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Law of Neighbouring Tenements and the Essence of Private-Law Obligation of Tolerance in Georgian Law

Private Law Reform. On the whole, the analysis of civil law reforms implemented in post-Soviet countries allows for the identification of two main competitive models. Within the framework of the first model the provisions of Soviet civil law, of non-ideological nature, were retained. Majority of post-Soviet countries opted for this model.[1] *In these countries the new civil codes were adopted on the basis of Model Civil Code, which codes still retain the provisions of Soviet period. Hence, in countries which applied the above model to themselves, the reform and development of civil law were based on the traditions of the Soviet period.*[2]

Georgia opted for fundamentally different line of development of civil law. When it came to the elaboration of the Civil Code of Georgia (CCG), which was drafted under the close cooperation of renown representatives of Georgian private law science and German scholars,[3] *the Civil Code of Germany was taken as the basis. In the formation of new legal institutes the CCG fed upon the European codifications.*[4;5] *Opting for German model was conditioned by its high scholarly authority and the fact, that the authors of the CCG regarded the European type of codification fully concurrent with Georgian historical traditions.*[6]

The law is a part of culture and quite a number of cultural and technical features should be taken into account in the course of reception.[7] *It should necessarily be stressed, that none of the abovementioned models of reformation of civil law exists "as is". The countries which opted for the development*

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1 Comp. *Kurzynsky-Singer E., Zarandia T.,* Rezeption des deutschen Sachenrechts in Georgien, Transformation durch Rezeption?, Transformation durch Rezeption? Möglichkeiten und Grenzen des Rechtstransfers am Beispiel der Zivilrechtsreformen im Kaukasus und in Zentralasien, *Kurzynsky-Singer E.* (hrsg.)*,* Tübingen, 2014, 108 ff.

2 Ibid.

3 Comp. *Zoidze B.,* Reception of European Private Law in Georgia, Tbilisi, 2005, 1 (in Georgian); *Knieper R.,* Methods of Codification and Conception in Transition Economies (Including the Situation in Georgia), Legal Reform in Georgia, *Jorbenadze S., Knieper R., Chanturia L.* (eds.), Tbilisi, 1994, 176-191 (in Georgian); Also, comp. *Jorbenadze S.,* Main Challenges of Future Civil Code of the Republic of Georgia, Legal Reform in Georgia, Tbilisi, 1994, 142 (in Georgian).

4 Comp. *Makovsky A*., Einige Einschätzungen der Hilfe bei der Ausarbeitung der Gesetzgebung und des Standes der internationalen Zusammenarbeit, Wege zu neuem Recht: Materialen internationaler Koferenzen in Sankt Petersburg und Bremen, *Boguslavskij M., Knieper R*. (hrgb.), Berlin, 1998, 339.

5 See. *Chitashvili N.*, Impact of Amended Circumstances on the Fulfilment of Obligations and Potential Secondary Claims of the Parties, Tbilisi, 2014, 81 (in Georgian).

6 Comp. *Zoidze B.,* Reception of European Private Law in Georgia, Tbilisi, 2005, 92 ff (in Georgian).

7 With this regard, see: *Kennedy D.,* The Politics and Methods of Comparative Law, The Common Core of European Private Law, Essays on the Project, *Mattei U*., *Bussani M*. (eds.), Hague, 2002, 143; With regard to the question of necroreception, see: *Burduli I*., Nekrorezeption in Transformationsgesellschaften, Dogmatik im Dienst von Gerechtigkeit, Rechtssicherheit und Rechtsentwicklung, Festschrift für Hanns Prütting, *Brinkmann M., Effer-Uhe D. O., Völzmann-Stickelbrock B., Weesser S., Weth St.* (hrsg.), Köln, 2018, 3 ff.

of civil law within the framework of existing traditions, inevitably borrow certain institutes from other legal systems, at least, to the extent that such borrowing is necessary to legally provide for civil circulation in market economy. On the other hand, in countries, which opted for the reception of foreign law, certain legal traditions, existing before the reception, will be inevitably retained.[8]

Overall, current European Private Law system, and specifically the property law system, is the result of political, economic and legal thinking of the nineteenth century[9]*. The foregoing is particularly apparent in the law of neighbouring tenements, which includes normative regulations important for agricultural society of that epoch. Contemporary industrial development posed new challenges in this respect.*

Key words: *property law, law of neighbouring tenements, neighbouring nuisances, encroachment on other land plot during construction, unacceptable encroachment, building collapse danger, demand to prevent danger, emissions, perfect emissions.*

1. Law of Neighbouring Tenements in the Light of Georgian Private Law Reform

The fact, that provisions regulating the law of neighbouring tenements are accumulated in the "Law of Neighbouring Tenements" Chapter and are not scattered fragmentarily, can be regarded as an achievement of the CCG. Such systematization of provisions was unfamiliar for the law of the Soviet period. Georgian law of neighbouring tenements is a part of property law and these provisions aim at the resolution of disputes arising between the neighbours and provision for peaceful cohabitation.[10] More specifically, the provisions of the law of neighbouring tenements establish the scope of acceptable nuisance against a neighbouring land plot or other real estate, duty of the "neighbouring property owner" to tolerate such nuisance in certain cases and also, the law of neighbouring tenements incorporates provisions, regulating legal consequences of the breach of this rules.

2. Duty of Mutual Respect

Under the first sentence of Article 174 of the CCG, in addition to the rights and duties prescribed by law, the owners of neighbouring land plots are bound to hold each other in respect. This provision introduces the principle of mutual respect. The descriptive part of the provision allows for distinguishing the following elements of mutual respect between the neighbours: the owners of neigh-

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8 E.g., Georgian law renounced the abstract model of transfer of title existing in German law. Comp. *Kurzynsky-Singer E., Zarandia T.,* Rezeption des deutschen Sachenrechts in Georgien, Transformation durch Rezeption?, Transformation durch Rezeption? Möglichkeiten und Grenzen des Rechtstransfers am Beispiel der Zivilrechtsreformen im Kaukasus und in Zentralasien, *Kurzynsky-Singer E.* (hrsg.), Tübingen, 2014, 110 ff. Furthermore, today the procedure of transfer of title to immovable things does not require notarization unlike German law. With this regard, see: *Zarandia T.,* Purchase of Immovable Property in Good Faith from Unauthorized Seller per Georgian Case Law, Journal Studia Universitatis Moldaviae. Stiinte Sociale, № 8(98), 2016, 75 ff.

9 Comp. *Akkermans B.*, Sustainable Property Law?, European Property law Journal, Vol. 7, Issue 1, 2018, 1.

10 Comp. *Totladze L.,* Article 174, Commentary on Civil Code of Georgia, Law of Things (Property), *Chanturia L.* (ed.), Tbilisi, 2018, 91-92 (in Georgian).

bouring land plots are bound to: 1. abide by the rules and bans prescribed by law, and 2. respect each other. Of these two elements the first one is an objective factor and specific prohibitions, prescribed by substantive law can always be presumes as its violation. As regards the second element, it is subject to evaluation and always becomes a matter of dispute in the light of circumstances of the case[11] and acquires specific content in judicial practice. Adjacency of land plots binds the neighbours to come to terms[12].

The duty to respect is not only a declared duty, it obligates the owners of neighbouring land plots and other real estate to respect the others' property and other civil rights and exercise their rights in a manner as not to impair the others' rights. The law allows for nuisances stemming from neighbouring real estate within acceptable limits, what is envisaged by Article 175 of the CCG and toleration of these nuisances is inherent for neighbouring relationships, what is concurrent with neighbours' duty to respect each other.[13] Although the rights and obligations of the neighbours are regulated by the Code and other acts, but this list can never be exhaustive. The neighbouring relationships easily escape the oversight of the law and due to this reason Article 174 of the CCG introduces the common-law obligation of the neighbours. Mutual respect means such bilateral binding, that will have legal implication.[14] Mutual respect, first and foremost concerns personal obligation of each owner to respect the rights of the neighbour while enjoying their property, what may even result in the restriction of enjoyment of own property to a certain extent. Property right, as one of the fundamental rights, is a social phenomenon, which should be protected and cared for in relationships between the neighbours.[15]

Furthermore, public-law regulation is also important for the law of neighbouring tenements, the fields like environmental law, construction law. The law of neighbouring tenements, construction and environmental law is an apparent example of coexistence of private law and public law.[16] To this end it is important to exercise property right is such a manner as to ensure common benefit to maximum practicable extent. This means the new conceptual understanding of property right itself, admitting that being an owner does not mean clearing out everything from the object of title, but rather this right is combined with the duty to look after, take care and keep it for the next generation.[17]

The provisions of the law of neighbouring tenements are based on classical principles of private law like party equality, good faith and disposition. Specifically, unless otherwise prescribed by law, a party agreement is admissible which prevails if there is a dispositional regulation.

3. Scope of Application

The "neighbouring property" relationship exists in every civilized community and is based on the recognition of property right as absolute estate on the one hand and on the other - respect of the

11 Comp. Decision of May 25, 2014 № AS-122-116-2014 Supreme Court of Georgia.
12 Comp. *Schwab K. H., Prütting H.,* Sachenrecht, 32 aufl., München, 2006, 129.
13 Comp. Decision of October 29, 2013 № AS-526-500-2013 Supreme Court of Georgia.
14 Comp. *Zoidze B.,* Georgian Property Law, Tbilisi, 2003, 111 (in Georgian).
15 Comp. Decision of July 15, 2016 № AS-413-396-2016 Supreme Court of Georgia.
16 Comp. *Wolf M., Wellenhofer M.*, Sachenrecht, 31 aufl., München, 2016, 663.
17 Comp. *Akkermans B.*, Sustainable Property Law?, European Property Law Journal, Vol. 7, Issue 1, 2018, 3.

rights of the thirds persons, the "neighbouring owners" in the case concerned, and taking account of their interests, also the general principle of bona fide exercise of a civil right. The law of neighbouring tenements regulates relations between the neighbours stemming from their property. To a certain extent it is a search for compromise between the freedom of ownership and its limitation in the interests of other persons.

