence and ethical requirements. This includes possible conflicts of interest from the provision of non-audit service.

### Quality assurance and audit oversight system

**299.** The Law on Accounting, Reporting, and Audit establishes SARAS as the only agency responsible for the monitoring and quality assurance of audit since 2016. The monitoring includes an assessment of the compliance of the audit firm with the requirements of ISA and ISQM 1 & 2.

**300.** SARAS is a state sub-agency within the system of the MoF (a budgetary organization). As required by the law, SARAS must submit a report on its activities to the Minister of Finance, issue a public report on its activities, and publish information on future plans related to its activities on its website.

**301.** SARAS is a full member of the International Forum of Independent Audit Regulators (IFIAR). SARAS has full rights for voting within IFIAR and participates in IFIAR's Emerging Markets Taskforce Working Group, which provides beneficial opportunities for international collaboration and support.

**302.** SARAS ensures independence from the auditors/audit firms it monitors. The SARAS board and staff are required to be non-practitioners and free from recent association with audit firms. In addition, inspectors who carry out the monitoring of an auditor/audit firm must not, for at least a year, have carried out audit services, held voting rights, been employed as a member of the management body or supervisory board of the audit firm to be inspected, or been otherwise associated with the audit firm.

### Quality assurance review procedures, approach, and communication of findings

**303.** In accordance with the Law on Accounting, Reporting, and Audit, quality assurance inspection of auditors/audit firms is conducted at least once in six

years for all auditors/audit firms, and at least once in three years for auditors/audit firms that conduct audits for PIEs and first category entities. In addition, SARAS implements a risk-based approach to selecting auditors/audit firms to inspect. SARAS aims to inspect at least 30 audit firms each year, including both PIE and non-PIE auditors.

**304.** SARAS conducts audit quality assurance in accordance with an established methodology, which has been developed in cooperation with international peers. An extensive EU-funded twinning project with the Greek audit regulator over a number of years assisted SARAS in developing and refining their audit inspection approach, procedures, and methodology. Cooperation with other audit regulators, including from the UK, New Zealand, Netherlands, Emirate of Dubai, have refined the approach further. The methodology is comprehensive and includes a focus on risk areas such as auditor judgment, group audits, and other high-risk areas.

**305.** The audit quality assurance results in one of 6 grading categories. SARAS presents the preliminary results of the inspection within one month after receiving the complete information requested by SARAS regarding the monitoring of a quality control system. The final results of the inspection are subsequently communicated to the firm in the quality assurance monitoring report. Audit firms are required to present a remediation plan to SARAS including dates when remediation procedures will be implemented. SARAS monitors whether the objectives of the remediation plan are achieved in a subsequent visit.

**306.** SARAS does not currently engage with audit committees or other bodies charged with governance within audit clients to discuss review findings. However, SARAS has started to conduct activities to promote the effective functioning of audit committees with the support of the World Bank, within the Georgia Financial Inclusion and Accountability Project with the EU.

**307.** SARAS is required by law to publish the results of individual auditor/audit firm monitoring on the audit register. In addition, it must publish a general report on the condition of audit quality on an annual

basis. However, EU law requires audit oversight bodies to publish more information than is yet included in the Georgian law, including the annual work program and activity report and aggregated information on the findings and conclusions of inspections. SARAS reports on most of these areas annually. As noted above in paragraph 289, SARAS could consider amending the law to make all the reporting areas listed in the EU respective requirement be required specifically in the law.

### Quality Assurance Inspectors

**308. SARAS currently has 5 inspectors in the audit quality assurance (QA) team.** Inspectors are required to have higher education in economics or business administration and at least two years of work experience in accounting, reporting, and/or auditing (in accordance with audit or international standards). Inspectors are appointed on a competitive basis and inspectors are compensated reflecting their professional level of competence. Inspectors undergo appropriate professional development and an annual evaluation process.

**309. SARAS takes measures to ensure that inspectors are independent of the profession and of the subject of their inspection.** Inspectors are required to sign an independence declaration at the beginning of each inspection.

**310. Upskilling of existing staff resources is an ongoing challenge for SARAS.** Technical updates and other training of inspection staff and others involved in the quality assurance process is provided by SARAS to staff on an ongoing basis, sometimes with donor support. This upskilling should cover changes in relevant financial reporting, auditing, and quality management standards; evolutions in best practices and peer developments in audit inspection methodologies and approaches; legislative developments, and any other relevant areas. Sustainable financing of future updates and training should be secured going forward.

**311. SARAS also needs to address other operational challenges such as in obtaining specialized software for audit inspection management and ensuring that inspection staff are not required to perform non-inspection activities in addition to their inspection duties.**

### Investigations and sanctions

**312. Auditors and audit firms must be registered in the SARAS register of auditors.**<sup>214</sup> Auditors who receive the lowest scores in quality assurance inspections can face sanctions including the annulment of their registration or prohibition from signing audit reports. Where auditors or audit firms receive grades 2-5 (where 5 is a low score), SARAS has the authority to request that they involve additional specialists in current audit engagements. Auditors who receive ratings of 4 or 5 may not audit PIEs, first, and second category companies. Courses of CPD to address deficiencies can also be required. In addition, SARAS can impose monetary sanction up to GEL 5,000.

### Performance Indicators – Audit Public Oversight

**313. The overall rating attributed to Georgia under the performance indicator “Audit Public Oversight”, is 3.9 out of 4, which equals the simple mean of the rating criteria comprising sub-indicators A, B and C below.**

*Sub-indicator A. Audit oversight system.*

**314. The attributed rating based on the legal requirements is 3.8, which equals the simple mean of the rating criteria comprising sub-indicators A.1-A.4 below (i.e.,  $3.8=(4+4+3+4)/4$ .)**

<sup>214</sup> The register is at <https://www.saras.gov.ge/en/Auditors>



### A.1. Membership of the audit oversight authority governing body

Georgia Rating	4	The SARAS board comprises 7 members nominated by other regulators and institutions. Practitioners are not allowed to be present, with a suitable cooling-off period required.
	1	Criteria for '2' rating not met.
Rating Criteria	2	Membership comprises representatives of the profession or the majority (more than 50 percent) are practitioners.
	3	Membership comprises a majority (more than 50 percent) of non-practitioners and a minority of practitioners.
	4	Membership comprises only non-practitioners, who are independent from the profession, according to IFIAR Core Principle 2.

### A.2. Scope of the audit oversight system

Georgia Rating	4	SARAS is established by legislation that is mostly in compliance with the EU legislative requirements for audit oversight. Accordingly, SARAS has oversight of (i) the approval and registration of auditors and audit firms; (ii) the adoption of standards on professional ethics and internal quality control of audit firms and auditors; (iii) continuing professional education, (iv) the quality assurance system; and (v) the investigative and administrative disciplinary systems for auditors.
	1	Criteria for '2' rating not met.
Rating Criteria	2	The audit oversight authority has oversight of: (i) the approval and registration of auditors and audit firms; (ii) the adoption of standards on professional ethics and internal quality control of audit firms and auditors; and (iii) continuing professional education.
	3	In addition to requirements under "2": The audit oversight authority oversees the quality assurance system.
	4	In addition to requirements under "3": The audit oversight authority oversees the investigative and administrative disciplinary systems.

### A.3. Funding of the audit oversight system

Georgia Rating	3	SARAS is funded by the government through the MoF. Its funding is generally adequate for its current operations. However, SARAS continues to benefit from donor support for training initiatives and other developments – sustainable funding for such training going forward should be ensured.
	1	Criteria for '2' rating not met.
Rating Criteria	2	Current funding levels are not sufficient to cover the audit oversight authority's core activities.
	3	Current funding levels are sufficient to cover the audit oversight authority's core activities, but concerns exist as to sustainability.
	4	Current funding levels are sufficient to cover the audit oversight authority's core activities and are sustainable. Funding is secured and free from undue influence by auditors.

#### A.4. Reporting by audit oversight authority

Georgia Rating	<b>4</b>	SARAS reports both to the MoF and publicly on an annual basis covering the results of inspections, its activities, and its future work plan. SARAS follows the IFIAR Core Principles as a member of IFIAR. To achieve full compliance with the relevant requirements of the EU audit regulation, the definition and description of the annual transparency report should be included in law.
Rating Criteria	1	Criteria for '2' rating not met.
	2	There are no legal obligations to publish annual work plans, activity reports, or outcome of inspections at the aggregate level or on a firm-by-firm basis.
	3	Legal requirements are in place to prepare and publish annual work plans and summary reports of annual activities within a specified timeframe.
	4	Annual work plans, activity reports, and the outcome of inspections (at the aggregate level or on a firm-by-firm basis) are published annually in accordance with legal requirements and following IFIAR Core Principle 3.

Sub-indicator B. Audit quality assurance.

315. The attributed rating based on the legal requirement is 4.0, which equals the simple mean of the rating criteria comprising sub-indicators B.1-B.4 below (i.e.,  $4.0 = (4+4+4+4)/4$ ).

#### B.1. Legal mandate for audit quality assurance inspections

Georgia Rating	<b>4</b>	SARAS has performed a full cycle of inspections of auditors of PIEs and has begun a third cycle. Its inspection function is independent of the accountancy profession and the Law on Accounting, Reporting, and Audit gives SARAS the necessary legal mandate and authority to perform this role.
Rating Criteria	1	Criteria for "2" rating not met.
	2	There is a requirement for the work of auditors to be subject to inspection for adherence to quality standards.
	3	Inspections for adherence to quality standards by auditors are required to be performed by a separate body which acts in the public interest.
	4	Inspections for adherence to quality standards by auditors of PIEs are performed by a body independent from the accountancy profession with the legal mandate and authority to perform this oversight role.

#### B.2 Requirements for audit quality assurance inspectors

Georgia Rating	<b>4</b>	Inspectors must have relevant experience and be independent both at recruitment and for each inspection. Training is provided to inspectors annually and on an ongoing basis. SARAS inspectors participate in the annual IFIAR Inspection Workshop where inspectors worldwide share their latest developments and concerns relating to inspection.
----------------	----------	--

### B.2 Requirements for audit quality assurance inspectors

Rating Criteria	1	Criteria for "2" rating not met.
	2	QA inspectors are required to have professional experience in auditing and financial reporting.
	3	QA inspectors are required to be independent of the auditor under review and free of conflict of interest.
	4	Inspectors of auditors of PIEs are required to undertake continuing professional development and specialized training on quality assurance and in other relevant areas based on the nature and complexity of PIEs in the jurisdiction, including industry specialized knowledge.

### B.3 Frequency of audit quality assurance inspections

Georgia Rating	4	SARAS operates both a cycle-based and risk-based approach to selection of auditors for inspection, in line with best practice. The cycle is three years for PIE auditors and six years for non-PIE auditors, in line with EU requirements. All active auditors are visited within this cycle. SARAS is starting its third cycle for PIE auditors.
Rating Criteria	1	Criteria for "2" rating not met.
	2	Auditors are selected for inspection according to a minimum cycle of at least once every 6 years.
	3	The minimum cycle for inspection of auditors of PIEs is at least once every 3 years.
	4	The QA body also takes into consideration risk-based criteria when determining which auditors to select for inspection.

### B.4 Audit quality assurance inspection procedures and findings

Georgia Rating	4	<p>The results of QA inspections are reviewed internally by SARAS management and in summary by the SARAS board. Any disputes with the subjects of review relating to the inspection results can be referred to a dispute resolution process implemented by the board.</p> <p>Part of the inspection process is to discuss with and agree a remediation plan with the auditor/audit firm which address the findings of the review. This plan is followed up in the subsequent inspection.</p>
Rating Criteria	1	Criteria for "2" rating not met.
	2	<p>QA inspection procedures are performed according to a defined methodology. Inspection procedures include on-site review of firm-wide procedures for compliance with legal, ethical, and professional standards.</p> <p>QA inspection findings are shared with the auditor in a written report.</p>
	3	<p>In addition to requirements under "2":</p> <p>QA activities also include on-site inspection of selected audit files and working papers, for compliance with legal, ethical, and professional standards.</p> <p>QA reporting procedures include circulation of a draft inspection report to the auditor for comment and action plans to address the findings prior to issuance of a final report.</p>
	4	<p>In addition to requirements under "3":</p> <p>QA inspection procedures and outcomes of reviews are also subject to internal quality control within the QA body to promote high quality and consistency in performing inspections.</p> <p>QA reporting procedures includes follow up on the status of remediation of the findings that the auditor has committed to address.</p>

Sub-indicator C. Investigations and sanctions.