In Georgia the provisions of the law of neighbouring tenements serve the purposes of regulation of everyday housing relations, like, use of adjacent land plot, consequences of trespassing, private boundaries, issues of neighbouring nuisances. Contemporary law of neighbouring tenements conforms modern challenges, the technological development brought about new disputes about electromagnetic waves as neighbouring nuisances. Hence, the law of neighbouring tenements is also linked with environmental issues.[18] Hence the property right of the owners of land plots and other real estate is limited from the every outset, it is necessary to find a balance between the interests of the neighbours. A land owner cannot exercise his right as if he is alone in the world.[19]

In Georgian reality the scope of application of the provisions of the law of neighbouring tenements extends not only to directly adjacent land plots, but rather, the provision of the law of neighbouring tenements also apply in cases when land plots do not have a common border, or are otherwise separated from each other. In practice, the most hazardous nuisances originates not from directly adjacent, but rather remote land plots, an example of the foregoing being the cases of water pollution by factories or leakage of harmful gases[20]. It is important to be possible to have a negative impact on the other land plot. Furthermore, the scope of application of the law of neighbouring tenements is not limited only to land surface, it also extends beyond and over it. However, a land owner is not entitled to claim the prohibition of such nuisance, he has no reasonable interest to prevent, e.g. flight of airplanes.[21]

4. Acceptable Nuisance - Tolerance of Neighbouring Nuisances

The property right entitles an owner to enjoy his land plot at his own discretion, exclusively, excluding others. Furthermore, Article 175 of the CCG provides for the limits of prohibited and acceptable enjoyment of land plot and other real estate. According to Part 1 of Article 175 of the CCG an owner of a land plot or other immovable property may not prohibit the impact of gas, steam, smell, soot, smoke, noise, heat, vibrations or other similar phenomena emanating from a neighbouring land plot, unless they obstruct the owner from enjoyment his land plot or immaterially impair his rights. According to literal interpretation of the provision only the owner of the neighbouring plot is entitled to claim the suppression of nuisances, but the provision should be interpreted widely and all the rightful owners should be given this right.[22] Furthermore, Part 1 of Article 175 of the CCG contains only a partial list of all possible nuisances, that may exist in legal relations under the law of neighbouring

[18] Comp. *Schwab K. H., Prütting H.,* Sachenrecht, 32 aufl., München, 2006, 123-124.
[19] Ibid.
[20] Comp. Ibid, 130.
[21] Comp. *Wolf M., Wellenhofer M.*, Sachenrecht, 31 aufl., München, 2016, 398.
[22] Ibid, 406.

tenements. The above provision provides for the obligation of tolerate nonessential emissions. Hence, as a general rule, an nuisance is nonessential when established limits are not violated as a result of nuisance. The established standards can be environmental or other standards[23][24] and they may be prescribed by law.

Under Part 2 of Article 175 of the CCG the obligation to tolerate still exists when nuisance is essential but is caused by ordinary enjoyment of the other land plot or real estate and it cannot be prevented through measures that are regarded as regular economic activity for such users. When establishing how essential the nuisance is, the focus is made on an average reasonable person, respectively on an ordinary user of a land plot or other real estate. In this case one cannot rely only on subjective comprehension of the aggrieved party.[25] The account is also taken of the location as there is a different approach in urban and rural area, densely populated area and industrial zones, also in recreational and touristic territories. Hence when assessing neighbouring nuisance the account is taken of the location, intensity and duration of impact and the assessment is made with due consideration of the criteria, pertinent to the place concerned,[26] from the point of view of an ordinary (impartial) observer.

However, when nuisance is essential, but is caused by "ordinary" enjoyment, the owner, who allowed such nuisance against his land plot or other real estate, is entitled to claim relevant, adequate monetary compensation from the owner of the neighbouring land plot.

It goes without saying, that nuisances can be of different type - it can be either material, as in the case of "penetration" onto the neighbouring land plot in the form of solid or liquid mass or immaterial - when nuisance is caused by some invisible material, smell, or vapour, e.g. gas leak, smoke, heat, noice vibration.[27]

Hence, according to Georgian law, when some nuisance is emanating from the neighbouring land parcel, what cannot be regarded as a material breach even from the point of view of an objective observer, such impact is non-essential. And contrary to the foregoing, the impact is essential, when an owner, living in the neighbourhood, neglects the interest of the neighbour, e.g. arranges a car-wash station in the garage, thus causing material restlessness in the neighbours.[28]

It is worth mentioning, that the law does not define whether what is an unacceptable nuisance and it is judicial practice, who has to answer this question. Furthermore, for instance, the air pollution conditioned by the activities of a neighbour, excessive noise, water discharge can be regarded as essential nui-

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23 E.g. Order № 297/N of the Minister of Labour, Health and Social Protection of Georgia on Approval of the Qualitative Environmental Standards of Tbilisi, dated 16/08/2001.

24 E.g. Code of Administrative Offences of Georgia, Article 77, Emission of harmful substances in atmosphere in excess to established standards or the absence of such standards and harmful physical impact on atmosphere, exceeding acceptable limits of harmful emission or/and temporarily approved limits of emission in atmosphere, the absence of these standards also the technical report on the inventory of the sources of pollution of atmosphere and hazardous substances emitted thereby and exceeding the established limits of harmful impact on atmosphere (amongst them of noise, vibration, electromagnetic fields) is punishable by fine in amount of five hundred to thousand GEL.

25 Comp. *Kropholler J.*, German Civil Code, Study Comments, *Chechelashvili Z.* (trans.), *Chachanidze E., Darjania D., Totladze L.* (eds.), Tbilisi, 2014, 690 (in Georgian).

26 Comp. *Prütting H.*, Sachenrecht, 36 aufl., München, 2017, 133.

27 Ibid, 130.

28 Comp. Decision of December 31, 2014 № AS-764-731-2014 Supreme Court of Georgia.

sance. Also, the arrangement of a mobile base station should require the permission of the neighbours. The so-called "sound pollution" is very frequent. The "acceptable" limit of voice is the level of voice, which does not cause material restlessness of a human being.[29] Normally, the noise pollution level should not exceed 40 decibels from 07:00 am. till 23:00 pm. and 30 decibels after 23:00 pm.

5. Perfect Emissions

Modern European literature widely disputes[30] the admissibility of nuisances stemming from a neighbouring land plot, that contradict "human feelings", their morale, ethics.[31] In legal literature an example of the foregoing is an unpleasant view from the neighbouring land plot, e.g. arrangement of a brothel or bordello; or depraved and immoral behaviour of the neighbours (e.g. walking naked in own yard). Overall, the question of such emissions is disputable and judicial practice is non-sequential. In certain cases a recourse can be made to provisions on the abuse of power.[32]

6. Local Rules and Traditions

When assessing the question of exceeding the limits of acceptable nuisance the account should necessarily be taken of the limits set according to local traditions. As a general rule, the case concerns car noise, hanging out of a flag in a yard, various yard games, operation of a lawn-mower, etc. It is widely accepted that while assessing these situations the account is taken of relevant rules of local public order. The absence of obligation to tolerate essential nuisance in places concerned results in deployment of a negative action, envisaged by Part 2 of Article 172 of the CCG. Furthermore, it is important for the assessment to pay attention, whether or not the offender tried to prevent this nuisance through available for him economically justified means. If nuisance is essential, the owner is entitled to claim monetary compensation. A precondition for receiving monetary compensation is the existence of essential negative nuisance, also of violation against the neighbouring land plot through such nuisance, and the obligation to tolerate such nuisance emanating from a neighbouring land plot.

Some types of exposure are quite common in practice and thus are duly regulated by law.

7. Unacceptable Encroachment, Building Collapse Danger

A neighbouring land plot can be subjected to different types of nuisances and the legislation regulates only that part of these nuisances that are most widely known in practice. According to Article 176 of the CCG an owner of a land plot may demand the prohibition of erection and utilization of such buildings on neighbouring land plots that unacceptably encroach on the right to enjoy the land

[29] Observance of accepted levels of noise on the territory of Tbilisi is overseen by the Supervision Service of Tbilisi Municipality. Comp. Resolution № 1-2 of the Assembly of Tbilisi Municipality on Approval of the Regulations of the Supervision Service of Tbilisi Municipality, dated 12/01/2016.

[30] Comp. *Prütting H.*, Sachenrecht, 36 aufl., München, 2017, 130.

[31] Comp. *Iro G.,* Bürgerliches Recht, B. IV, Sachenrecht, 3 aufl., Wien, New York, 2008, 64.

[32] *Zoidze B.,* Georgian Property Law, Tbilisi, 2003, 113 (in Georgian).

plot and the foregoing is apparent from the very outset. It should be stressed that mentioned Article is of preventive nature and in the case of unacceptable encroachment, based on the interests of the owner guaranteed by this provision, subject to suppression of interference is the nuisance, emanating from the building constructed even in accordance with construction rules.[33] Furthermore, unacceptable encroachment means the construction or such exploitation of a building that exceeds the statutory scope of toleration neighbouring nuisances and endangers the owner of a neighbouring land plot to a certain extent.[34] Hence, in the case of observance of normative construction rules by a neighbour regarding the distance between constructions and the borderline of the land plot, also other preventive measures, that the provision can be applied only when "unacceptable encroachment" is actually present with all its elements.

According to the interpretation of the Court of Cassation offered in one of its cases, prohibition of exploitation of a high-risk fuel station can be based on the provision on unacceptable encroachment. It can be said, that given its legal nature Article 176 of the CCG again prevails over to Article 175, regulating the obligation to tolerate neighbouring nuisance, as it grants an owner of a land plot with the right to prohibit the construction or exploitation of a building when the following two preconditions are present: the right to enjoy the land plot is unacceptably violated and the foregoing is apparent from the very outset. According to the explanations of the Court of Cassation the above cumulative conditions generate the precondition for demanding the prohibition of exploitation of already constructed building, what is the stringent form of restring the right to property enjoyment. In this case the holder of the right to claim bears the burden to prove that his land plot is subjected to unacceptable encroachment in the case of exploitation of a fuel station. Only the fact, that the fuel station is the source of high risk cannot be regarded as a proof to the foregoing, as public law provides for its technical security requirements to these very end.[35]

Also, only the fact, that, e.g. a gas pipeline is the source of high risk, cannot become ground for dismantling constructions. As stated with regard to one of the cases, whereas a gas pipeline is a high-risk unit, the respective normative act provides for the rules of its protection and terms and conditions of regulation of protective zones. These provisions aim at the prevention of hazards emanating from or against this gas pipeline and determination of protective zones and provision for different terms and conditions of regulation serve these very purpose. Hence, only the fact, that a gas pipeline is a high-risk unit is not sufficient ground for prohibition of construction or exploitation of a building in the neighbourhood. The construction of such units is admissible when specific technical terms and conditions are abided by, the violation of which should be proved for it to be qualified as an unacceptable encroachment.[36]

Part 1 of Article 177 of the CCG provides for the right to demand the elimination of the danger of building collapse only when such danger may be emanating from the neighbouring land plot. In this case the owner may demand that the neighbour undertake necessary measures to eliminate the danger.

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33 Comp. Decision of May 25, 2014 № AS-122-116-2014 Supreme Court of Georgia.
34 Comp. Decision of March 22, 2012 № AS-40-38-2012 Supreme Court of Georgia.
35 Comp. Decision of July 15, 2016 № AS-413-396-2016 Supreme Court of Georgia.
36 Comp. Decision of October 29, 2013 № AS-526-500-2013 Supreme Court of Georgia.

In the case of exceptional circumstances, when the owner is avoiding the fulfilment of his obligations, the owner, who is facing danger is entitled to deploy self-assistance articles by way of analogy and relay on the rules on carrying out the duties of the other persons without assignment[37] as nobody is required to wait until the neighbouring building "falls on him". The responsibility also includes fixing expenses.[38] Furthermore, the law prohibits changing the direction of waters or ground waters passing through several land plots or such manipulation with waters what may result in the decrease or the amount of water or/and deterioration of its quality, also the encroachment upon natural flow of rivers.

8. Invasion into the other land plot during the construction works

Article 179 of the CCG provides for the case when an owner of a land plot unintentionally encroaches the boundaries of the neighbouring land plot. Crucial in this case is the mode of crossing the border: intentionally or as a result of negligent action. If the boundary was crossed intentionally the owner may relay on Article 172 of the CCG and demand the dismantling of the construction. If the boundary was crossed without an intention or gross negligence,[39] the law obliges the owner of the neighbouring land parcel to tolerate this nuisance on his land parcel as in this case the economic interest of the other party is involved, except for the cases, when he opposed the foregoing in advance or as soon as he became aware. Construction is a process and a party may unintentionally conduct certain works beyond the boundaries of his territory due to non-awareness of the exact outline of the boundary. Encroachment on border, if there is such, can easily be noticed by the neighbouring owner. Thus, the law obliges the owner, for whom it is important for his land plot not to be subject to any such nuisance, to immediately inform the other party about the encroachment on the border - in advance, as soon as a doubt has arisen about this danger or as soon as he became aware of the foregoing. In the case of failure of the owner to do so, he loses the right to demand dismantling of the construction erected on his land plot.[40] Hence, if the neighbour in breach is acting wilfully, then nothing will prevent demanding the suppression of negative nuisances caused by construction works. And if construction works are extended to the land parcel of the other owner without any intention, this demand can be upheld only when the neighbour whose rights were violated, laid a claim in advance or as soon as he became aware of the foregoing. But if he becomes aware of potential violation, but lays no claim immediately, the owner of the land plot, whose rights were violated should tolerated the nuisance concerned.[41] The neighbour encroaching the boundary is obliged to pay monetary compensation, which should be paid in advance on an annual basis. Furthermore, in the case of deciding on compensation, no subsequent claim for restitution of old boundaries should not be satisfied.[42]

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37 Comp. *Zoidze B., Zarandia T.,* Check Your Knowledge, Cases in Property Law (Questions and Answers), Georgian Property Law, Tbilisi, 2003, 513 (in Georgian).

38 Comp. *Prütting H.*, Sachenrecht, 36 aufl., München, 2017, 139.

39 Comp. *Wolf M., Wellenhofer M.*, Sachenrecht, 31 aufl., München, 2016, 417.

40 Comp. Decision of November 28, 2016 № AS-142-138-2016 Supreme Court of Georgia.

41 Comp. Decision of October 30, 2015 № AS-36-33-2015 Supreme Court of Georgia.

42 Comp. Decision of September 16, 2002 № 3K-601-02 Supreme Court of Georgia.

Hence, Georgian legislation provides for a special provision to regulate cases of unintentional intrusion into the other land plot during construction works (CCG, Article 179), which provision aims at striking balance between the interests of the owners of the land plots and compensation of the obligation of the owner of the neighbouring land plot to tolerate through paying damages.[43] However, the Civil Code regulation concerns only the cases of unintentional encroachment. Hence the jurisprudence boldly confirms, that every construction, intentionally erected on the territory of the other owner land plot, against the will of the latter, is subject to dismantling. *Prima facie*, if we recognise the inviolability of property right and absolute and special nature of property, we should also recognise the right to claim the dismantling of the construction, crossing the border, irrespective of mental attitude of a perpetrator towards this fact (was it an intentional act or negligence). Actually, allowing the maintenance of erected construction, even in lieu of payment of compensation, is equal to allowing expropriation not in favour of the state, but rather of the other private person. Hence, when a builder has no direct intention to encroach upon and misappropriate the neighbouring land plot, this should explicitly lead the former to dismantling of the construction. Hence the owner has the absolute right to protect the integrity of his property against his neighbours.[44]

9. Easement by necessity

Under Article 180 of the CCG, when a land plot has no access to public roads, power grid, oil, gas and water supply system its due enjoyment, the owner is entitled to request for the neighbour to tolerate the enjoyment of his land parcel to ensure such necessary utilities. The main purpose of this regulation is for any land parcel to have necessary access to public roads and necessary utilities even when such utilities are not located on directly adjacent or neighbouring land plot. The foregoing can be requested only by the owner and not possessor of the land plot from the neighbour, whose land plot allows for the shortest and most reasonable access to public road or utility.[45] Furthermore, the right to easement by necessity implies single-option cases and should be conditioned by certain "urgency"[46]. This road should be important for ensuring the necessary access to the main land plot.

Hence, Article 180 provides for terms and conditions of statutory binding, in the case of existence of which the neighbour is required to tolerate encumbrances, his land plot is subjected to due to easement by necessity. Furthermore, these encumbrances should be conditioned by objective factor, specifically, when the land parcel is fully isolated from the public road or the major part of it is landlocked, or when there was as a road necessary for its due enjoyment but currently it cannot be used to this end. The necessary road implies not only a path, a footpath, but also a motor-way. The right to easement by necessity can be employed for the passage of a pipeline.[47] The right to connect to a public road is a statutory

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43 Com. *Totladze L.,* Article 174, Commentary on Civil Code of Georgia, Law of Things (Property), *Chanturia L.* (ed.), Tbilisi, 2018, 91-92 (in Georgian).

44 Com. *Capitant H., Terré F., Lequette Y.,* Les grands arrêts de la jurisprudence civile, Tome I, 11e ed., Dalloz, 2000, 334-338.

45 Comp. *Wolf M., Wellenhofer M.,* Sachenrecht, 31 aufl., München, 2016, 421.

46 Comp. *Prütting H.,* Sachenrecht, 36 aufl., München, 2017, 140 ff.

47 Comp. Case on the passage of Baku-Tbilisi-Ceyhan pipeline, qualification as a necessary road and exclusion of construction and easement. Decision of April 21, 2005 № AS-1416-1548-04 Supreme Court of Georgia.

right and it cannot be restricted.[48] In judicial practice the right to easement by necessity is proved by various evidences, including an expert opinion.

It should be stressed that only the comfortable connection cannot be used as an argument for easement by necessity. What is more, without this necessary road the marketability of the land plot should be unjustifiably decreased.[49] Article 180 of the CCG is applicable to power, gas or water supply systems, also in the case of the Internet and other means of communication. This right applies both to land plots and constructions. Judicial practice with this regard is mostly uniform, the easement by necessity is employed for ensuring the access to public road or connection to utilities when the land plot is landlocked and there is no connection. The right to request easement by necessity should be conditioned by objective conditions - the owner should be unable to enjoy own land plot without encumbrance of the neighbouring land plot. The property right can be limited only in such cases of enjoyment of others' property.[50] The neighbours, whose land plots are crossed by necessary road or utility system, should be paid the adequate compensation, which can be made as a lump-sum payment. The amount of compensation is determined through mutual agreement of the parties, but if the compensation is determined by court, it should be reasonable and should not impose excessive burden on the party. In one of its cases the Supreme Court of Georgia found that imposition of 200 GEL as a compensation for tolerance of easement by necessity was not reasonable as this would have taken the person, responsible for compensation over a rough road.[51]

Furthermore, the obligation to tolerate easement by necessity will not arise if there is no connection as for this moment, but the earlier existing connection was eliminated due to wilful actions of the owner.

10. Conclusion

As mentioned above, Georgia went through the reception of German property law, however the reception concerned the basic structures of regulation in the very first place.[52] The transposed rules were considerably simplified during the process of reception, what goes true with the part of the law of neighbouring tenements. As a result of such simplification the reception did not cover quite a number of details, which *prima facie* seem to be of accessory nature, but relatively in-depth analysis demonstrates that these details maintain the balance of interest, which is embodied in German model. However, requirements concerning unacceptable encroachment and suppression of danger are widely applied in Georgian judicial practice and acquire specific legal meaning in specific court decisions.