316. The attributable rating based on the legal requirements is 4.

C.1. Audit quality investigations and sanctions	
Georgia Rating	4 SARAS has a range of sanctions available in addition to publicizing the visit grading result. This publicity is an effective sanction in its own right. In addition, sanctions ranging from imposing CPD to exclusion from the audit register are available to SARAS.
Rating Criteria	1 Criteria for "2" rating not met.
	2 Some investigations <b>and</b> sanctions exist but these are not effective and rarely applied in practice.
	3 Investigation systems target non-compliance, but sanctions are not commensurate with the severity of non-compliance.
	4 Effective systems of investigation and sanctioning are in place and sanctions are commensurate with the severity of non-compliance.  Mechanisms to receive information anonymously (including from the public) regarding non-compliant actions taken by auditors of PIEs are in place. Such information can trigger an investigation.

## 10. Setting Accounting and Auditing Standards

### Financial Reporting Standards

317. The Law on Accounting, Reporting, and Audit mandates the use of international financial reporting standards for financial statement preparation (IFRS or the IFRS for SMEs), other than for microenterprises, and international auditing and quality management standards for audits (ISA, ISQCM1 &2). As such, SARAS is not a standard setter other than for microenterprises as set out below. It is responsible for legally adopting revision to the international standards. These international standards are set outside of Georgia; updates are translated and adopted by SARAS in a short period following issue by the relevant international standards setting organizations.

318. SARAS adopts the latest version of IFRS/the IFRS for SMEs. At the time of this report, SARAS had adopted the latest updated version of IFRS in May 2023 without any changes. SARAS is responsible

for translation of IFRS and the IFRS for SMEs into the Georgian language. There is a SARAS Review Committee that reviews the translations.

319. SARAS has adopted the latest version of the IFRS for SMEs. It was translated, reviewed by the same Review Committee as IFRS standards and adopted by the order of the head of SARAS. According to the process set out in the Law on Accounting, Reporting, and Audit, members of the Review Committee are appointed by the Head of SARAS and include experts in the field, representatives of professional organizations, practitioners, and other stakeholders.

320. SARAS develops and publishes a financial reporting standard for microenterprises (national GAAP). This standard was developed in 2018 by a group of experts, both local (including SARAS) and international. The draft standard was publicly available for 6 months on the SARAS website and open for comments. Learning materials were also developed with donor support for microenterprises. The Standard was developed with a view to improving micro entities access to finance, thereby fostering investment and leading to economic growth. To

enable this outcome, the Standard was developed on the basis of international good practice tailored to the Georgian context. Moreover, it is accompanied by bespoke, non-mandatory self-learning material. It is envisaged that over time, micro entities financial information on the basis of the Standard will provide useful information to Georgia's credit rating agencies to rate micro entities more accurately, and that improved credit risk information will enable banks to better price loans to micro entities. This should also result in a lower cost of borrowing for micro-entities.

**321. SARAS supports the implementation of the microenterprise standard.** Self-learning materials were developed with the help of donor organizations to ease the burden of compliance for microenterprises. In addition, there is an interpretations committee within SARAS for the microenterprises financial reporting standard. As with the translation review committee, in accordance with the law, members of the interpretation committee are appointed by the Head of SARAS and the committee contains experts in the field, representatives of PAOs, practitioners, and other stakeholders.

## Auditing Standards

**322. SARAS adopted the 2020 edition of ISA issued on September 14, 2021.** These were translated and adopted in May 2022. The standards translated into the Georgian language are published on the SARAS website and are available for all interested parties.

**323. Amendments to ISA and ISQM1 and 2 are adopted according to the process implemented by SARAS.** A translation and reproduction agreement with IFAC is signed and, in accordance with the agreement, the ISA/ISQM standards amendments are translated by translators employed by SARAS. SARAS' review committee performs a technical review of the translation. Following the consideration of review comments, the final approval is provided by the review committee. The final draft of the translation is provided to IFAC for pre-publication review. Following this, the adoption decree for the new amended ISA/ISQCM is signed by the head of SARAS.

**324. The copyright for the auditing standards belongs to IFAC.** There can be delays in obtaining agreement from the government for SARAS to sign a copyright agreement with IFAC for use of updated versions of the standards.

**325. SARAS has participated in the process of amending the IFRS for SMEs.** With the help of the World Bank, consolidated comments of Georgia, Armenia, and Ukraine on the proposed amendments to the IFRS for SMEs were submitted to IASB.

## C. Observed Financial Reporting Practices and Perceptions

**326. The observed financial reporting practices suggest that gaps exist between the applicable legislative requirements and actual practice.** Non-compliance with applicable financial reporting standards and filing requirements were identified, ultimately leading to limited availability of financial information in the market to support economic decision making. However, it is noteworthy that bank and, to a lesser extent, insurance financial statements reviewed were generally assessed to have complied with most aspects of IFRS accounting standards. Significant non-compliance was observed in all other sectors. The financial statements of entities that are subject to regulation by multiple regulators were generally found to be of a higher quality than those that are subject to regulation by SARAS only.<sup>215</sup> The compliance gap is an indication that further capacity strengthening is needed for institutions responsible for audit oversight and for enforcement of financial reporting practices.

**327. The ROSC A&A process included reviews of financial statements and regulators' reports<sup>216</sup> and discussions with stakeholders.** The objectives of this section are to: (a) corroborate the findings from the assessments of A&A standards (**Section II.A**) and the institutional framework for corporate financial

<sup>215</sup> For example, both sets of IFRS financial statements reviewed of entities that are neither listed on the GSE nor subject to regulation by NBG or ISSSG are fundamentally deficient—one of these companies lodged only summary financial statements on the SARAS portal and the other company lodged financial statements prepared using an older (outdated) version of IFRS Accounting Standards.

<sup>216</sup> NBG Annual Report 2020, Insurance Supervisor Annual Report 2021, and SARAS non-compliances identified as a result of reviewing financial statements (second edition).

reporting (**Section II.B**) with reference to financial statements issued and reports from the regulators, where they are available; and (b) gather perceptions on the demand for and quality of financial information from users of financial statements. In the published anonymized results of its risk-based financial statement compliance reviews, SARAS identifies relatively high levels of non-compliance with IFRS 7 *Financial Instruments: Disclosure* and IAS 1 *Presentation of Financial Statements* and, to a lesser extent, non-compliance with other IFRS accounting standards.<sup>217</sup> SARAS's findings are generally consistent with both the results of the compliance reviews of financial statements performed as part of this ROSC A&A and discussions held with users of financial statements and auditors. SARAS also publishes general information in the form of summary anonymized results of its monitoring of audit quality of audit firms/auditors and quality control system that SARAS conducted either fully or thematically.<sup>218</sup>

## Financial Statements Review

**328. Limited reviews of financial statements were performed to assess the compliance gap and the quality of financial information available in the market.** The ROSC A&A team reviewed a sample of consolidated AFSS' of December 31, 2020,<sup>219</sup> to assess the extent to which they complied with the financial reporting framework they purport to be prepared in compliance with — IFRS or the IFRS for SMEs. Conclusions should be treated with a degree of caution; given the limited sample size and inherent problems in examining the compliance gap, the reviewer of financial statements cannot be certain that everything that should have been disclosed has indeed been disclosed. Furthermore, financial statements of entities in similar economic sectors could reasonably be expected to have similar formats and disclosures and therefore it is relatively easy for those preparing financial statements to make them appear to comply simply by conforming to a typical format without regard to the entity's underlying

financial transactions and position.

**329. A total of 22 sets of financial statements were reviewed, of which 19 were prepared using IFRS and three prepared using the IFRS for SMEs.** The sectors and types of entities were selected based on their importance to the national economy:

- \* seven financial institutions—four banks all with equity or debt, or both, listed on GSE; and three MFIs;
- \* three insurance companies, one with equity and debt listed on GSE;
- \* two non-financial institutions with equity listed on GSE;
- \* two non-financial institutions with debt listed on GSE;
- \* two non-financial institutions with neither equity nor debt listed on GSE;
- \* three SOEs; and
- \* three non-financial institutions with neither equity nor debt listed on GSE using the IFRS for SMEs.<sup>220</sup>

**330. In terms of economic significance for the country, the sample of 19 IFRS financial statements reviewed included:**

- \* Nearly all companies with equity listed on GSE (i.e., the only company with an A listing; two of the three companies with B listings; and two of the three companies admitted for trading on the GSE);
- \* About a third of the institutions other than international and regional development banks with debt listed on GSE (i.e. the sample includes two banks and two non-financial institutions);
- \* The two biggest banks that dominate the Georgian banking sector and a further five FIs—two of the 12 smaller banks and three of the 37 MFIs;<sup>221</sup>
- \* Three of the 16 major SOEs;<sup>222</sup> and
- \* Three of the 18 insurance companies.

<sup>217</sup> <https://saras.gov.ge/en/News/Detail/2546>

<sup>218</sup> [https://www.saras.gov.ge/Content/files/Annual\\_Report\\_2021\\_%e1%83%93%e1%83%90%e1%83%a1%e1%83%a0%e1%83%a3%e1%83%9a%e1%83%94%e1%83%91%e1%83%a3%e1%83%9a%e1%83%98\\_ENG.pdf](https://www.saras.gov.ge/Content/files/Annual_Report_2021_%e1%83%93%e1%83%90%e1%83%a1%e1%83%a0%e1%83%a3%e1%83%9a%e1%83%94%e1%83%91%e1%83%a3%e1%83%9a%e1%83%98_ENG.pdf)

<sup>219</sup> The 2020 AFS were reviewed because the compliance review commenced before the deadline for filing 2021 financial statements on the SARAS portal (1 October 2022).

<sup>220</sup> For the year ended December 31, 2020, 4,892 entities filed IFRS for SMEs financial statements on the SARAS portal.

<sup>221</sup> The only credit union was not included in the sample.

<sup>222</sup> None of the other 330 smaller SOEs are included in the sample.

## Pervasive IFRS non-compliance issues across all industries

### 331. There were examples of good practice.

However, outside of the banking and insurance sector, the overall quality of financial reporting needs improvement due to likely non-compliance with IFRS and the IFRS for SMEs identified in several areas across all other sectors reviewed. Five of the audit reports (28 percent) on IFRS financial statements reviewed were qualified.<sup>223</sup> Unmodified audit reports could suggest the attainment of at least the minimum level of compliance with the standards, assuming that audits were adequately performed. The review of the sample of financial statements from all non-bank sectors and across all ownership structures revealed some instances of questionable financial reporting practices, and some cases of probable non-compliance with IFRS and the IFRS for SMEs. The issues identified impact on the quality of financial information presented and disclosures, ultimately leading to less reliable information being available for decision making and accountability of those charged with governance.

### 332. Pervasive IFRS non-compliance issues observed across most industries included:

\* **Basis of preparation:** While companies claim compliance with IFRS we observed that, contrary to the requirements: (i) a company filed only summary IFRS consolidated financial statements on the SARAS portal; (ii) another company used an older version of IFRS; (iii) some companies did not apply some aspects<sup>224</sup> of recent new IFRS; and (iv) auditors issued qualified audit reports on some companies' financial statements for non-compliance with multiple IFRS standards. This non-compliance denies external resource providers the information they need to make their own projections of the reporting entity's future cash flows and to assess the stewardship of management.

\* **Financial statement presentation:**<sup>225</sup>

Management generally appeared to have considered some aspects of materiality. However, the organization and flow of financial statements was sometimes very difficult to follow with redundant, immaterial, or irrelevant information disclosed with boilerplate disclosures. Both omissions and cluttering deny external resource providers the entity-specific information that IFRS specify disclosure of, consequently inhibiting their abilities to make their own projections of the reporting entity's future cash flows and to hold management to account.

\* **Disclosure of significant judgments made in applying accounting policies:**<sup>226</sup>

Some entities omitted these disclosures in their entirety. Other entities identified seemingly insignificant judgments while omitting seemingly significant judgments. Some entities disclosed boilerplate information about the significant judgments they identified, thus denying external resource providers the entity-specific information about significant judgments they need to inform their resource allocation decisions and to hold management to account.

\* **Disclosure of key measurement assumptions:**<sup>227</sup>

Some entities omitted these disclosures in their entirety. Other entities appear to have omitted some key measurement assumptions from these disclosures.<sup>228</sup> Where key measurement assumption disclosures were made, boilerplate information was typically provided rather than quantified entity-specific explanations of the assumptions made and information about the sensitivity of estimates to changes in assumptions, the range of reasonably possible outcomes, and changes made to past assumptions during the year. Consequently, external resource providers are denied the fuller understanding of management's key measurement assumptions that are required to inform their resource allocation decisions and to hold management to account.

<sup>223</sup> None of the three sets of IFRS for SMEs financial statements reviewed purported to have been audited.

<sup>224</sup> For example, some entities continued to test their financial assets for impairment using IAS 39's incurred credit loss model after it was replaced by IFRS 9's expected credit loss model.

<sup>225</sup> IAS 1 *Financial Statement Presentation*.

<sup>226</sup> Paragraphs 122-124 of IAS 1.

<sup>227</sup> Paragraphs 125-129 of IAS 1.

<sup>228</sup> For example, some items identified by the external auditors as key audit matters because of the inherent significant estimation uncertainty.

**\* Disclosure of events after the reporting period:**<sup>229</sup>

Despite significantly evolving geopolitical tensions and socio-economic issues (for example, the COVID-19 pandemic effects on domestic, regional, and international economies), during the post-balance sheet period, some entities disclosed no significant events after the end of the reporting period. Other entities provided only boilerplate disclosures. Consequently, external resource providers are denied the entity-specific decision-useful information that is required about the nature and the effects of material post-balance sheet events.

**\* Related party disclosures:**<sup>230</sup> Some companies appeared to have omitted all related party disclosures from their financial statements. The companies that made disclosures about their material related party relationships generally provided insufficient information to explain the nature of the relationships, how the risk exposures were managed,<sup>231</sup> and whether and to what extent transactions were at arms-length.<sup>232</sup> Some related party transactions attracted audit qualification. Others appeared confusing, possibly contradictory. External resource providers are denied a fuller understanding of the risks and obligations the entity assumes. This is particularly the case for related party transactions where considerations other than commercial might drive the decision-making processes. An understanding of the risks and obligations the entity assumes is required to inform resource allocation decisions and to hold management to account.

**\* Fair value measurement:** Deficiencies observed include: (i) omitting disclosures about the fair value of investment property, revalued property, plant and equipment, and financial instruments; (ii) likely inappropriately concluding that fair value approximates carrying amount for most, if not all, of the entity's financial instruments; and (iii) inadequate disclosures, including inappropriately concluding on the level of the fair value

measurement hierarchy, or omitting disclosing such levels.<sup>233</sup> Incomplete fair value measurement disclosures potentially detract from users' abilities to make informed resource allocation decisions and to hold management to account.

**\* Liquidity risk disclosures:**<sup>234</sup> Most entities provided only boilerplate disclosures about how they manage liquidity risk and the nature and extent of the liquidity risk to which the entities are exposed. Improvements could be made by: (i) being entity-specific in explaining how liquidity risk is managed; (ii) using more appropriate time bands; (iii) including all relevant on-balance sheet and off-balance sheet items; (iv) preparing maturity analysis using undiscounted cash flows; and (v) allocating liabilities to the earliest period in which the entity can be required to pay. Consequently, external resource providers are denied access to entity-specific information relevant to informing their investing and lending decisions about exposure to and the management of liquidity risk.

**\* Market risk disclosures:**<sup>235</sup> Some entities provided the disclosures only for some of their market risk exposures. For example, providing currency risk disclosures but omitting disclosures about significant interest rate risk exposures. Moreover, most entities provided only boilerplate disclosures about how they manage market risk and there was significant variation in the range identified by different entities as representing the limit of the reasonably possible change in currency exchange rates for 2021. Consequently, external resource providers are denied access to entity-specific information relevant to informing their investing and lending decisions about exposure to and the management of market risk.

**\* Asset impairment testing:** Despite the effects of the pandemic and increased geopolitical uncertainties, some entities appeared not to have performed impairment testing. Likely non-compliance with aspects of the reporting of financial asset and non-financial<sup>236</sup> asset

<sup>229</sup> IAS 10 *Events After the Reporting Period*.

<sup>230</sup> IAS 24 *Related Party Disclosures*.

<sup>231</sup> IFRS 7 does not specify exceptions to financial instruments risk reporting for related party transactions.

<sup>232</sup> Paragraph 17 of IAS 24 requires the disclosure of the nature of related party relationships.

<sup>233</sup> IFRS 13 *Fair Value Measurement* and, when relevant, IFRS 7 *Financial Instruments: Disclosures*.

<sup>234</sup> IFRS 7.

<sup>235</sup> IFRS 7.

<sup>236</sup> IAS 36 *Impairment of Assets*.



impairment testing was observed across all non-bank sectors and across the range<sup>237</sup> of applicable asset impairment models as elaborated on separately for each sector below.

### IFRS compliance issues – Georgian Stock Exchange-listed (debt, equity, or both) companies

#### 333. All GSE-listed banks reviewed generally appeared to have prepared their consolidated annual IFRS financial statements reasonably well.

All bank AFS reviewed likely did comply with most aspects of IFRS. In particular, disclosures on expected credit losses were generally well set out and included sufficient detail.

334. However, all non-bank GSE-listed institutions reviewed likely did not comply with at least some significant aspects of IFRS. Areas of likely non-compliance with IFRS that are pervasive across all industries are set out above. Selected aspects of such likely non-compliance with IFRS that are potentially most relevant to users of financial statements of GSE-listed companies reviewed are expanded on as follows:

\* **The external auditor's report of one equity insurer's financial statements was qualified in respect of four matters.** One qualification matter is a legacy issue related to pre-1993 inventories. However, the other three qualification matters related to the application of IFRS to transactions or events that occurred in 2020: (i) measuring the fair value of fixed assets transferred to a joint venture related party in 2020; (ii) defective accounting (i.e. recognition and measurement) for government grants received in 2020; and (iii) omitting disclosures of the fair value of investment property at December 31 2020. Moreover, the reviewer found further likely deficiencies in this company's audited consolidated AFS. These deficiencies significantly detract from the users'

ability to use that financial information as inputs to inform resource allocation decisions and to hold management to account.

\* **Related party disclosures:**<sup>238</sup> Disclosures about material related party relationships generally provided insufficient information to explain the nature of the relationships, how the risk exposures were managed,<sup>239</sup> and whether and to what extent transactions were at arms-length.<sup>240</sup> Some related party disclosures appeared confusing, possibly contradictory. One company's related party transactions attracted audit qualification and its related party disclosures seem irreconcilable with related information provided elsewhere in the financial statements. Another company explicitly stated it has 'no controlling party' but disclosed 'under common control' related party transactions. Other related party transaction disclosures without adequate explanation included disclosing cost of sales but no sales and a gain on sale of investment property carried at fair value. One company's management identified that significant judgment is involved in its determination that its related party transactions were conducted on market terms. However, it provided little disclosure to help users of its financial statements understand the judgments made. External resource providers are denied a fuller understanding of the risks and obligations the entity assumes. This is particularly the case for related party transactions where considerations other than commercial might drive the decision-making processes. An understanding of the risks and obligations the entity assumes is required to inform resource allocation decisions and to hold management to account.

\* **Incomplete disclosures of impairment of non-financial assets possibly impact the presentation of financial position.**<sup>241</sup> Despite external auditors identifying it as a key audit matter and management identifying it as involving key measurement assumptions, inadequate disclosures and possible inconsistencies with the underlying economics were observed.

<sup>237</sup> For example, for financial asset impairment testing: (i) most insurance companies reviewed applied IAS 39 *Financial Instruments: Recognition and Measurement*; (ii) financial institutions reviewed applied the general model specified in IFRS 9 *Financial Instruments*; (iii) most other entities used alternative methods under IFRS 9 that are not available to financial institutions; and (iv) the entities using the IFRS for SMEs applied Section 11 of the IFRS for SMEs.

<sup>238</sup> IAS 24.

<sup>239</sup> IFRS 7 does not specify exceptions to financial instruments risk reporting for related party transactions.

<sup>240</sup> Paragraph 17 of IAS 24 requires the disclosure of the nature of related party relationships.

<sup>241</sup> IAS 36 *Impairment of Assets*.

- \* **Possibly deficient financial asset impairment testing and incomplete credit risk disclosures potentially deny users a proper understanding of credit risk exposures and how credit risk is managed.**<sup>242</sup> Despite being identified as involving key measurement assumptions, inadequate disclosures and possible inconsistencies with the underlying economics were observed. Most entities reviewed appeared to ignore the expected credit losses potentially present in financial assets other than trade receivables. Some also appeared to underapply the simplified expected credit losses model to their trade receivables. Moreover, all entities reviewed provided insufficient entity-specific disclosures about their application of the expected credit losses model and some entities inappropriately claimed to have no significant concentrations of credit risk.
- \* **Fair value measurement is the most commonly cited key source of estimation uncertainty identified by the companies reviewed.** However, none of the companies reviewed satisfied the disclosure requirements triggered by such identification. In particular, companies typically disclosed boilerplate information rather than quantified entity-specific explanations of the assumptions made and information about the sensitivity of estimates to changes in assumptions, the range of reasonably possible outcomes, and changes made to past assumptions during the year. Other deficiencies observed include: (i) omitting disclosures about the fair value of investment property, revalued property, plant and equipment, financial instruments, and particular related party transactions; (ii) likely inappropriately concluding that fair value approximates carrying amount for most, if not all, of the entity's financial instruments; and (iii) inadequate disclosures, including inappropriately concluding on the level of the fair value measurement hierarchy or omitting disclosing that level.<sup>243</sup> Incomplete fair value measurement disclosures potentially detract from users' abilities to make informed resource allocation decisions and to hold management to account.

335. Other IFRS non-compliance issues observed that likely detract from users' ability to use that financial information as inputs to inform resource allocation decisions and to hold management to account, include:

- \* **Going concern disclosures.** One company appropriately made comprehensive disclosures about its material going concern uncertainties. However, other companies generally failed to provide sufficient entity specific information about going concern risks in a manner that would enable understanding of the process the entity has followed to evaluate going concern, particularly in the context of the COVID-19 pandemic. For example, one company, inconsistently with identifying going concern as a critical assumption that has a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, made only the boilerplate disclosure "Based on the analysis of the Group's financial position, its historical and current financial performance, availability of the financial resources to the Group and access to additional financial resources, if required, management believes that the Group will continue to carry on its business without significant curtailment of operations for the foreseeable future." Disjointedly, in a separate note about key assumptions about the future the company disclosed, "management has determined that COVID-19 has no material impact on the Group and that the use of the going concern assumption is warranted." Further disjointedly, in a separate note the company disclosed that it is in breach of contractual commitments that could ultimately result in termination of a significant contract "without any reimbursement for incurred expenditures to the Group." Moreover, this company's going concern related disclosures make no reference to the significant adverse post-balance sheet events disclosed elsewhere in its financial statements,<sup>244</sup> and consequently likely did not appropriately disclose information about possible material uncertainties that may cast doubt upon the entity's ability to continue

<sup>242</sup> IFRS 7 and IFRS 9.

<sup>243</sup> IFRS 13 and, when relevant, IFRS 7.

<sup>244</sup> IAS 10 *Events After the Reporting Period*, paragraph 21 requires disclosure of information about the nature and estimated financial effects of non-adjusting events (or a statement that such estimate cannot be made).

as a going concern.<sup>245</sup> Consequently, external resource providers are denied the entity-specific decision-useful information that is required about the nature and the effects of material post-balance sheet events and possibly significant uncertainties about its ability to continue as a going concern.