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48 Comp. Decision of March 6, 2012 № AS-1732-1713-2011 Supreme Court of Georgia.

49 Comp. *Wolf M., Wellenhofer M.,* Sachenrecht, 31 aufl., München, 2016, 421-422.

50 Comp. Decision of May 24, 2011 № AS-102-100-2011 Supreme Court of Georgia.

51 Comp. Case 20 GEL instead of 200 GEL, Decision of October 5, 2005 № AS-328-648-05 Supreme Court of Georgia.

52 *Kurzynsky-Singer E., Zarandia T.,* Rezeption des deutschen Sachenrechts in Georgien, Transformation durch Rezeption?, Transformation durch Rezeption? Möglichkeiten und Grenzen des Rechtstransfers am Beispiel der Zivilrechtsreformen im Kaukasus und in Zentralasien, *Kurzynsky-Singer E.* (hrsg.)*,* Tübingen, 2014, 110 ff.

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31. Decision of May 24, 2011 № AS-102-100-2011 Supreme Court of Georgia.
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Certain Aspects of Regulation of Factoring in Georgia

The article below considers certain specifics of legal institute of factoring and issues connected with regulation of this financial service in Georgia. Effective legislation factually ignores factoring and this set on the agenda necessity of comprehensive processing of this legal field on legislative as well as on scientific level. Discussion provided in the article is based on analysis of legislation and practice of various countries. Taking into account the international experience, the article presents proposals for regulation of factoring in Georgia. Pursuant to author's view, factoring which is traditionally considered as a regulated field of economics, should preferably fall under supervision of regulatory body but at the same time such supervision should not complicate delivery of factoring services and activities in the area of mentioned legal institute should be attractive, profitable and interesting for an entrepreneur. Along with the achievements of foreign countries in the field of factoring, the article refers to experience gained in inter-agency working group dedicated to factoring law reform and factually presents certain outlines of Georgia's future factoring legislation.

Key Words: *Factoring, Financial Service, Factoring Company, Commercial Bank, Microfinance Organization, National Bank of Georgia, Licensing, Supervision, Reporting.*

1. Introduction

A number of obstacles hinder the full-scale development of entrepreneurial activities in Georgia. Lack of working capital is one such major issue. Georgian small and medium enterprises (SME) suppliers are commonly required to provide trade credit to their large buyers and to hold accounts receivable on their balance sheets. This creates funding problems to SMEs that typically lack cash flow and may have difficulties accessing other sources of funds. Developed markets have established a highly efficient solution to face the problem, namely, factoring, which can help suppliers since it allows relatively easy and quick access to working capital by SMEs.

The Georgian legislation in force does not contain any detailed provisions on factoring, except for a brief mention of factoring in the Georgian Banking Law and several less noteworthy regulations, which broadly define factoring as a trade finance transaction[1] where the financing of a client's working capital includes a collection of accounts receivable, lending against accounts receivable, guaranteeing foreign exchange and credit risk. The Banking Law does not define different permutations of factoring services and only mentions that factoring services can be offered with or without recourse.

Georgian factoring companies do not require any license or permit if they are properly registered with the Registry of Entrepreneurial and Non-Entrepreneurial (Non-Commercial) Legal Entities (Entrepreneurial Registry) maintained by the National Agency of Public Registry of the Ministry of

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[1] Article 1.p., Law of Georgia on Activities of Commercial Banks, 23/02/1996.

Justice of Georgia. There is no specific supervisory body or regulatory mechanism of Georgian factoring companies. As factoring is not regulated, there are no limitations on the types of receivables subject to factoring.

Therefore, proper regulation of factoring is on the agenda along with the establishment of the scope of the relevant legislation to ensure stability of the market and legal efficiency of the transactions, while not putting undue regulatory burden on the industry.

Thus, it is desirable to encourage the development of factoring services by guaranteeing stability and legitimacy of the industry (ensuring that market players are well-established commercial entities capable of meeting certain regulatory requirements) as well as by raising legal certainty of factoring transactions.

According to international experience, the legal framework for factoring lies in the combination of the following three key elements: (i) the legal rules governing commercial contracts and assignment of receivables; (ii) the legal act establishing a regulatory framework and regulatory body with a mandate to regulate or supervise factoring; and (iii) the tax code and accounting rules and their application to factoring transactions and companies.[2]

2. Overview of Factoring Market in Georgia and the Advantages of Factoring

As Georgian law does not properly define and regulate factoring, there is no surprise that Georgian factoring market is currently underdeveloped and respective services are offered in a very limited volume. Currently, factoring operations in Georgia are mostly conducted by commercial banks, as most comprehensive regulation of factoring available at the moment is provided in 1996 Law of Georgia on Activities of Commercial Banks. Factoring, without being further defined is also a type of permitted activity for microfinance organizations pursuant to 2006 Law of Georgia on Microfinance Organizations.[3] However, to the best of our knowledge, microfinance organizations in Georgia refrain from entering this segment, which is locally an unregulated field of financial activities and largely unknown.

For conducting factoring operations, respective service providers are not required to obtain any licenses, certifications or authorizations. Factually, the right to act in the capacity of a factor is granted to all Georgian commercial banks and microfinance organizations by virtue of respective banking license (applicable in relation to commercial banks) and registration with National Bank of Georgia (applicable in relation to microfinance organizations). Other types of commercial legal entities can theoretically also provide factoring services as such activity is not subject to specific licensing or permitting under 2004 Law of Georgia on Licenses and Permits. However, lack of regulation excludes participation of commercial legal entities, other than commercial banks and microfinance organizations from factoring operations.

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2 Comp.: Southeast Europe Enterprise Development, for the Establishment of Factoring Company in Bosnia and Herzegovina, 2007, 8, <http://documents.worldbank.org/curated/en/440521468199442423/pdf/375110ENGLISH01ing1company01PUBLIC1.pdf>, [28.09.2018].

3 Article 4.1.h., Law of Georgia on Microfinance Organisations, 18/07/2006.

Having conducted respective research of factoring market in Georgia, we can state that main providers of respective services are several commercial banks. In absence of proper legal framework for factoring in Georgia, these players of factoring market mainly rely on various sources of international regulation of factoring such as 1988 *UNIDROIT* Ottawa Convention on International Factoring, *UNCITRAL* Legislative Guide on Secured Transactions, other similar sources and best international practices in general.

Therefore, a brief overview of the advantages of factoring is not uninteresting to the reader.[4] For example:

- Speaking about general advantages of factoring, first we can emphasize facilitating access to finance for SMEs. Factoring provides a quick boost to cash flow. This may be very valuable for businesses that are short of working capital. If done without recourse, factoring allows cash-strapped SMEs to increase their cash holdings and improve their balance sheets without taking on additional debt;
- Furthermore, proper regulation of factoring market leads to development of this industry and the more companies are conducting factoring transactions, the more competitive applicable service fees/ prices become;
- Factoring also assists smoother cash flow and financial planning. It is noteworthy that some customers may respect factors and pay more quickly;
- Factors may give useful information for businesses about the credit standing of their customers and can further help them to negotiate better terms with suppliers;
- It is believed that factors can prove an excellent strategic – as well as financial – resource when planning business growth;
- Businesses would be protected from bad debts if they choose non-recourse factoring;
- Generally, the cash is released as soon as orders are invoiced, and such cash is available for capital investment and funding of next orders; and
- Factors will credit check the customers of applicable entrepreneurs and can help them trade with better quality customers.

3. Factoring Operations

In general, a factoring relationship is based on a contract between a client (supplier) and a factoring company. The contract usually starts with a preamble which defines the scope of the contract, its objectives and goals. This is followed by the main body of the agreement, which specifies the client's duty to offer (deliver) claims arising from supply (purchase, service) contracts, to the factor and the factor's duty to buy these claims (and conditions to be fulfilled in order for that obligation to arise).[5] In this context, terms of payment, provisions on interest, allocation of risk (with or without

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4 Comp.: *Klapper L.*, The Role of Factoring for Financing Small and Medium Enterprises, 2007, 6-7, <http://siteresources.worldbank.org/INTEXPCOMNET/Resources/Klapper,_The_Role_of_Factoring_for_Financing_Small_and_Medium_Enterprises.pdf>, [28.09.2018].

5 *Orheian O. M.,* The Advantages of Using Factoring, as Financing Technique on International Transactions Market, The Annals of "Dimitrie Cantemir" Christian University, Economy, Commerce and Tourism Series, Vol. 9, 2012, 105-106.

recourse), services to be provided by the factor (maintenance of accounts, insurance, provision of information, etc.) and bank accounts involved in the transaction are particularly specific. At the end of the contract, there are provisions on the obligation to provide information, negative pledge clauses, and terms of agreement, contractual penalties, notices and jurisdiction in the case of dispute (usually arbitration).

Once the contract is signed, a typical factoring cycle consists of the following steps:[6]

(1) The client sells goods or provides services to the customer in the ordinary course of business;

(2) The client invoices the customer and sends a copy of the invoice to the factor, who then takes over sales ledger administration;

(3) The factor applies credit control procedures. Once satisfied, it advances funds to the company at a discount (usually around 80% of gross invoice value);

(4) The factor collects the debt from the customer when it is due; and

(5) Once monies are received from the customer, the factor deducts an amount equal to the funds advanced to the company, the interest accrued on the daily outstanding balance of those funds and retains its fees. The balance is released to the client.

There are typically two costs involved,[7] viz., a service charge expressed as a percentage of sales factored, and an interest charge for the cash advances. The service charge (commission), covering sales ledger management and collections services, usually ranges up to 3.0% of turnover. The primary considerations in determining the service charge are annual turnover, number of invoices and number of customers. The interest charges calculated on the daily usage of funds are typically comparable to secured bank overdraft rates.