- \* **Questionable classifications:** Insufficient disclosures supporting some classification judgments deny external resource providers information about the nature and the extent of the entity's resources and obligations which could affect their resource allocation decisions and could be useful in holding management to account. For example, judgments in: (i) distinguishing key sources of estimation uncertainties<sup>246</sup> from other most significant judgments<sup>247</sup> management made in preparing the financial statements; (ii) determining the level of the fair value measurement hierarchy;<sup>248</sup> (iii) differentiating property, plant and equipment<sup>249</sup> from investment property<sup>250</sup> and biological assets in agricultural activity.<sup>251</sup>
- \* **Unrecognized assets and liabilities:**<sup>252</sup> Some entities appeared to have not recognized in their balance sheets some present rights and obligations that likely satisfied the relevant recognition criteria. One company's defective government grant accounting attracted audit qualification. Another company, contrary to IAS 37, inappropriately cited the "seriously prejudicial" disclosure exemption<sup>253</sup> as a basis for not recognizing a liability. Omitting items from the balance sheet denies external resource providers information about the entity's resources and obligations that they need to inform their resource allocation decisions and to hold management to account.

## IFRS compliance issues – Financial institutions: banks

**336. All banks reviewed appear to be in compliance with most aspects of IFRS.** In particular, disclosures on expected credit losses were generally well set out and included sufficient detail.

**337. Areas of likely non-compliance with IFRS that are pervasive across all industries are set out above.** Of those, the following were particularly relevant to banking entities in the sample:

- \* **Financial statement presentation and disclosure:** In addition to there being some boilerplate disclosures, some balance sheet and income statement items appeared to be inappropriately disaggregated, aggregated, presented, or disclosed.<sup>254</sup>
- \* **Going concern disclosures:** Going concern disclosures were frequently not sufficiently comprehensive and entity specific to understand the process the entity had followed to evaluate going concern, and the entity specific risks arising, particularly in the context of the COVID-19 pandemic.

**338. Some areas of compliance with IFRS are particularly relevant to banks, because of the nature of their business.** Although compliance was generally observed to be good, observations of areas of possible non-compliance include:

- \* **Management report not included in the versions of financial statements available on banks' websites. Financial statements are required to include a management report.** However, this is a requirement of SARAS and not of NBG. Consequently, these commentaries were

<sup>245</sup> IAS 1 and IAS 10.

<sup>246</sup> Paragraph 125 of IAS 1.

<sup>247</sup> Paragraph 122 of IAS 1.

<sup>248</sup> IFRS 13.

<sup>249</sup> IAS 16 *Property, Plant and Equipment*.

<sup>250</sup> IAS 40 *Investment Property*.

<sup>251</sup> IAS 41 *Agriculture*.

<sup>252</sup> IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

<sup>253</sup> Paragraph 92 of IAS 37.

<sup>254</sup> IAS 1, paragraph 29 requires separate presentation of each material class of similar items and separate presentation of items of a dissimilar nature or function unless they are immaterial.

not generally included in the financial statements available on banks' own websites. The audit reports note that "Our opinion on the consolidated financial statements does not cover the other information ..... [typically, the Management Report] our responsibility is to read the other information identified above when it becomes available." When the Management Report was available at the time the financial statements are audited, the audit report notes "in connection with our audit of the consolidated and separate financial statements, our responsibility is to read the Management Report and, in doing so, to consider whether the Management Report is materially inconsistent with the consolidated and separate financial statements, or our knowledge obtained in the audit."

- \* **The primary financial statements frequently included immaterial items (see comment in paragraph 332 above).** Items are included on the face of the statement of financial position or statement of financial performance, even though the value was low and the nature non-material (for example accounts receivable of 0.007 percent of total assets in one case). Other items that were considerably more material were only disaggregated in the notes to the financial statements. This risks both cluttering of the primary financial statements and obscuring of material information.
- \* **Deficiencies in disclosures about financial instrument risk management.** Whilst generally useful and entity specific, some likely evidence of boilerplate disclosures was observed in the financial institution financial statements reviewed. While it is anticipated within a small banking sector that entities will have many practices and processes in common, it is none the less likely that some of commonalities represent boilerplate disclosures. Such deficiencies deny external resource providers the required entity specific information needed as inputs to their resource allocation decisions and to hold management to account.
- \* **Related parties:** Most of the companies had material related party relationships and there was substantial quantitative disclosure in the financial statements for these. However, in

general, there was insufficient information to explain the nature of the relationships, how the risk exposures were managed, and whether and to what extent transactions were at arms-length. External resource providers are denied a fuller understanding of the risks and obligations the entity assumes. This is particularly the case for related party transactions because considerations other than commercial may drive the decision-making processes. An understanding is required to inform resource allocation decisions and to hold management to account.

### IFRS compliance issues – Financial institutions: microfinance

339. **Areas of likely non-compliance with IFRS that were pervasive across all industries are set out above.** Many of these deficiencies were observed in the small sample of microfinance financial statements reviewed.

340. **All MFIs' financial statements reviewed likely did not comply with some significant aspects of IFRS.**

- \* One MFI reviewed received an audit qualification for using NBG regulatory provisioning rather than applying IFRS 9's expected credit loss model. It also omitted from its financial statements many of the related credit risk disclosures required by IFRS 7 and it omitted particular disclosures from other aspects of its financial risk disclosures. This company also omitted from its disclosures the fair value of its financial instruments.
- \* The other MFI reviewed likely:
  - underapplied the IFRS 9 expected credit loss model;
  - omitted particular disclosures from aspects of their financial risk disclosures, made noncompliant disclosures (for example, using carrying amounts instead of undiscounted amounts for liquidity disclosures), and made boilerplate disclosures about other aspects of their financial risk disclosures;
  - omitted to disclose the fair value of some of their financial assets and financial liabilities and likely incorrectly assumed that the fair value

of many of their financial assets and financial liabilities approximate their carrying amounts; and

- likely incorrectly identified the level of the fair value measurement hierarchy that applied to at least some of their financial instruments.

## IFRS compliance issues – Insurance Companies

**341. Most insurance companies reviewed likely did comply with most aspects of IFRS, however there was significant variation in quality, with the financial statements of one entity being significantly weaker than those of others.** A company included in the review sample received an audit qualification in its 2020 financial statements. The qualification did not relate to IFRS compliance per se, but rather to the inability of the auditors to obtain evidence to support an expense recorded in the reporting period.

**342. Areas of likely non-compliance with IFRS that are pervasive across all industries are set out above.** Of those, the following were particularly relevant to insurance entities in the sample:

- \* **Financial statement presentation and disclosure:** In addition to there being some boilerplate disclosures, some balance sheet and income statement items appeared to be inappropriately disaggregated, aggregated, presented, or disclosed.<sup>255</sup>
- \* **Going concern disclosures.** Going concern disclosures were frequently not sufficiently comprehensive or entity specific to understand the process the entity had followed to evaluate going concern and the entity specific risks arising, particularly in the context of the COVID-19 pandemic.
- \* **Boilerplate information about accounting policies.** Whilst much of the information in the financial statements was useful and entity specific, there were still examples of boilerplate disclosures of accounting policies. These included in isolated circumstances accounting policies in respect of transactions or events the entities did not have.

- \* **Disclosure of key measurement assumptions:** Measurement of insurance liabilities were subject to significant estimation risks, particularly as regards claims experience and persistency. This was particularly the case in emerging markets and underdeveloped insurance markets where there was little historical data to draw on. Disclosures of key measurement assumptions used generic rather than quantified entity-specific explanations of the assumptions made and information about the sensitivity of estimates to changes in assumptions, the range of reasonably possible outcomes, and changes made to past assumptions during the year.<sup>256</sup>

**343. Financial instrument risk management disclosures:** Insurance companies had significant exposure to financial assets and typically were exposed to at least exchange rate risk (for example one entity reviewed earned a third of its income from exchange rate difference, but provided no insight into how exchange rate risks are managed), credit risk (for example an entity had invested 89.5 percent of its total assets with banks, but did not provide information about how the credit and concentration risk was managed), market risk, and liquidity risk. An entity used questionable time bands (two categories, less than one year and more than one year with everything in the former category). The same entity, while maintaining that it had “medium term bank placements” (defined by it as more than one year), nonetheless had no assets in the more than one year category in either the previous or the current period. Some disclosures evidence use of boilerplate language, frequently excluding or providing incomplete insight into how the risks were managed.

**344. Issues with disclosures and application of IFRS Accounting Standards appeared likely in some key areas particularly relevant for the insurance industry, including information about insurance risk, credit risk, liquidity risk, and fair value measurement.** The compliance issues arose in different ways as described below.

- \* **Management report not included in the versions of financial statements available on banks websites.** Financial statements are required

<sup>255</sup> IAS 1, paragraph 29 requires separate presentation of each material class of similar items and separate presentation of items of a dissimilar nature or function unless they are immaterial.

<sup>256</sup> Paragraphs 125-129 of IAS 1 and paragraphs 36 and 37 of IFRS 4 *Insurance Contracts*

to include a management report. However, this is a requirement of SARAS and not of the ISSSG. Consequently, these commentaries are not generally included in the financial statements available on the entity's own websites.

**\* Insurance contract risk management**

**disclosures:** Some insurance risk management disclosures generally excluded descriptions of product specific information, sources of economic and insurance data, and comparisons of actual versus expected. For example, the financial statements of one insurance company did not acknowledge any insurance risk at all, or explain how that risk is managed. Incomplete disclosures about an entity's exposure to and management of insurance risks potentially detract from users' abilities to make informed resource allocation decisions and to hold management to account.

- \* Related Parties:** Most of the companies have material related party relationships, and there was substantial quantitative disclosure in the financial statements for these. However, in general, there was insufficient information to explain the nature of the relationships, how the risk exposures were managed, and whether and to what extent transactions were at arms-length. External resource providers are denied a fuller understanding of the risks and obligations the entity assumes. This is particularly the case for related party transactions where considerations other than commercial may drive the decision-making processes. An understanding is required to inform resource allocation decisions and to hold management to account.

### IFRS compliance issues – State-owned Enterprises

345. All of the SOEs' financial statements reviewed likely did not comply with some significant aspects of IFRS. However, there were signs of improvement.

- \* An SOE included in the review sample received multiple audit qualifications in its 2020 financial statements. The qualifications related to non-compliance with IAS 2 *Inventories*, IAS 16 *Property, Plant and Equipment* and IFRS 9 *Financial Instruments*.**
- \* The other two sets of SOE financial statements reviewed collectively included 13 material prior period error corrections, reflecting deficient past accounting practices and possibly indicating recent improvements in the application of IFRS.**
346. Areas of likely non-compliance with IFRS that are pervasive across all industries are set out above. Of those, the following were particularly prevalent in the sample of SOE financial statements:
- \* Financial statement presentation and disclosure: Cluttering:** lengthy boilerplate accounting policy and risk management disclosures followed by contradictory practices evidenced in the accounting. For example:
- One SOE described the IFRS 9 expected credit loss model over multiple pages but created no loss provision because deeper in its financial statements management likely inappropriately assumed that there was no credit risk in its trade receivables and cash balances at Georgian banks.
  - Another SOE with no recognized goodwill and seemingly immaterial amounts of recognized intangible assets disclosed key estimation uncertainty regarding goodwill and intangible asset impairment testing and in determining the useful life of intangible assets.
  - Another SOE disclosed multiple pages of boilerplate disclosures about changes to IFRS that were yet to become effective and disclosed accounting policies for transactions that it did not appear to enter into.
- \* Disclosure of key measurement assumptions and other judgments:** Some SOEs likely omitted disclosures about particular key sources of estimation uncertainty. Other SOEs seemed to confuse disclosures about key sources of estimation uncertainty with disclosures about other significant judgments in applying accounting policies. Consequently, external resource providers are denied useful information about key sources of estimation uncertainties. Moreover, SOEs' disclosures about key sources of estimation uncertainties typically used generic rather than quantified entity-specific explanations of the assumptions made and information about the

sensitivity of estimates to changes in assumptions, the range of reasonably possible outcomes, and changes made to past assumptions during the year.

- \* **Financial risk disclosures and impairment testing:** All SOEs' financial risk management disclosures likely needed improving. For example, liquidity risk time bands seemed too broad, some used carrying amounts rather than undiscounted amounts, off-balance sheet items were likely omitted, and payments were not necessarily allocated to the earliest time band in which payment could be required. One SOE appeared not to have performed impairment testing of its financial assets despite making lengthy boilerplate disclosures about how it applied the IFRS 9 expected credit loss model. The other SOEs appeared to have materially underapplied the IFRS 9 expected credit loss model.

### IFRS for SMEs compliance issues

**347. The sample of financial statements reviewed prepared in accordance with the IFRS for SMEs is limited to only three of the 4,892 non-financial institutions regulated by SARAS that prepare financial statements using the IFRS for SMEs.**

Consequently, the findings below should be read with caution as they may not represent a majority of the IFRS for SMEs preparers in Georgia.

**348. All three of the financial statements reviewed likely did not comply with some aspects of the IFRS for SMEs.** Two of the sets of financial statements reviewed were evaluated to be presented relatively well. The other set of financial statements reviewed was evaluated to be of significantly lower quality.

**349. Areas of likely non-compliance with the IFRS for SMEs observed in the sample of financial statements reviewed include:**

- \* **Financial statement presentation:**<sup>257</sup> Management generally appeared to have considered some aspects of materiality. However, some material

information was likely omitted from all companies' disclosures; and some immaterial or irrelevant information was disclosed with boilerplate disclosures. Both omissions and cluttering deny external resource providers the entity-specific information that the IFRS for SMEs specifies disclosure of, consequently inhibiting users' abilities to make their own projections of the reporting entity's future cash flows and to hold management to account.

- \* **Disclosure of significant judgments made in applying accounting policies:**<sup>258</sup> These disclosures were omitted in their entirety from all IFRS for SMEs financial statements reviewed, thus denying external resource providers the entity-specific information about significant judgments they need to inform their resource allocation decisions and to hold management to account.
- \* **Disclosure of key sources of estimation uncertainty:**<sup>259</sup> These disclosures were omitted in their entirety from most of the sets of IFRS for SMEs financial statements reviewed. Consequently, external resource providers are denied understanding of management's key measurement assumptions that are required to inform their resource allocation decisions and to hold management to account.
- \* **Disclosure of events after the reporting period:**<sup>260</sup> Despite significantly evolving geopolitical tensions and socio-economic issues (for example, the COVID-19 pandemic effects on domestic, regional, and international economies), during the post-balance sheet period, none of the entities reviewed disclosed any significant events after the end of the reporting period. One entity provided only a boilerplate accounting policy note for post-balance sheet events. Consequently, external resource providers are denied the entity-specific decision-useful information about the nature and the effects of material post-balance sheet events.
- \* **Related party disclosures:**<sup>261</sup> Some companies reviewed appeared to have omitted all related party disclosures from their financial statements. The companies that made disclosures about their

<sup>257</sup> Section 3 *Financial Statement Presentation*.

<sup>258</sup> Paragraph 8.6 of the IFRS for SMEs.

<sup>259</sup> Paragraph 8.7 of the IFRS for SMEs.

<sup>260</sup> Section 32 *Events After the End of the Reporting Period*.

<sup>261</sup> Section 33 *Related Party Disclosures*.

material related party relationships generally provided insufficient information to explain the nature of the relationships and whether and to what extent transactions were at arms-length. External resource providers are denied a fuller understanding of the risks and obligations the entity assumes. This is particularly the case for related party transactions where considerations other than commercial might drive the decision-making processes.<sup>262</sup> An understanding of the risks and obligations the entity assumes is required to inform resource allocation decisions and to hold management to account.

- \* **Financial asset impairment testing:**<sup>263</sup> Despite the effects of the pandemic and increased geopolitical uncertainties,<sup>264</sup> some entities appeared not to have performed impairment testing on their trade receivables. This likely non-compliance leaves primary users questioning the value of the entity's financial assets,<sup>265</sup> and consequently likely impedes users' abilities to make informed resource allocation decisions and to hold management to account.

## Compliance with Auditing Standards

### 350. Five of the audit reports on the 19 sets of IFRS financial statements reviewed were qualified.<sup>266</sup>

An unmodified audit report indicates the attainment of at least a minimum level of compliance with IFRS. Nonetheless, the financial statements needed improvement. During the review of the financial

statements, audit reports were also assessed for anecdotal evidence on the extent to which they complied, in practice, with applicable auditing standards. The same limitations apply in analyzing a relatively small sample of audit reports,<sup>267</sup> and the review comprises only an analysis of the extent to which reports prepared are in compliance with ISA 700<sup>268</sup> and ISA 701<sup>269</sup> and general perceptions drawn from the financial statements themselves.<sup>270</sup>

- \* **Compliance with IFRS:** Based on the review of audit reports, it can be concluded that standards relevant to audit reporting were generally being complied with. However, the issues of compliance with IFRS referred to above suggested that there may have been issues with compliance with auditing standards by auditors. This is particularly, but not only, the case for:
  - Presentation and disclosure issues, including the significant use of boilerplate language and the omission of entity-specific information about the entity's most significant judgments and estimates and with regard to risk management; and
  - Recognition and measurement, including use (or apparent use) of accounting policies that are inconsistent with the requirements of IFRS.
- \* **Audit reports:** On the basis of the review of the external auditor reports on the sample of 19 IFRS financial statements reviewed:
  - Key audit matters were not reported regarding the audit of the financial statements of one company with equity listed on the GSE.<sup>271,272</sup>

<sup>262</sup> Paragraph 33.9 requires the disclosure of the nature of related party relationships as well as information about transactions, balances, and commitments necessary for an understanding of the potential effects of the relationship on the financial statements.

<sup>263</sup> Paragraphs 11.21-11.25 of the IFRS for SMEs.

<sup>264</sup> In particular, paragraph 11.23 suggests that these factors may evidence impairment.

<sup>265</sup> For example, despite revenue decreasing significantly in 2020 an entity recorded a significant increase in year-on-year trade receivables and did not record an impairment loss.

<sup>266</sup> In addition to the five qualified audit reports, one company lodged only summary IFRS consolidated financial statements on the SARAS portal (see above). The external audit report on those summary IFRS consolidated financial statements stated that the summary financial statements are consistent, in all material respects, with the audited consolidated financial statements on which the external auditor issued an unmodified audit opinion.

<sup>267</sup> The review is not akin to a formal audit review and is based only on the evidence included in the financial statements. The reviewer does not examine underlying evidence on the practical application of auditing standards, audit quality, or general challenges facing the audit profession, and does not have access to auditors.

<sup>268</sup> ISA 700 *Forming an Opinion and Reporting on Financial Statements*.

<sup>269</sup> ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*.

<sup>270</sup> It is worth noting that given the standard format of audit reports, it is reasonably easy for preparers of audit reports to make them appear good simply by conforming to the format, regardless of the entity's underlying financial transactions and position.

<sup>271</sup> Although this audit report includes reference to the four audit qualifications (paragraph 15 of ISA 701) it does not identify any key audit matters unrelated to the audit qualifications.

<sup>272</sup> The external audit reports on the financial statements of the other eight companies in the sample with equity or debt listed (or both), or in the process of being listed, on the GSE all included one or more key audit matters.



Deficiencies observed in reported key audit matters included likely omission of some key audit matters (for example, at least some of the most significant judgments and key measurement assumptions disclosed in the financial statements<sup>273</sup> that were not identified as key audit matters). Improvements could generally also be made to the overall quality of the key audit matters, for example, increasing relevance by using fewer boilerplate descriptions and, in particular, by relating the matter more directly to the specific circumstances of the entity and referencing more precisely, if at all, to the note disclosures in the financial statements.

## Perceptions

**351. Stakeholders recognized considerable progress in Georgia corporate financial reporting for all categories of entities.** Group discussions with stakeholders generally confirmed recent improvements in domestic corporate financial reporting and the perceived high-quality of bank financial statements. Significant improvements are attributed to both ends of the “carrot<sup>274</sup> and stick<sup>275</sup>” approach implemented in Georgia. However, they acknowledged that for most entity types there remained much room for improvement in significant areas. In particular, concerns remained about the quality of financial statements (albeit improving) prepared by entities in other sectors. The stakeholders included regulators, lenders, entrepreneurs, audit firms, rating agency, and academia.

**352. Financial statements for PIEs and first, second, and third category enterprises were publicly available through the SARAS reporting portal.** However, some stakeholders expressed concern that the current deadline for filing financial statements

on the SARAS portal (1 October) was too far after the entities’ reporting date. This time lag detracted from the decision-usefulness of the financial information.

**353. Management reports for PIEs and first and second category enterprises are publicly available through the SARAS reporting portal.** Stakeholders generally confirmed recent improvements in the quality of management reports and the perceived high-quality of bank management reports. However, concerns remained about the quality of management reports prepared by entities in other sectors. Moreover, some stakeholders expressed concern that the current deadline for filing management reports of regulated entities were lodged on the SARAS porthole only in October when those regulated companies’ AFS were, as specified in the relevant regulatory framework, publicly available from the companies’ own websites much earlier (variously May 15 or June 1). These disconnects detracted from the decision-usefulness of both the management report and the related financial statements.

**354. The quality of financial statements prepared by banks was perceived to be much higher than the financial statements of other first category enterprises.** Consequently, less reliance was reportedly placed on corporate financial reporting of non-bank entities. The quality of third category financial statements was generally perceived to be rapidly improving but still significantly lower quality than those of first or second category entities. Nevertheless, following recent improvements, some stakeholders are now using third category information (for example, Enterprise Georgia’s monitoring system).

**355. Improvement in the quality of fourth category financial statements would make them more useful.** Most stakeholders viewed the recent requirement for fourth category companies to file financial information on the SARAS portal as a positive development,

<sup>273</sup> In accordance with paragraphs 122 and 125 of IAS 1.

<sup>274</sup> For example, the BARTA award (see [www.worldbank.org/en/news/press-release/2022/03/16/world-bank-and-european-union-announce-launch-of-2022-best-annual-report-and-transparency-award](http://www.worldbank.org/en/news/press-release/2022/03/16/world-bank-and-european-union-announce-launch-of-2022-best-annual-report-and-transparency-award)).

<sup>275</sup> For example, significantly increased monitoring of audit function and financial statement quality, leading to regulatory actions.

but all stakeholders expressed little confidence in the quality of fourth category financial statements. Nevertheless, some stakeholders were already using that information (for example, Enterprise Georgia's monitoring system) and other stakeholders expressed interest in it (for example, CreditInfo). However, the lack of access to all fourth category entities' financial statements significantly impeded its usefulness.<sup>276</sup>

**356. Stakeholders recommended maintaining the strong momentum of improving financial reporting.** Specific recommendations included: (i) strengthening the monitoring and enforcement of accounting and auditing by entities by increasing the number of SARAS technical compliance review staff, providing compliance review training for IFRS and the IFRS for SMEs financial statements, and ensuring suitable policies are in place to enable staff retention; (ii) improving the institutional/legal framework for financial statement compliance issue dispute resolution; (iii) clarifying the financial statement compliance review responsibilities for institutions under dual domestic regulation and improving compliance coordination between dual regulators; (iv) further capacity building to the preparers of IFRS and the IFRS for SMEs financial statements; (v) development of a venture capital market and expanding domestic stock exchanges (broader and deeper trading) to encourage more demand-driven improvements.

<sup>276</sup> Fourth category enterprises select whether financial statements are made publicly available when lodging their financial statements on the SARAS portal each year.





## III. MAIN CHANGES SINCE THE PREVIOUS ROSC A&A ASSESSMENT

357. The main finding of the 2015 ROSC A&A<sup>277</sup> was that a much greater degree of compliance with relevant EU legislation relating to corporate financial reporting, accounting and auditing was needed. In particular, compliance with EU Directive 2013/34/EU on the Annual Financial Statements, Consolidated Financial Statements and Related Reports of Certain Types of Undertakings (Accounting Directive) and EU Directive 2014/56/EU on Statutory Audits of Annual Accounts and Consolidated Accounts (Audit Directive) was needed to meet Georgia's obligations under the EU Association Agreement entered into by Georgia.

The ROSC A&A noted many of the areas where such compliance was weak or lacking.

358. The 2016 Law on Accounting, Reporting, and Audit addressed most of these areas and brought compliance with EU legislation to a high level, with only a few areas of partial compliance noted in the recent assessment by the European Commission.

359. This section summarizes the main changes since the 2015 ROSC A&A. More detailed information about the status of implementation progress on 2015 recommendations is provided in **Annex A**.