4. International Standards for Factoring Services

In light of the 2013 Association Agreement between the EU and Georgia which, among other topics, implies harmonization of local legislation with EU standards, regulation of factoring at EU level could have been a major source for introducing new legislation in Georgia. However, since the factoring sector is not regulated by the EU, there is no comprehensive established definition of factoring at the EU level. Factoring is only mentioned as a service in several directives regulating credit and other financial institutions (e.g. EEC Directive 89/646 on the annual accounts and consolidated accounts of banks, etc.).[8]

The 1988 UNIDROIT Ottawa Convention on International Factoring (currently in force in nine countries) defines a factoring contract as a contract concluded between one party (the supplier) and another party (the factor) pursuant to which: (a) the supplier may assign to the factor receivables aris-

6 *Bakker M. H. R., Klapper L., Udell G. F*., Financing Small and Medium-size Enterprises with Factoring: Global Growth in Factoring — and Its Potential in Eastern Europe, Warsaw, 2004, 6.

7 *Tatge D. B., Tatge J. B.,* Fundamentals of Factoring, Journal Practical Law, September, 2012, 65.

8 EU Second Council Directive 89/646/EEC on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions and amending Directive 77/780/EEC, 15/12/1989.

ing from contracts of sale of goods; and (b) the factor performs at least two of the following functions: (1) finance for the supplier; (2) maintenance of accounts (ledgering) relating to the receivables; (3) collection of receivables; and (4) protection against default in payment by debtors.[9]

Examples of legal definitions of factoring can be found in the national legislation of several European countries as well. For example, the German Banking Act (*Kreditwesengesetz*) defines factoring as the continuing acquisition of receivables on the basis of master agreements, with or without recourse,[10] while the Latvian Commercial Code defines factoring as a contract under which one contracting party undertakes an obligation to acquire receivables of a client against a third person (debtor) as well as to fulfil other commitments specified in the factoring contract to another contracting party for the agreed remuneration.[11]

In the absence of universal legal definitions, an analysis of general terms and conditions of factoring contracts used by factoring companies around the world indicates that factoring is a complex partnership agreement, covering a range of business services, commission fees, assignments and loan assumptions, customer research, accounting, billing and collections.[12]

From these various sources, it can be concluded that the core of factoring is a contractual relationship involving (a) a Supplier of goods and services, and (b) a factor to which the supplier sells (assigns) existing or future receivables arising from contracts of sale of goods or services made between the supplier and its customers (the Debtors), who are duly notified of the factoring contract.

The factor usually performs at least two of the following functions:

1) Provides finance for the supplier, including advance payments, through the purchase (transfer, assignment) of the receivables;

2) Maintenance of accounts (ledgering) related to the receivables;

3) Collection of the receivables; and

4) Provides protection against default in payment by debtors due to the debtors' inability to pay.[13]

5. Elements of Factoring

A factoring transaction implies several key elements which should be considered in the process of defining this financial service. Specification of the type of factoring, determination of whether the transfer of receivables represents a sale of receivables or a security agreement, implications of transfer

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9 Chapter 2, UNIDROIT Convention on International Factoring, Ottawa, 28/05/1988.

10 §1, Punkt 1a, Nummer 9, Gesetz ueber das Kreditwesen (Kreditwesengesetz), 09/09/1998, <https://www.bundesbank.de/Redaktion/DE/Downloads/Aufgaben/Bankenaufsicht/Gesetze_Verordnungen_Richtlinien/gesetz_ueber_das_kreditwesen_kwg.pdf?__blob=publicationFile>, [28.09.2018].

11 Sec. 468, Commercial Code of Latvia, 04/05/2000.

12 Comp.: *Klapper L.*, The Role of Factoring for Financing Small and Medium Enterprises, 2007, 5, <http://siteresources.worldbank.org/INTEXPCOMNET/Resources/Klapper,_The_Role_of_Factoring_for_Financing_Small_and_Medium_Enterprises.pdf>, [28.09.2018].

13 Comp.: *Institute of Chartered Accountants in England and Wales*, The Finance Function: A Framework for Analysis, 2011, 41, <https://charteredaccountantsworldwide.com/wp-content/uploads/2016/09/Developing-effective-finance-functions-for-the-unique-contexts-within-which-they-operate.pdf>, [28.09.2018].

of future receivables, defining the scope of factoring as well as distinguishing between factoring and non-factoring forms of receivables finance can be regarded as such key elements.

5.1. Types of Factoring

Various forms of factoring may arise when some, but not all, of the previously mentioned four functions are provided. The industry has developed various types of factoring contracts and these are commonly grouped together on the basis of three criteria: transfer of risk, places of business of the concerned parties and whether the debtor is notified.

Hence, according to those criteria, factoring transactions can be classified as:

1) Non-recourse and recourse factoring;
2) Domestic and international factoring; and
3) Disclosed (notified) and silent factoring.

In addition, current practices include an additional type of factoring in which the factor's client is the debtor and not the supplier creditor. This model of factoring is referred to as reverse factoring.[14]

5.1.1. Non-Recourse and Recourse Factoring

In non-recourse factoring, the lender not only assumes title to the accounts, but also assumes most of the default risk because the factor does not have recourse against the supplier if the accounts default. The factor may choose to pass on the credit risk by taking out credit insurance against non-payment of the debts. This type of factoring is also sometimes referred to as real, complete or standard factoring.[15]

Under recourse factoring, the factor has a claim against the seller for any account payment deficiency. Therefore, losses occur only if the underlying accounts default and the seller cannot make up the deficiency.[16]

5.1.2. Domestic and International (Export) Factoring

A major difference between domestic and international factoring is that domestic factoring involves parties which operate in a single legal system and use local currency, while the parties to international factoring operate in more than one legal system and in foreign currencies.

International (export) factoring covers the exporter's accounts receivable arising from cross-border deliveries of goods or services. International factoring can be organized through a two-factor system or as direct (import and export) factoring.[17]

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[14] *Regenbogen I*., Reverse Factoring – Funding the Un-Fundable, Romanian Review of Private Law, Vol. 2, 2017, 115.

[15] Comp.: *Allegiant Business Finance*, Factoring Guide, 2016, 3, <https://www.allegiant1.com/wp-content/uploads/2016/09/FactoringGuide.pdf>, [28.09.2018].

[16] Comp.: *Ivanovic S., Baresa S., Bogdan S.*, Factoring: Alternative Model of Financing, UTMS Journal of Economics, № 2(2), 2011, 193.

Under the two-factor system, one company acts as the export factor – dealing with financing, credit management, sales ledger accounting, or a combination of these services – in the supplier's country. A second company, the import factor, handles credit cover and collection in the buyer's territory. Thus, functions and risks are divided between the import factor and the export factor. The main goal of this model is to use local credit and collection knowledge and to limit administrative costs. Factors usually establish cross-border business relationships through memberships in international factoring groups, which enable them to work effectively together in offering a total service to the end-user.

In the case of direct factoring, the accounts receivable are assigned to a factor located either in the export or import country. A problem with direct export factoring is that the factor in the exporting country can be faced with significant difficulties with the credit function (verification of solvency) and collection of claims, as the factor may lack local information and expertise. Import factoring, in which the receivables are assigned to the factor in the import country, is a more straightforward option than export factoring. However, if the client is operating in many countries simultaneously, this model could raise overall costs of transactions as the client needs to find suitable factors in each import country. Therefore, the two-factor system, in which the client enters into a single relationship with the home factor, may be a more convenient option.

5.1.3. Disclosed (Notified) and Silent Factoring

Factoring can be defined as disclosed or silent, depending on whether the debtor is informed about the assignment of the claim. Some experts consider this theoretical division to be obsolete, as most jurisdictions require a notice to be sent to the debtor, either to validate the assignment, or at least to make it opposable to the debtor (obliging the debtor to pay the factor).[18] Therefore, silent factoring has practical use only if both the credit and collection functions are left with the client, in which case, we then have in fact an invoice discounting type of transaction. This form of financing is very popular in the United Kingdom, especially with larger companies that can afford the staff and information systems to efficiently manage and collect outstanding invoices.[19]

5.1.4. Reverse Factoring

Instead of entering into a contract with the supplier (creditor) as in a usual factoring agreement, under the reverse factoring scheme, the client of the factoring company is the buyer (debtor). This type of factoring product is also known as confirming (e.g. Spain) and sometimes as supply chain finance.[20]

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17 *RAI University*, Factoring — Theoretical Framework, 2011, 90, <http://psnacet.edu.in/courses/MBA/Financial%20services/5.pdf>, [28.09.2018].

18 Comp.: *Farrenkopf M.*, Corporate Finance Instrument: Single-Factoring and Sales of Defaulted Accounts (at the example of car dealers and repair service in Germany), Saimaa University of Applied Sciences, South Korea, 2014, 20.

19 Ibid.

20 *Kouvelis P., Dong L., Turcic D.*, Supply Chain Finance: Overview and Future Directions, Supply Chain Finance, *Kouvelis P., Dong L., Turcic D.* (eds.), US, 2017, 3.

Eligible clients are usually large companies with strong market presence and many suppliers (e.g. large retailers). Instead of the assignment of receivables, the underlying legal relationship in reverse factoring is essentially assumption of the client's debt and subrogation of the supplier's claim by the factoring company.[21]

One of the advantages for clients in reverse factoring is in the possibility of decreasing administrative and processing costs by effectively outsourcing the payment department, i.e., the buyer makes one payment to a factor rather than to multiple suppliers. In addition, by providing suppliers with timely working capital financing, buyers can also improve their reputations and relationships with suppliers and still keep their working capital cycle based on deferred payments.

Essential to any reverse factoring scheme is the buyer's acceptance of the payment obligation and therefore close co-operation with the buyer. In this respect, an enforceable agreement is mandatory. Factoring companies and buyers usually enter into a mid to long-term framework agreement, setting the terms and conditions for the acceptance and advance payment of the buyer's accounts payable.