<sup>277</sup> ENG: <https://documents1.worldbank.org/curated/en/254551468189259272/pdf/ACS13210-REVISED-Georgia-ROSC-AA-Report-FINAL-092015-Box393232B-PUBLIC-ENGLISH-Dissemination.pdf>  
 GE: <https://documents1.worldbank.org/curated/en/486411468189258787/pdf/ACS13210-GEORGIAN-Box393232B-PUBLIC-Georgia-ROSC-AA-Report-FINAL-092015-Dissemination-GEO.pdf>

## Statutory Framework

360. The 2016 Law on Accounting, Reporting, and Audit made substantive improvements to the statutory framework for corporate reporting in Georgia. As confirmed in detail in the assessment in Annex A, each of the 2015 recommendations in the area of statutory framework was addressed, with some harmonization still needed. The definitions of large/medium/small/micro enterprises have been made consistent across Georgian legislation. The current definitions of entities for corporate reporting purposes are in line with international good practices. There also remain some inconsistencies with the equivalent definitions in the Tax Code. However, the impact on corporate reporting in general is not significant. Areas for further harmonization with the EU requirements include further reduction of the financial reporting requirements for SMEs and country by country reporting by very large multinational companies.

## Professional Education and Training

361. Recommendations were made in the 2015 ROSC relating to professional education and training. However, the two recommendations that have not been fully addressed do not actually relate to professional education and training, but rather to university education that has as a pre-entry role to professional training.

362. The recommendation related to strengthening university curricula and aligning them with professional qualification curricula in Georgia has been mostly addressed. An academic curriculum which would align university programs with professional training and examination requirements of relevant PAOs, GFPAA, and ACCA, was developed in 2021 with the help of donor organizations and endorsed by SARAS.<sup>278</sup> The curriculum is in line with IES. It is available at the SARAS website but has not yet been endorsed by the MoE.

363. Less progress has been made on the recommendation to establish and coordinate minimum acceptable requirements for university level education in accounting and audit. This aimed to ensure such consistent application among universities in Georgia, taking into consideration good international practices and agreed with the MoE. This has been discussed with relevant parties, but progress is still pending. The NCEQE plans to develop minimal standards for accounting and audit education in 2024. In addition, SARAS may consider external initiation of development of the National Standard for Accounting Education, earlier than 2024.

364. Other recommendations relating to professional education and training have been fully addressed.

<sup>278</sup> <https://www.saras.gov.ge/Content/files/sarekomendacio-silabusi.pdf>



## IV. RECOMMENDATIONS

365. This section makes a series of policy and institutional recommendations to help improve the corporate financial reporting framework in Georgia.

### **Regulatory and Institutional Framework**

366. The establishment of SARAS and its progress in implementing the requirements of the law has been a very great achievement and is a credit to all involved. In a dynamic environment, SARAS should and will continue to evolve to address new and ongoing challenges. Among others that will arise, current challenges highlighted by this assessment include:

- \* Enhancing SARAS' capacity and funding to be fully sustainable and independent of external donor support, to address operational challenges such as: ongoing training of all staff to update them on relevant developments and best practices in areas related to their work; obtaining specialized software for audit inspection management; and ensuring that inspection staff are not required to perform non-inspection activities in addition to their inspection duties, etc.
- \* Addressing SARAS' ability to attract and retain staff and consultants with the high level of expertise needed, such as to ensure the quality of its monitoring and enforcement activities in specialized areas such as financial services.
- \* Considering if there is a need to enhance the composition, capacity and competencies of the SARAS board to increase its effectiveness in areas such as dispute resolution and adopting regulations.

SARAS should also consider the need for a dispute resolution mechanism with paid independent audit experts to address disputes arising from auditor registration and inspections. This would reduce the challenge which the SARAS board faces, where not all board members have detailed technical knowledge of audit matters and where the non-payment of board members restricts their available time and resources.

**367. In line with Georgia's efforts to achieve EU membership candidate status and to enhance the country's overall capacity to uphold the membership obligations, SARAS and legislators should continue efforts to further align with the EU requirements in the areas of accounting and financial reporting.** Areas for further alignment in relation to corporate reporting, as highlighted by the EC Analytical Report<sup>279</sup> on Georgia's EU membership application, include financial reporting standards relating to small entities; and country-by-country reporting by very large multinational companies. While there is some simplification of financial reporting requirements by entity (and group) categories, SARAS should implement the further financial reporting simplifications that are needed to meet the EU requirements, given Georgia's commitment under the Association Agreement to approximate its institutions and policies with those of the EU.

**368. In relation to EU audit legislation, SARAS should address areas of partial compliance, including:** the definition of "key audit partner" should be introduced in the law; requirements about the disclosure of an audit firm's office locations and about the network should be added to the registration requirements; the mechanism for possible delegation of tasks by SARAS to other bodies should be covered by the law; all annual reporting requirements for regulators should be included in the law; and the definition and the description of the annual transparency report by auditors should be introduced in the law.

**369. PIE annual reports that are required by regulators to be published or otherwise disseminated earlier than the deadline for non-PIE annual reports should include a management report.** SARAS' annual report filing requirements include a requirement to produce a management report. Management reports provide context to

the financial numbers reported in the AFS, and are generally considered an important, if not essential, element of financial reporting. SARAS requires that entities file their results by October 1 of each year. Regulations for certain PIEs (banks, insurers, listed entities, and MFIs) require that these entities publish their financial statements earlier (variously April 15, May 15, or June 1). These earlier requirements are appropriate given the public nature of the entities. However, the earlier requirements do not always include the publication of management reports. The consequence is that financial statements are frequently filed without management reports, with the management reports following at a later date, sometimes months later, and the further consequence is that the management report is sometimes never published on the entity's website. This somewhat defeats the objective of the early reporting requirements and of the requirement for a management report.

**370. The date for publication and public dissemination of annual reports of PIEs should be aligned more closely with the requirements by regulators for earlier finalization of those annual reports.** PIEs operating in regulated sectors are required to provide audited annual reports to their regulators at a date earlier than they are required to publish those annual reports on REPORTAL. For example, insurers are required to submit annual reports to regulators by April 15 each year but are only required to publish those financial statements on REPORTAL after October 1. The consequence is a possible delay in providing available, verified information to stakeholders.

**371. Publishing requirements should specify the wider dissemination of financial statements of PIEs.** Currently, financial statements of PIEs are required to be submitted to regulators and/or posted on their own websites on a date in advance of their filing on the SARAS website. Each entity has a unique design for its website, some website links do not work, and the location of the financial statements is not always readily apparent. Financial statements of PIEs promote transparency for investors and lenders, but also for other stakeholders such as providers of broader investment into Georgia, customers, depositors, policyholders, and staff. Consideration should be given

<sup>279</sup> [https://neighbourhood-enlargement.ec.europa.eu/system/files/2023-02/SWD\\_2023\\_31\\_Georgia.pdf](https://neighbourhood-enlargement.ec.europa.eu/system/files/2023-02/SWD_2023_31_Georgia.pdf)

to requiring broader dissemination of information for PIEs, including publication of summarized information in newspapers and posting of information in branches. Hard copies of full financial statements should be available on reasonable request.

**372. Systematic and legally enforceable collaboration between all sector regulators and external auditors of regulated entities should be established.** Under the current legal framework, different regulators have differing levels of authority and practice for contacting auditors, demanding communication from auditors, and requesting clarification or additional work. There are generally no requirements for periodic meetings or intervention in audit planning, although the banking regulator does have periodic meetings as mandated by an internal manual. International good practices recommend that regulators should establish a system of collaboration with auditors. Such collaboration can vary from regular exchanges of information and meetings to requiring auditors to perform additional scope work for regulatory purposes. Collaboration should be consistently mandated in regulations for different sectors, mandated meetings with auditors should occur on a regular basis, and regulators should be empowered to demand certain information from auditors, including audit management reports and advance notice of qualifications and significant findings.

**373. Consider simplifications to requirements for MFIs.** Existing regulatory practice for MFIs restricts their ability to raise funding from individuals. Consequently, MFIs are funded by a combination of specialist loan funding, professional funding and shareholder capital.<sup>280</sup> This is credited with helping the MFI industry survive the effects of the COVID-19 pandemic. The MFI industry is subject to significant prudential and financial reporting requirements which are justified protections if the industry is raising funding from the general public. However, if the existing restriction on retail loan funding by the MFIs is maintained or is codified in law or regulation, consideration should be given to allowing MFIs or some subgroups of MFIs to report under the IFRS for SMEs. To the extent that an MFI is only raising funds

from professional lenders, the additional burden of preparing IFRS financial statements is not warranted.

**374. A consolidated Code of Corporate Governance for all PIEs should be issued, and laws and regulations updated to ensure its effective enforcement.** Regulations on corporate governance are fragmented, with some sectors (for example commercial banks) having specific requirements, others (for example insurance) having no specific requirements, and some requirements being partially incorporated into law or regulations pertaining to a specific industry. There are both gaps and duplications. The insurance regulator is in the process of drafting new and separate regulations for the insurance industry. A consolidated Code for all PIEs should be issued by a single, centralized authority incorporating the best of the existing requirements. The legal framework should be amended to ensure the consolidated Code is applied consistently, with monitoring of compliance and consequences for non-compliance. Duplications should be removed. In preparing a new corporate governance framework, consideration should be given to international and EU best practice.<sup>281</sup> International good practices recommend that PIEs, such as banks, financial institutions, insurance companies, and entities having stocks or bonds issued to the public, must prepare and publish an annual self-assessment of their compliance with the Code, normally as part of the annual report. This should include results of the self-assessment against the implementation regulation; share ownership details; frequency of board meetings; number of internal fraud cases and how the entity handled them; the number of legal claims and the entity's settlement efforts; transactions with a conflict of interest; buy back of shares and/or bonds; and provision of funds for social activities and political activities with details of the nominal value and recipients.

**375. A Country Action Plan for sustainability reporting should be developed and introduced to meet the increasing demand from investors and institutions for insights into the sustainability effects of new and existing projects and activities.** Internationally, the development and

<sup>280</sup> While restricting MFIs from taking deposits, the Law of Georgia on Microfinance Organizations specifies (Article 4) that MFIs shall be entitled to obtain loans (credits) from resident and non-resident legal and natural persons (Article 4.f).

<sup>281</sup> This should include frequency of reporting, composition of Board and audit committees and considerations for sustainability reporting.

quality of sustainability reporting is becoming the preemptive area of focus for both PIEs and governments. Adopting or establishing a framework for sustainability reporting as a new early objective will allow stakeholders to become familiar with the requirements of sustainability reporting and, where appropriate, to amend behavior before this becomes a generally accepted reporting requirement. Whilst this falls broadly under financial reporting requirements, the skills involved in preparing these reports are typically different, the capacity challenges are different, and the international consensus on the precise format and content is still developing. Consequently, consideration should be given to providing a separate legal framework for sustainability reporting that does not unduly impact existing financial reporting requirements. Considering Georgia's commitment under the EU Association Agreement to approximate its institutions and policies with those of the EU, it would be necessary to ensure that the Country Action Plan introduces the required actions, resources, and timelines for adoption of the requirements of the recent EU Corporate Sustainability Reporting Directive,<sup>282</sup> as well as the European Sustainability Reporting Standards (ESRS)<sup>283</sup> developed by the European Financial Reporting Advisory Group (EFRAG).<sup>284</sup> It is important to note that non-EU companies will also have to follow the new rules. Namely, non-EU companies with substantial activity in the EU market will have to follow equivalent reporting rules. By the time of the ROSC assessment the above requirements had not been incorporated into the Georgian local legislation. In the interim, the NBG has been taking a leading role in the sustainable finance agenda in Georgia<sup>285</sup> with its sustainable finance roadmap, banking sector disclosure requirements, and sustainable finance taxonomy issued in 2022. In addition, the MOESD is leading the Georgia Green Growth Strategy. While sustainability reporting certainly goes beyond the financial sector, it'd be good if the MoF and SARAS also consider building on the experience of NBG and progress made.

**376. Implementation of the Comprehensive SOE Reform Strategy 2023-2026, that is based on good practice and sets a clear roadmap for moving forward with SOE reform, should be followed though.** The plan for an SOE framework law to put in place the various elements of the Strategy is well justified in terms of improving governance of SOEs and described in the SOE Strategy. The piloting of the three selected SOEs should be expedited, as the commencement of its implementation is already lagging behind. The new CGCSOE will constitute an important step forward once implemented and should be followed through with implementation support and enforcement without further delay starting with the pilot SOEs that are required to issue compliance statement with the CGCSOE by July 2023. Significant capacity building support should be provided to the SOEs to implement the CGCSOE.

**377. Establishment of audit committees in SOEs should be expedited.** Despite the fact that SOEs have been legally required to have audit committees since their classification as PIEs in 2020, in practice, only few SOEs have established audit committees. As audit committees have an important role in providing oversight of the financial reporting process, the audit process, and the company's system of internal controls, the government as a shareholder should take necessary measures to establish audit committees in all SOEs that have a PIE status without further delay.

**378. The MoF should seek to enhance SOE aggregate reporting and disclosure of SOE portfolio information.** The existing Fiscal Risk Statement is already very comprehensive and is a good basis for regular SOE aggregate reporting. To correspond to good practices, as promulgated by the OECD,<sup>286</sup> it could be strengthened by specifying main SOE performance trends, the Government's sector policy, and the "bigger picture" on critical contextual and non-financial information that supports an informed reading of financial information. The MoF should work with individual ownership units, ministries, and SOEs to provide inputs. The aggregate report can

<sup>282</sup> <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32022L2464&from=EN>

<sup>283</sup> The EFRAG approved the first set of ESRS in November 2022. It is expected that the European Commission will adopt the ESRS by June 30, 2023. The new standards are part of the Corporate Sustainability Reporting Directive, entering into force for reporting year 2024, with first submissions due in 2025.

<sup>284</sup> <https://www.efrag.org>

<sup>285</sup> <https://nbg.gov.ge/en/page/sustainable-finance>

<sup>286</sup> OECD Guidelines for Corporate Governance of SOEs (revised edition, 2015).



accompany the Fiscal Risk Statement, be presented to the Parliament, and publicly disclosed.

**379. As recommended by the Corporate Governance Report on Observance of Standards and Codes,<sup>287</sup> SOE management reports, mandated by the law,<sup>288</sup> could be strengthened to include:**

- \* A mandatory Corporate Governance Report, indicating the SOE's compliance with the new CGCSOE.
- \* Public statement of the SOE's objectives and their fulfilment; for fully owned SOEs this would include the mandate elaborated by the ownership entity.
- \* Costs and funding arrangements pertaining to fulfillment of public policy objectives or public service obligations.
- \* Remuneration of SOE's supervisory board members and key executives.
- \* Information about financial assistance, including guarantees, subsidies, and capital transfers received from the state.
  - Information about material transactions with the Government and related entities.
  - Information about significant issues relating to employees and other stakeholders.

**380. Consideration should be given to requiring prominent disclosure of SOE Public Service obligations and/or quasi-fiscal activities and obligations in the financial statements.** Currently, the line between commercial and non-commercial activities of enterprises is blurred. As a consequence, the MoF and other stakeholders struggle to distinguish public service obligations and/or quasi-fiscal activities in the SOE financial statements. IFRS requires the disclosure of additional information where other requirements of IFRS are insufficient to enable users of financial statements to understand the impact of particular transactions, events, and conditions.<sup>289</sup>

Understanding the nature and extent of SOE public service obligations and fiscal activities is typically material to understanding the financial position and performance of SOEs. It is recommended that SOEs be encouraged to provide these disclosures, and that a review of these disclosures be incorporated as part of enforcement activities.

**381. Consideration should be given to requiring earlier publication of annual reports of SOEs that are classified as PIEs.** Currently, SOEs that are PIEs have the same submission deadlines as non-PIEs. They are required to submit audited financial and other types of reports to SARAS by July 1 of the year immediately following the reporting period, while unaudited financial and other types of reports should be submitted by April 1.<sup>290</sup> This aims to improve compliance with international commitments outlined in the 2022 Public Expenditure and Financial Accountability Assessment<sup>291</sup> and ensure the early availability of information on SOEs' financial results to enable timely compilation of the Fiscal Risk Statement by the MoF. However, the requirement lacks an enforcement mechanism and is not fully followed by the relevant SOEs. Consideration should be given to amending the Law on Accounting, Reporting, and Audit to include earlier submission deadlines for SOEs classified as PIEs.

## ■ Monitoring and Enforcement of Financial Reporting

**382. Existing regulators' monitoring of general purpose AFS against applicable financial reporting standards should be enhanced.** Ensuring financial statements' full compliance with recognized accounting standards, including adequacy of

<sup>287</sup> Georgia Corporate Governance Report on the Observance of Standards and Codes, World Bank, 2021 (<https://documents1.worldbank.org/curated/en/09925500612222665/pdf/P1695430ad47ef0860b13f0120e7715aa67.pdf>).

<sup>288</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 7.

<sup>289</sup> IAS 1, Presentation of Financial Statements.

<sup>290</sup> Government of Georgia Decree N217 adopted on February 11, 2021.

<sup>291</sup> <https://www.pefa.org/node/5197>

disclosures and information, is a critical role for regulators to safeguard the public interest and enhance entities' transparency. International good practices include the availability of regulatory actions for non-compliance. Regulators' findings could also trigger actions by SARAS related to the quality of audits. These processes are already in place or are in the process of being developed. However, they are critically dependent on the attraction, development, and retention of skilled staff. The development of these processes should continue and the processes themselves should be enhanced.

**383. Regulations should explicitly provide for graduated sanctions to facilitate enforcement of financial reporting requirements.** Existing regulations authorize SARAS, BSD, NISD, and ISSSG to review entities' AFS, including management reports and auditor reports. The regulations also provide for some circumstances where regulators can approach the entities and auditors to conduct further investigations on exceptions found. The regulations contain sanctions and enforcement procedures for non-compliance with financial reporting and auditing standards. However, these sanctions are not graduated. Instead, they are either very mild or very severe. Findings and recommendations should be enforced by specific provisions in relevant laws and regulations to improve the quality of financial reporting and auditing and protect the public interest. Regulators should have processes in place to respond to qualifications of financial statements including, but not limited to, imposing graduated sanctions on the entity.

**384. Systematic collaboration between sector regulators with responsibility for reviewing IFRS compliance and SARAS should be established.** Under the current legal framework, regulators in the banking, insurance, microfinance, and listed entity sectors are authorized and required in varying degrees to review financial statements for compliance with financial reporting standards. The regulators have different levels of resourcing, and the effectiveness is inconsistent. SARAS is also authorized to review financial statements and has its own resourcing to achieve this. The existing arrangement appears to result in both duplication of effort and gaps in the

review processes. Effective regulation could be enhanced by a system of collaboration between the regulators. Such collaboration can vary from regular exchanges of information and findings, to more clearly defining the various responsibilities.

**385. Annual publications by each of the insurance regulator, the banking regulator, and by SARAS should detail the material findings of reviews of financial statements.** IFRS compliance reviews are being conducted by multiple regulators. In some circumstances, these reviews result in proactive changes to the financial statements of the entity being reviewed. Consideration should be given to incorporating the findings of these reviews in an aggregated and anonymized form in each of the annual reports of those regulators if they are relevant to entities under regulation. In addition, all material IFRS-relevant issues identified by various regulators should be consolidated and incorporated into the SARAS report. This will have the benefit of enabling an understanding of the review process, providing an opportunity for other entities to learn from the experience of entities that have been subject to review and making all relevant and material information more easily accessible.

**386. The implementation of XBRL by SARAS should be considered.**<sup>292</sup> As a digital reporting standard, XBRL makes reporting more harmonized, enables more efficient use of reports, and facilitates comparability of reports. The XBRL standard enables using common technical (digital) formats and thus facilitates data comparability via information harmonization (standardization), at the same time improving the quality and reliability of information submitted by the entities.

## Audit Oversight and Quality Assurance

**387. SARAS should be given a wider range of graduated sanctions on auditors and audit firms in cases of misconduct or non-compliance with standards and registration requirements.** The

<sup>292</sup> <https://www.xbrl.org/>

gap between a maximum fine of GEL 5,000 on auditors, which has a low deterrent effect, and deregistration, the ultimate sanction, is large. SARAS' ability to regulate auditors would be improved by the availability of a greater range of graduated sanctions on auditors.

## Accountancy Profession

**388. GFPAA should continue to make progress in complying with all the requirements of IFAC's SMOs as identified by IFAC's assessment of the 2022 SMO Action Plan submitted by GFPAA.** The updated self-assessment was submitted in 2022.<sup>293</sup> Once IFAC's assessment is complete, GFPAA should work on addressing any areas of non-compliance or partial compliance identified.

**389. GFPAA should work to address any recommendations made by SARAS as part of its oversight of the PAO processes and its process for ongoing approval of the GFPAA's certification.** These areas include:

- i. The PAO's board should establish a set of fundamental values by which the organization operates. All those participating in governance should embrace these fundamental values.
- ii. The PAO should manage the risks associated with possible conflict of interests and ways to address these risks.
- iii. The PAO's board should ensure that reasonable demands from stakeholders for information are met, and that the information provided is relevant, understandable, and reliable.
- iv. The PAO's board should understand the organization's business model, operating environment, and how sustainable stakeholder value is created and optimized.

## Accounting Education

**390. An educational standard for accountancy degrees at HEIs should be developed in line with IES and good international practice with the involvement of universities, SARAS, and PAOs.**

Educational standards for HEIs' accounting specialty at bachelor and master's level are recommended to be developed based on IES. These standards represent a benchmark that IFAC members are expected to meet for the initial and continuous development of professional accountants. IES establish the essential elements of the content and process of education and development at a level that is aimed at gaining international recognition and acceptance. The development of educational standards based on IES will promote convergence of requirements on professional skills, competences, examination processes, and other aspects at both initial and continuous professional development levels.

**391. Consideration should be given to adding audit and accounting to the list of regulated professions in the Law on Higher Education.** The Law defines a list of regulated professions for which certain preconditions must be fulfilled to enter the profession, including appropriate qualifications, passing a state certification examination, and going through a specific accreditation process. Currently, audit and accounting are not listed, although they have all the features of a regulated profession. Their inclusion on the list would add consistency among educational providers to the process of gaining the auditors' qualification.

**392. University curricula should be aligned with a model curriculum, and aligned with PAOs' curricula, aiming to promote recognition of university degrees by PAOs and SARAS.** A benchmarking study of accountancy education in Georgia,<sup>294</sup> recommended that universities enhance their competency-based approach to undergraduate/graduate programs in their curricula and closely align them with IES,

<sup>293</sup> <http://gfpaa.ge/site/index.php?tid=66&color=blue&lid=66&sid=66>

<sup>294</sup> A Benchmarking Analysis and Review of Accountancy Education in Georgia: Curricula, Teaching, Assessment and Governance, World Bank, 2020 (<https://www.saras.gov.ge/Content/files/Georgia%20Benchmarking-report-eng.pdf>)

internationally recognized benchmarks, and the needs of employers. As a result, a model competency-based curriculum has been developed, based on the ACCA qualification incorporating IES, and supported by SARAS. The alignment of university curricula with the model curriculum will underpin recognition of university programs by SARAS, national and international PAOs, and peer universities.

**393. Assessment practices across universities should be aligned with IES to expedite recognition by PAO and SARAS.** A consistent approach across universities to student assessment should be implemented to ensure that competencies in the upgraded curriculum are achieved. Assessment procedures should reflect the content and intentions of the competency-based curriculum and should ensure that students are tested fairly, properly, and in accordance with international standards.

## **Setting Accounting and Audit Standards**

**394. SARAS should be ready and prepared to adopt the forthcoming IAASB standard on the audit of less-complex entities when it becomes extant, and to assist auditors with implementing the standard.**

# ANNEX A

## PROGRESS ON ROSC 2015 RECOMMENDATIONS

### ■ Statutory Framework

#### Recommendation 1. Addressed

To define PIEs in Georgian legislation, including: (i) entities traded on a regulated market; (ii) credit institutions; (iii) insurance undertakings, and (iv) undertakings that are of significant public relevance due to the nature of their business, their size or the number of their employees, as defined by the EU Directive 2013/34/EU “on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings” (Accounting Directive).