5.2. Sale of Receivables

In discussions on the legal nature of the transfer of receivables in a factoring agreement, much attention has been paid to whether the transfer in recourse factoring represents a sale of receivables from the client to the factor company or a security assignment.

Currently, there are three prevailing theories: purchase-contractual theory, commission-contractual theory and loan-contractual theory.[22] Special attention has to be given to the loan–contractual theory, due to the possible consequences of its application on recourse factoring. This theory essentially defines recourse factoring as a secured loan transaction (by security assignment), with the collateral being transferred accounts receivable. Apart from the risk of making such transactions void if requirements for establishing collateral were not met (e.g. registration), such an interpretation may create additional risks as factored receivables may become part of the bankruptcy estate of the debtor in the case of insolvency. This question is especially relevant in those jurisdictions where inefficient bankruptcy regulations or priority rights of groups of preferential creditors in insolvency proceedings might dilute the value of the security over the accounts receivable.

Considering potential consequences of the application of such a definition, special attention has to be paid to a clear definition of the nature of the transfer of receivables when legislating factoring.

5.3. Transfer of Future Receivables

Future receivables are a potentially important source of factoring and should be included in any definition of factoring. When a commercial relationship is stable, the future cash flow from product

[21] Comp.: *Klapper L.*, The Role of "Reverse Factoring" in Supplier Financing of Small and Medium Sized Enterprises, 2004, 9-10, <https://www.factoring-mittelstand.de/19_experinces.pdf>, [28.09.2018].

[22] Comp.: *Kettering K. C.,* True Sale of Receivables: A Purposive Analysis, 2009, 514-515, <https://www.researchgate.net/publication/228220314_True_Sale_of_Receivables_A_Purposive_Analysis, [28.09.2018].

delivery may be considered reliable, so a supplier may wish to factor these future receivables and a factor may wish to purchase these receivables. This is a common practice, which increases the flexibility of factoring as a financing instrument.[23]

5.4. Scope of Factoring

The scope of factoring is usually limited to commercial/trade receivables and does not include consumer receivables (contracts for the sale of goods and services bought by individuals primarily for personal, family or household use). However, by some definitions, receivables arising from consumer services, such as utility or telephone bills, can be factored. In the United States, there are no restrictions, and receivables for any goods or services, regardless of the type of debtor, can be factored.[24] In some countries, a governmental or publicly-owned entity may not be a debtor in a factoring transaction.

It is also advisable to limit factoring services to the purchase of accounts receivable originating from trade to make sure that the developing industry stays focused on trade finance. Otherwise, there is a risk of the industry being misunderstood by its users (SMEs) and commingling with other types of financing usually not considered factoring, e.g., investing in non-performing loans (the NPL). This can have negative consequences for the reputation of the factoring industry that is usually misunderstood as a collection service or NPL management, which keeps SMEs away. This is usually done by defining receivables eligible for factoring as receivables which are still not due and payable (or exceptionally if already due, then to refinance them for a maximum one year) and which arise from sale of products and provision of services. In case this would be necessary in a particular jurisdiction, a law could provide more detailed description of what is considered trade and service provision, as well as to explicitly exclude NPLs.

5.5. Non-Factoring Forms of Receivables Finance

Factoring is one, but not the only, form of receivables financing. There are other forms of receivables financing that should not be confused with factoring. These include:

(1) Forfeiting, which involves the purchase or discounting of documentary receivables (promissory notes, for example) without recourse to the party from whom the receivables are purchased. Forfaiting involves financial rather than commercial transactions, and does not have the same collection properties, so it is not typically an activity of factoring companies. The terms factoring and forfaiting have been frequently confused. Factoring is suitable for financing several different smaller claims for consumer goods with credit terms up to 360 days, whereas forfaiting is used to finance capital goods exports with credit terms between a few months and seven years. It is noteworthy that 1996 Law of

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[23] Comp.: *Akseli O.*, Turkish Law and UNCITRAL's Work on the Assignment of Receivables with a Special Reference to the Assignment of Future Receivables, Law and Financial Markets Review, Vol. 1, Issue 1, 2007, 47.

[24] Comp.: *Tatge D. B., Flaxman D., Tatge J. B.*, American Factoring Law, American Bankruptcy Institute, 2009, 44-46, <https://www.bna.com/uploadedfiles/abi_journal_review.pdf>, [28.09.2018].

Georgia on Activities of Commercial Banks duly (although superficially) defines forfaiting separately from factoring;[25]

(2) Refinancing, which involves the assignment of receivables against some form of bank or other credit granted to the assignor;

(3) Securitization, which can involve issuance of securities backed by commercial receivables of various types, which are purchased by the securitization company (the issuer of the securities) from the commercial entity which originated the receivables; and

(4) Project finance, which involves loans to project contractors which are secured by future revenues generated by the project.

6. Currents Status of Factoring in Georgia

The most significant provisions of Georgian law in relation to factoring are provided in 1996 Law of Georgia on Activities of Commercial Banks, which broadly defines factoring as a trade finance and commission transaction relating to crediting of a client's working capital and encompassing the collection of the client's receivables as well as the credit and currency risk guarantees. The law does not define different permutations of factoring services. In particular, pursuant to Article 20 of 1996 Law of Georgia on Activities of Commercial Banks, such credit institutions may, among others, conduct factoring operations with and without the right of recourse.

Along with the banking law, factoring is mentioned in the 2006 Law on Microfinance Organizations (and related bylaws) as one of the types of activities which might be performed by microfinance organizations. Moreover, 2010 Georgian Tax Code considers factoring as one of the types of financial services/instruments.[26] Factoring is further mentioned in several less significant regulations. However, in all applicable pieces of legislation, factoring lacks a clear and comprehensive definition. As repeatedly stressed by representatives of Georgian legislative and executive power, commercial legal entities and international experts, Georgian legislation would benefit from exhaustive regulation of this form of financial service, including, but not limited to, defining specific types of factoring such as international factoring, reverse factoring, factoring of future receivables, etc.

Regulation of factoring market would increase legal certainty and support factoring service providers with developing new factoring products.

7. Proposal of Definition

7.1. Essence of Factoring

Based on international experience, it is desirable that factoring is defined as a legal transaction of purchase of existing or future short-term, non-matured receivables (with payment period up to 360 days) arising from a contract on the sale of goods or provision of services and conducted on repetitive basis.

[25] Article 1.s., Law of Georgia on Activities of Commercial Banks, 23/02/1996.
[26] Article 15.2.c., Tax Code of Georgia, 12/10/2010.

At the same time, reverse factoring might be defined as a special type of factoring based on a three-part contractual relationship between factor, client (debtor) and supplier (creditor), whereby the factor assumes existing or future short-term non-matured payables arising from a contract on the sale of goods or provision of services between the client and supplier, and undertakes to pay the assumed debt on call from the creditor for consideration (discount and factoring fee) before its maturity, being reimbursed the full value of the assumed debt by the client on maturity of the assumed debt.

7.2. Subject of Factoring

Pursuant to well established concepts of international financial law, subjects of factoring may be any existing or future, entire or partial, matured or non-matured short-term receivable arising from a contract on a sale of goods or provision of services.[27] A future receivable may be subject to factoring. A future receivable shall be deemed to be sufficiently defined if the factoring contract indicates the debtor under such receivable.

In addition to purchasing receivables, the factoring company may undertake to perform the following services:

1) Keeping records of and ledgering transferred receivables;
2) Collecting receivables; and
3) Assuming the risk of collecting transferred receivables.

7.3. Types of Factoring

Based on the location where a receivable is collected, factoring may be domestic or international. Based on the obligation to undertake the risk of collecting a receivable (*del credere* function) factoring can be with or without recourse.

(1) Domestic Factoring

It is recommendable to define domestic factoring in Georgia as factoring, the object of which is the transfer of receivables arising through the sale of goods or provision of services between domestic legal or natural entities.

(2) International Factoring

Desirable definition of international factoring would imply factoring, the object of which is the transfer of receivables arising through foreign trade in goods or services. International factoring may involve a one-factor system, in which the factor undertakes to collect, through its own agency, a receivable from a debtor domiciled abroad; or a two-factor system, in which the factor transfers a receivable or assumes a debt from another factor domiciled abroad in accordance with the terms and conditions of the factoring contract and the factoring law.

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[27] Comp.: *EU Federation for Factoring and Commercial Fianance*, Factoring and Commercial Finance: An Introduction, 2017, 3, <https://www.intermarket.at/content/dam/at/intermarket/common/files/intro% 20to% 20factoring.pdf>, [28.09.2018].

(3) Non-Recourse Factoring

Factoring without recourse shall entail the factor assuming the risk of collecting a receivable (including insolvency, bankruptcy and liquidation risk). The client shall be liable to the factor for the existence of a receivable; however, he/she shall not be responsible for the success of the collection (credit worthiness).

(4) Recourse Factoring

Under factoring with recourse, the factoring client (assignor) shall jointly and severally guarantee the successful collection of the transferred receivable. Where factoring with recourse has been provided for in the factoring agreement, the factoring client (assignor) shall be liable to the factor for the existence of a receivable, and for the collectability of a receivable as of the date the receivable becomes due.

Where the factor has exercised recourse, the factor may require that the client refund the advance payment increased by the amount of contractual interest, fees and expenses. Recourse factoring should not be characterized as a secured transaction. It is a form of title finance and should be treated as such. In contrast to collateralized loans, in a factoring transaction, the transfer of the receivable is the purpose of the transaction and not a guaranty for debt repayment. It is the value (solvency) of the transferred receivable that is guaranteed by the general right of recourse (claim) against the factoring client. In order to avoid negative implications of potential re-characterization of factoring with recourse into secured transaction (such as nullity, onerous enforcement restrictions, bankruptcy freezes, conflicts with negative pledge clauses, etc.), it is important that a clear and straightforward definition of the common types of factoring be included in national legislation.