#### Status of implementation as of 31 December 2022

The Law on Accounting, Reporting, and Audit defines PIEs. The definition includes (i) entities, whose securities are admitted to trading on a stock exchange in accordance with the Law of Georgia on Securities Market; (ii) commercial banks, in accordance with the Organic Law of Georgia on the NBG; (iii) microfinance organizations, in accordance with the Law of Georgia on Microfinance Organizations; (iv) insurance entities, in accordance with the law of Georgia on Insurance; (v) founders of a non-state pension scheme, in accordance with the Law of Georgia on the Provision of Non-state Pensions and Non-state Pensions Insurance; (vi) investment funds, in accordance with the Law of Georgia on Collective Investment Undertakings; (vii) non-bank deposit institutions – credit unions, in accordance with the Law of Georgia on Non-bank Deposit Institutions – Credit Unions.

In 2019, large and medium SOEs were added to the definition based on Government Decree №584.<sup>295</sup>

## Recommendation 2. Mostly Addressed

To introduce and harmonize definitions of PIEs, large, medium, small, and micro undertakings by size of their business and type of ownership across various pieces of legislation (including but not limited to the 2012 A&A Law, Commercial Code, Tax Code, and other regulations of various governmental and regulatory bodies), to eliminate any lack of clarity, and facilitate standards compliance and enforcement.

These thresholds will determine the accounting, auditing and reporting requirements for various types of entities. Specifically, consider reducing the reporting requirements for small and micro undertakings, as many of them may be overburdened by new reporting requirements to apply the IFRS for SMEs that come into effect on June 1, 2015.

### Status of implementation as of 31 December 2022

The Law on Accounting, Reporting, and Audit introduced clear definitions of PIEs, and other entities by size of their business that determine the accounting, auditing, and reporting requirements for various types of entities. The large, medium, small, and micro are instead referred to as first, second, third, and fourth category entities in the Law on Accounting, Reporting, and Audit, to avoid confusion of terms with the Tax Code.

The definitions of entities for corporate reporting purposes in the Law on Accounting, Reporting, and Audit are in line with international good practices.

There remain some inconsistencies with the equivalent definitions in the Tax Code. However, the impact on corporate reporting in general is not significant.

The reporting requirements for small and microenterprises have been reduced by adoption of the Law on Accounting, Reporting, and Audit and subsequent SARAS regulations, including development of dedicated standards for microenterprises.<sup>296</sup>

## Recommendation 3. Addressed

To establish publication requirements for companies significant to the Georgian economy, for example PIEs and large undertakings as defined by the EU Accounting Directive 2013/34/EU, to publish their audited, unabridged financial statements before the AGM or within a reasonable period of time, which shall not exceed 12 months after the balance sheet date, either through the internet or by providing copies free of charge, so that shareholders are better prepared to decide on the approval of these statements.

### Status of implementation as of 31 December 2022

The Law on Accounting, Reporting, and Audit established publication requirements for all entities except microenterprises to publish their financial statements 9 months after the balance sheet date via the REPORTAL platform<sup>297</sup> developed by SARAS and PIEs to publish on their websites as well.<sup>298</sup> Reports of all category entities except the small and microenterprises must be audited. The reports of microenterprises are accessible upon request via SARAS.<sup>299</sup>

<sup>295</sup> Government of Georgia Decree №584 on Defining Criteria of Determining Public Interest Entities by the Service of Accounting, Reporting, and Audit Supervision of 29.11.2019.

<sup>296</sup> SARAS Decree on Adopting Financial Accounting Standards for the Entities of the Fourth Category of 26.06.2018.

<sup>297</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 9.

<sup>298</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 9.5.

<sup>299</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 9.3.

## Recommendation 4. Addressed

To establish a sustainable funding support mechanism to allow the accredited professional organization(s) to perform functions delegated by the Government effectively and on a timely basis, free from undue influence and bias: (i) translation and timely updates of the standards; (ii) development of the simplified accounting standards for microenterprises; and (iii) initial registration of auditors, and maintenance of such registry.

### Status of implementation as of 31 December 2022

The Law on Accounting, Reporting, and Audit does not delegate the key functions to the PAOs (as was the case at the time of 2015 A&A ROSC). The translation and timely updates of the standards; the development of simplified accounting standards for microenterprises;<sup>300</sup> and the initial registration of auditors, and maintenance of such registry,<sup>301</sup> are now assigned to SARAS, which is funded by the state budget.

## Accounting and Auditing Standards

### Recommendation 5. Addressed

To enhance the standards translation process to ensure sustainability of timely and quality translations, with consideration of funding support from the Government and other sustainable sources of funding.

### Status of implementation as of 31 December 2022

SARAS ensures timely and quality translations of standards from its allocated state budget, which can be considered as sustainable funding.

## Recommendation 6. Addressed

To develop and adopt further standards, for example simplified accounting standards for microenterprises.

### Status of implementation as of 31 December 2022

Simplified accounting standards for microenterprises have been developed and adopted by SARAS in 2018. The standards are already implemented in Georgia among the respective entities.

## Recommendation 7. Addressed

To develop an ISA compliant standard audit methodology and audit manual for small and medium audit practices, which would improve the quality of the audit profession of Georgia as a whole and lead to an increase in public confidence in the reliability of the information contained in financial statements.

### Status of implementation as of 31 December 2022

ISA compliant audit manual developed by the HAT Group for small and medium audit practices has been translated into Georgian (with the help of the donor community and in collaboration with the GFPAA) and transferred to the respective audit practices. The HAT manual has also been integrated into the E-Dok program to facilitate easier uptake by SMPs. A dedicated train the trainers program has been rolled out for the SMPs to help them properly implement the HAT manual. Up to 350 SMPs were trained as a result.

## Recommendation 8. Addressed

To identify and designate an existing regulatory body(-ies), or department(s) within the existing regulators, to enforce accounting standards and reporting compliance for PIE and large undertakings. This body(-ies) should be equipped with standard enforcement mechanisms and respective enforcement authority.

<sup>300</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 3.6.

<sup>301</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 12.

### Status of implementation as of 31 December 2022

SARAS was created in 2016 to enforce accounting standards and reporting compliance for all undertakings. SARAS is fully equipped with the standard enforcement mechanisms and respective enforcement authority.<sup>302</sup>

### Recommendation 9. Addressed

To centralize filing of SOE financial statements in a single agency or department within the existing regulator. This step will avoid duplication of functions and allow the Government to get a consolidated view of the companies in which the state owns some of the capital.

### Status of implementation as of 31 December 2022

Filing of all SOE financial statements is centralized under SARAS. In addition, around 120 SOEs file financial information with the Fiscal Risk Unit under MOF, which performs fiscal risk analyzes based on received information.

### Recommendation 10. Addressed

To establish a new, or designate an existing, body as competent authority in charge of the regulation and/or oversight of statutory auditors and audit firms, as required by the EU Directive 2014/56/EU “on statutory audits of annual accounts and consolidated accounts” (Audit Directive). The Directive provides for significant flexibility in audit regulation, requiring only a limited level of obligatory provisions for implementation. Georgia should use the time allowed under the Association Agreement to learn more about this policy area, drawing on the experience of other countries, exploring the obligatory requirements of the Audit Directive and considering the implementation of optional provisions for a later stage.

### Status of implementation as of 31 December 2022

SARAS was created in 2016 and is in charge of the regulation and oversight of statutory auditors and audit firms.<sup>303</sup>

### Recommendation 11. Addressed

To continue increasing the institutional capacity of regulators to improve their ability to enforce compliance with financial reporting requirements. These institutions should have adequate resources to perform in-depth reviews of corporate financial statements and related audit reports. The staff of regulatory agencies will need training to be able to effectively enforce compliance with IFRS.

### Status of implementation as of 31 December 2022

SARAS enforces compliance with financial reporting requirements on a risk-based basis, however capacity and resources to perform in-depth reviews of corporate financial statements and related audit reports could be increased.

### Recommendation 12. Addressed

To enhance collaboration between the Government and the professional accounting organizations to strengthen compliance and enforcement of IFRS application, establish quality control over audits, ensure timely translation of standards, and raise the quality of continuing professional education.

### Status of implementation as of 31 December 2022

The Law on Accounting, Reporting, and Audit changed the approach and assigned the function to strengthen compliance and enforcement of IFRS application,

<sup>302</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 20.3.N.

<sup>303</sup> The Law of Georgia on Accounting, Reporting, and Audit, Chapter V.



establish quality control over audits, ensure timely translation of standards, and develop the standards of continuing professional education to SARAS.<sup>304</sup> SARAS effectively collaborates with the PAOs with respect to the quality control system monitoring. PAOs are required to ensure permanent cooperation with their member auditor and audit firms and implementation of the following activities: training and continuous education in the area of quality assurance; development and provision of the methodology and manuals; evaluation and diagnostics of the quality control systems of their member auditors and audit firms; facilitation to eliminate identified weaknesses.<sup>305</sup>

### Recommendation 13. Addressed

To significantly strengthen the mechanisms to monitor compliance with the standards within the respective regulatory agencies: for accounting - NBG, ISSSG, National Agency of State Property etc., and for auditing - GFPAA, including application of appropriate sanctions for noncompliance. This will improve transparency and accountability to stakeholders. The absence of enforcement diminishes the requirement to follow the standards, creating a perception among Georgian companies that they are non-mandatory.

#### Status of implementation as of 31 December 2022

Monitoring for noncompliance with standards, previously dispersed among various agencies, has been centralized under SARAS and is being effectively implemented. SARAS was given authority to impose appropriate sanctions for noncompliance. The sanctions can be imposed on auditors, entities, and PAOs. The sanctions extend from a written notice to a range of monetary sanctions depending on the gravity of the administrative offence.<sup>306</sup> The sanctions for poor quality reporting are, however, on the lower size (up to GEL 5,000) and could be increased.

## Professional Education and Continuing Development

### Recommendation 14. Mostly Addressed

To strengthen academic curricula and align university programs with professional training and examination requirements at the accredited professional organizations in the field of accounting and auditing, as well as continuing professional education and training, in line with IFAC's education standards. These enhanced curricula should be endorsed by the Ministry of Education for consistent application throughout the country.

#### Status of implementation as of 31 December 2022

A revised academic curriculum was developed in line with IES in 2021 (with the help of donor organizations and is available at the SARAS website).<sup>307</sup> It aligns university programs with professional training and examination requirements at the GFPAA and ACCA. It is endorsed by SARAS but not yet by the Ministry of Education.

### Recommendation 15. Pending

To establish and coordinate minimum acceptable requirements for university level education in accounting and audit, taking into consideration good international practices and agreed with the Ministry of Education, and ensure such consistent application among universities in Georgia.

<sup>304</sup> The Law of Georgia on Accounting, Reporting, and Audit.

<sup>305</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 10.

<sup>306</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 23.

<sup>307</sup> <https://www.saras.gov.ge/Content/files/sarekomendacio-silabusi.pdf>

### Status of implementation as of 31 December 2022

The NCEQE plans to develop minimal standards for accounting and audit education in 2024. There will need to be early coordination with SARAS on the development process.

### Recommendation 16. Addressed

To require that professional accountants follow training programs to improve and update their knowledge of the standards and best practices in the field of accounting and auditing. For GFPAA, other professional organizations, and leading audit and accounting companies to consider offering comprehensive training courses for bookkeepers and accountants working with IFRS and the IFRS for SME.

### Status of implementation as of 31 December 2022

Continuous education requirements, in line with the Accounting Directive, have been adopted and implemented. They are overseen by SARAS.<sup>308</sup>

PAOs are obliged to monitor the CPD of certified accountants and keep appropriate records.<sup>309</sup>

Training the trainers on the IFRS for SMEs has been delivered (with donor support) and subsequently rolled out to about 1,500 accountants and other bookkeepers in Georgia.

### Recommendation 17. Addressed

To improve professional development training for professional auditors. To raise the quality of audit services among existing practitioners, GFPAA should consider developing an ISA compliant standard audit methodology and audit manual and offer comprehensive training courses to its members.

### Status of implementation as of 31 December 2022

Standard audit methodology (the HAT Group manual for SMPs) has been translated into Georgian and shared with Georgian audit firms. Training the trainer courses and end user training have been provided with the help of donor organizations.

<sup>308</sup> SARAS Decree on Approving Continuous Education Standard of 18.08.2017.

<sup>309</sup> The Law of Georgia on Accounting, Reporting, and Audit, Article 11.9.