(5) Bills of Exchange Discounting

The factor can engage in the practice of discounting of bills of exchange as long as the bill of exchange originates (represents a receivable) from the underlying transaction of sale of goods or provision of services. For regulating factoring in Georgia, discounting of such bills of exchange should be considered as purchasing the underlying receivables.

8. Factoring Legal Framework

Factoring has developed in a variety of legal and regulatory settings specific to the individual country in which factoring services are provided. However, factoring is almost universally understood as a combination of three contractual relationships: 1) framework agreements (setting conditions for assignments, services to be provided, fees, etc.); 2) contract on sale (or sometimes seen as a commission contract or even a loan); and 3) assignment of receivables (as a discharge of sale or provision of security for the loan).

The assignment of receivables lies at the heart of every factoring operation, and all European jurisdictions have more or less detailed laws regulating this practice. There are differences in the approach to assignment of rights (formal steps, opposability to a third party, assignment of future rights, etc.), but despite those differences it is safe to say that receivables can be more or less effectively assigned throughout Europe.

When analyzing the legal environment for factoring, special attention should be paid to the provisions regulating the form of the factoring agreement, assignability (and legal characterization of assignment) of accounts receivable; notification requirements, assignment of future receivables, contractual prohibitions on assignments, and third-party rights affecting factoring.

8.1. Factoring Contract

A factoring contract between a factoring firm and a client is a framework agreement regulating all aspects of the factoring relationship (e.g. type of factoring, recourse rights, provision of additional services, present and future assignments, etc.). It is the basis for provision of factoring services. It is structured as a revolving factoring facility (under which numerous individual accounts receivable are factored).[28] In practice, almost all factoring is performed on the basis of written factoring agreements.

8.2. Assignment

8.2.1. Assignment Form and Requirement of Notification

While a factoring agreement is a framework contract regulating all aspects of a factoring relationship between the factoring company and its client, assignment is the method by which transfer of receivables from a client to a factoring company is achieved.

European practice varies regarding the prescribed form of individual assignments.[29] Whereas in some countries such as Greece, Latvia and Portugal, the law requires assignments to be made in writing, assignment agreements in countries such as Malta and Sweden are not required to be in a specific form.[30] An informal approach to assignment is preferred, since a written form could increase the risk of assignments performed by electronic means.

In some jurisdictions (e.g. Norway and Czech Republic) notification of the debtor of the assignment is a legal requirement for the validity of assignment.[31] Factoring companies in other countries (e.g. Great Britain, Poland and Portugal) need to notify the debtor not to make the assignment legally valid, but only to ensure that the debtor can discharge the debt by paying the factoring company only.

Notification should not be mandatory for the validity of the assignment. Such approach fully corresponds to respective provisions of Georgian Civil Code regulating assignment of claim.[32] This allows companies to offer the service of silent factoring and reduces the risk of procedural errors during assignment. Furthermore, the law should support the validity of general notification that would include the assignment of future receivables (thus avoiding the need to notify each assignment specifically).

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28 Comp.: *Dogaru D. -M., Bratiloveanu I.,* Factoring Contract — Short Term Financing Technique, 2016, 29, <http://cis01.central.ucv.ro/revistadestiintepolitice/files/numarul52_2016/3.pdf>, [28.09.2018].

29 Comp.: *Milenkovic-Kerkovica T., Dencic-Mihajlov K.,* Factoring in the Changing Environment: Legal and Financial Aspects, Procedia — Social and Behavioral Sciences, № 44, 2011, 433.

30 Ibid, 434.

31 Comp.: *European Bank for Reconstruction and Development*, Factoring Survey in EBRD's Countries of Operation, 2018, iv, <https://www.ebrd.com/documents/ogc/factoring-survey.pdf>, [28.09.2018].

32 Article 199, Civil Code of Georgia, 26/06/1997.

8.2.2. Assignment of Future Receivables

The possibility of assigning future receivables is an important feature for the factoring industry, as this enables establishment of long-term factoring relationships and may protect a factors' priority in case of competing claims. The majority of European countries allow for the possibility of assigning future claims. It is usually required that receivables and/or the debtor are determined or specified with sufficient precision for a future assignment to be valid.

For example, in Austria, a necessary requirement for the validity is the concretization and individualization of the claim.[33] This requirement is met, if, for example, all receivables arising in the business of the assignor are assigned. Whether the prospective debtor is known is not relevant as far as determination is possible. While the actual assignment cannot happen before the receivable is in legal existence, the framework agreement on the assignment can be made in advance. Whenever these receivables come into existence, they are automatically assigned to the assignee without a requirement for any further actions. Similar regulations can be found for example in Spain or Germany but with an additional requirement of identification of the future debtor.[34]

8.2.3. Ban on Assignment by Virtue of a Contract

Contracts between small businesses acting as suppliers to large companies that dominate the market usually contain provisions prohibiting the assignment of receivables to third parties. This, in combination with long payment terms, may put such suppliers in a disadvantageous position, making it impossible for them to seek working capital from financial markets based on their accounts receivable.

There is no clear solution to this situation, as this is a typical example of conflict of legitimate interests. Should legislation governing factoring restrict freedom of contract by making it possible for receivables to be assigned even where contracts do not allow it? Is such an approach justified, and, if so, should it be governed by factoring legislation? Might it not be more appropriate to regulate this field through laws on competition?

Article 6 of the 1988 *UNIDROIT* Ottawa Convention on International Factoring stipulates that the assignment of a receivable by the supplier to the factor shall be effective, notwithstanding any agreement between the supplier and the debtor prohibiting such assignment. However, such assignment shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, it has its place of business in a contracting state which has made a declaration under Article 18 of this convention.

1988 *UNIDROIT* Ottawa Convention on International Factoring, therefore, stipulates that any prohibition of assignment of receivables is to be deemed null and void, but nevertheless provides for possible exceptions to this rule. It should, however, be borne in mind that the convention deals with international factoring, which entails cross-border assignment of receivables and differing legal sys-

[33] Comp.: *Bakker M. H. R., Klapper L., Udell G. F.,* Financing Small and Medium-size Enterprises with Factoring: Global Growth in Factoring — and Its Potential in Eastern Europe, Warsaw, 2004, 23.

[34] Comp.: *Milenkovic-Kerkovica T., Dencic-Mihajlov K.,* Factoring in the Changing Environment: Legal and Financial Aspects, Procedia — Social and Behavioral Sciences, № 44, 2011, 343.

tems and powers. It reflects its own specific logic and rationale as well, especially regarding reducing information asymmetry, harmonizing legal rules and reducing regulatory risk.

In many European jurisdictions, contractual prohibitions on assignments are tolerated, possible and legally valid. However, the effects of such contractual prohibitions on factoring vary and range from the contractual prohibition having no effect whatsoever on the assignment and the factoring relationship (for example, in Austria, or in Italy, where a special law on factoring renders such contractual provision unenforceable) to the contractual prohibition rendering any assignment null and void and therefore making factoring in such cases practically impossible (e.g. in Spain, Czech Republic or Bulgaria).

The traditional reasons for allowing contractual freedom to prohibit assignments (the ability to control who your creditor is) are not valid in the case of factoring, since the assignees in factoring are legitimate companies offering legitimate, internationally recognized financial services. This argument becomes even more valid in jurisdictions where a certain level of regulation over the factoring industry already exists.

8.2.4. Priority Rights in Assigned Receivable

The extent to which competing rights can affect the factoring company as an assignee varies. It depends on the legal rights of a third party (e.g. conflict of several assignments over the same receivable, pledges over the assigned receivable or purchase of money security interests) as well as on how priorities are regulated in a particular legal system.

Rationales for determining the priority of competing claims differ among various jurisdictions, but the solutions are usually formed around several basic principles:[35]

The first-in-time rule: The first party to sign a valid assignment agreement is protected, because from that moment on the transferor has no right to assign or to pledge something that he/she no longer owns. Therefore, any such disposition is not valid. The difficulty in this system lies in proving the date of the valid assignment, especially if no formalities are required.

The best title rule: The first one to register, if registration of assignment is required, or the first one to notify the debtor. The problem here is proof of perfection, i.e., who notified the debtor first.

Austria is an example of a jurisdiction that deals with priorities according to the first in time rule. Under Austrian law, if several assignments of one receivable conflict, the first assignment in time is valid and all further assignments will be considered void as the assignee cannot transfer more rights than it de facto holds. Similar laws apply in Belgium, Czech Republic, Italy or Germany.[36]

On the other hand, in Bulgaria, the best title principle has been the basis for regulation of priorities. The notification of the debtor is mandatory for the assignment to be opposable to the debtor and to third parties (similar principles are applied in Ireland).[37]

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35 Comp.: *Nishtani Y.*, Cross-Border Assignments of Receivables, Japan, 2017, 3-4.

36 Comp.: *UK Factoring Association*, International Factors Group, Receivables Finance & ABL, A Study of Legal Environments across Europe, 2007, 23, 32, 36, 77, <http://www.abfa.org.uk/members/newsletter/EU-LegislationReport.pdf>, [28.09.2018].

37 Comp.: *The British Institute of International and Comparative Law*, Study on the Question of Effectiveness of an Assignment or Subrogation of a Claim against Parties and the Priority of the Assigned or Subrogated

Romania is another example of a jurisdiction that bases the rules of priority on the best title principle. However, Romanian authorities have taken a somewhat different and perhaps unusual approach compared to other European jurisdictions. For the assignment to be opposable against third parties in Romania, it has to be registered with the electronic archive of pledges. In the case of successive transfers, the assignee who registered his/her transfer first shall have priority, no matter whether he/she knows about the existence of other transfers.[38]

However, regardless of the principle on which priority rules are based, when examining the conditions for performing factoring in a particular jurisdiction, one should investigate whether the system allows for easy and certain determination and protection of priority positions of the assignees, in this case, factoring companies.

9. Georgian Legal Framework

In absence of proper definition of factoring under Georgian law, there is no surprise that local legislation does not regulate factoring agreement to any extent. It is proposed that the new factoring law should not only define factoring, but also introduce a definition of the factoring contract as well as define the parties and their duties and rights.

Taking into account the legal realities in Georgia, it is recommendable that factoring can be provided only on the basis of a written factoring agreement, in the following manner: Under a factoring agreement, the factor undertakes to purchase existing or future short-term non-matured receivables (up to 360 days) arising from a contract on the sale of goods or provision of services.

Parties to the factoring agreement are the factor (a credit institution in accordance with applicable laws and a factoring company providing factoring services), the client (a legal entity or individual selling accounts receivable) and the debtor (of sold accounts receivable).

A factoring agreement shall contain, in particular, information on the parties to the agreement; an indication of the type of factoring to be conducted, grounds for and information about the receivable that is the subject of the agreement, the amount and manner of calculating the factoring fee, the interest rate and other potential expenses.

10. Assignment of Claims

Transfer of receivables as execution of sale for the purposes of performing factoring is regulated by the provisions of the law regulating assignment (cession) of claims. According to Georgian Civil Code, the assignment of a claim is effected by a contract concluded between the creditor and a third party.[39] The contract does not have to be in a specific form, unless specifically requested by the as-

Claim over a Right of another Person, 2011, 338, <http://edz.bib.uni-mannheim.de/daten/edz-k/gdj/12/report_assignment_en.pdf>, [28.09.2018].

38 Comp.: *UK Factoring Association*, International Factors Group, Receivables Finance & ABL, A Study of Legal Environments across Europe, 2007, 104, <http://www.abfa.org.uk/members/newsletter/EU-LegislationReport.pdf>, [28.09.2018].

39 Article 199, Civil Code of Georgia, 26/06/1997.

signee. Until the debtor is notified of the assignment of the claim, he/she is entitled to pay to the assignor. If the assignor has agreed on the assignment of one and the same claim with a number of persons, then the person with whom the assignor entered into relations first shall be entitled to the claim. If this cannot be determined, then priority shall be given to the person notified to the debtor earlier. The assignor is obligated to hand over all documents in his/her possession with respect to the claims and rights, as well as all information that is required for use of these claims and rights, to the assignee.

Since there is no specific requirement for the written form of assignment, receivables can be validly assigned using electronic data exchange messages. Electronic signature is regulated, but it is not widely used in Georgian practice. Registration is not required for the validity of assignment and no stamp duty applies.

Analysis of Georgian legislation makes clear that contractual prohibition against assignment of receivables is permitted. A breach of such provision deems the assignment invalid.

There are no specific provisions on the assignment of future debt. However, it is considered that, from the perspective of contract law, there is no obstacle to assigning future debts as long as the debt is identifiable (the debtor has to be known, as does the relationship out of which the debt will arise). Confirming and reinforcing future assignments and general notices on future assignment might be a welcome change to the factoring services industry.

Provisions confirming this possibility and allowing for general notification of future assignments would be welcome. The assignment of receivables may be contractually prohibited and an assignment in contradiction with such a term would be effective towards the debtor. Parties should be free to agree on the recourse right of the assignee (factor) against the assignor (client).

There are no special provisions on electronic factoring. However, due to lack of requirements for the form of assignments, there should be no obstacles to electronic assignments. Introduction of certain *lex specialis* provisions, which would improve the legal stability of factoring operations and support the development of factoring services, would be useful for Georgian law. These are, in particular, provisions on prohibition of assignments, definition of future accounts receivable, general notice on future assignments and recourse right in the case of recourse factoring. Hence, it seems desirable to adopt the following regulations:

• The client shall at all times guarantee that any and all receivables sold are free of pledges, contestations, burdens and other rights of third parties and that such receivables may not be contested on any grounds, even when not explicitly agreed. Where any receivables sold are the subject of a pledge or objection by the debtor or other right of any third party, or if such receivables have been contested in any manner by the debtor or any third party, the factor shall have recourse against the assignor for such receivables, regardless of whether factoring with recourse or without recourse has been agreed on;

• Notice of the assignment of receivables may be given with respect to all receivables covered in a factoring agreement, regardless of whether they actually exist at the time the agreement was entered into;

• A future receivable may be subject to factoring. A future receivable shall be deemed to be sufficiently defined if the factoring contract indicates the debtor under such receivable; and

• Where the assignment of a receivable is prohibited under a contract between the client and the debtor, or the general terms and conditions of the debtor, such prohibition shall not have legal effect on the assignment of such receivables to entities permitted to provide factoring services.

11. Regulatory Framework

From the standpoint of public policy, three basic criteria are generally used to determine whether financial institutions should be subject to prudential regulation (licensing, supervision, reporting and capital adequacy requirements).[40]

One of these criteria is whether the type of institution is a significant repository of savings of the public, such that the failure of this type of institution could cause a significant shock to general financial stability. A second consideration is whether the type of institution is a direct participant in the clearing and settlement of payments, such that the failure of a significant participant could disrupt the payments system. The third consideration is whether the type of institution is a source of credit with macroeconomic significance to the general economy.

If the type of institution does not accept deposits from the public, extends only modest amounts of credit, and is not a direct participant in the clearing and settlement of payments, (e.g. financial leasing and factoring companies), then there is dramatically less justification for subjecting such institutions to capital adequacy requirements and strict regulation in general.

The factoring community opposes strict regulation in general and the application of the Basel capital adequacy principles in particular. It is believed that the Basel framework does not properly consider the low risk level of factoring activities (as noted by the International Chamber of Commerce, European Banking Federation and Swedish Banker's Association).[41] On the other hand, it is recognized that an appropriate level of supervision may add more legitimacy, respect and harmonization to the industry. Current practices across Europe vary from a liberalized approach to relatively strict regulation.

12. Examples of Regulation

12.1. Unregulated

The United Kingdom represents an example of an unregulated factoring industry.[42] In the UK, each factoring company operates according to its corporate governance rules, contractual relationships and the Code of Business Practice, a framework developed by The Asset Based Finance Association (whose 40 members represent about 95% of the UK and Irish market). The only supervision exerted over

[40] Comp.: *Llewellyn D. T.,* Institutional Structure of Financial Regulation and Supervision: the Basic Issues, Washington DC, 2006, 5.

[41] Comp.: *European Bank for Reconstruction and Development*, Factoring Survey in EBRD's Countries of Operation, 2018, iii, <https://www.ebrd.com/documents/ogc/factoring-survey.pdf>, [28.09.2018].

[42] Ibid.

factoring companies is conducted by the FSA under Anti-Money Laundering Laws. Other examples of unregulated countries include Ireland, Belgium, the Netherlands, Poland, Slovakia, Switzerland, Russia, the Czech Republic, Lithuania, Luxemburg, Denmark, Estonia, Latvia, Slovenia, and Cyprus.[43]

12.2. Types of Regulation

12.2.1. Regulation without Capital Adequacy Requirements

Factoring in Germany is considered a regulated financial service subject to the German Banking Act (*Kreditwesengesetz*). The reported rationale behind the decision to regulate the industry was the growing importance of factoring in Germany, especially for SME financing.[44] There were worries that missteps based on unsound management could cause significant damage, not only to the clients of the relevant company, but also to the industry as a whole. This danger was thought to be sufficient enough to put factoring companies under limited supervision. As a consequence, anyone who intends to provide factoring services in Germany is required to apply to the regulating agency (Federal Financial Supervisory Authority ─ *BaFin*) for a license. In addition, management has to be approved, qualified participating interests have to be reported, and evidence of the suitability of shareholders to hold qualified participating interests needs to be provided. There are also some internal organizational requirements, in particular with respect to risk management and outsourcing of activities. Obligations to submit annual accounts, management reports and auditor's reports on a regular basis have also been introduced.

However, capital adequacy requirements were not introduced in Germany. With respect to international factoring services provided in Germany, a license is not required if the relevant entity qualifies as a credit institution as defined by the European Banking Directive 2006/48/EC and has its seat in the European Economic Area. For all other companies wishing to provide factoring services, a German financial services license is required. Romania, Norway and Turkey are also examples of countries where some regulation has been imposed but no capital adequacy rules exist.[45]

12.2.2. Regulation with Mitigated Capital Adequacy Requirements

Italy and Spain have aligned their regulation of factoring companies with Basel capital adequacy requirements with some relaxations in specific areas, in particular with respect to the capital adequacy requirement.[46] In Italy, companies are subject to capital adequacy rules arising from EU capital requirement directives and prudential risk-based supervision of the Bank of Italy. Supervision consid-

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43 Comp.: *Llewellyn D. T.*, Intitutional Structure of Financial Regulation and Supervision: the Basic Issues, Washington DC, 2006, 36-39.

44 Comp.: *European Bank for Reconstruction and Development*, Factoring Survey in EBRD's Countries of Operation, 2018, iii, <https://www.ebrd.com/documents/ogc/factoring-survey.pdf>, [28.09.2018].

45 Comp.: *UK Factoring Association*, International Factors Group, Receivables Finance & ABL, A Study of Legal Environments across Europe, 2007, 103, 127, 130, <http://www.abfa.org.uk/members/newsletter/EU-LegislationReport.pdf>, [28.09.2018].

46 Comp.: *European Bank for Reconstruction and Development*, Factoring Survey in EBRD's Countries of Operation, 2018, iii, <https://www.ebrd.com/documents/ogc/factoring-survey.pdf>, [28.09.2018].

ers credit, operational, foreign exchange (FX) and trading risk. The introduction of capital adequacy requirements (which are lower than those for banks and weighted depending on the type of financing source) was based on the position of the Bank of Italy that greater transparency of the risk involved in lending to the factoring companies and their financial soundness would offer potential for growth and development of the industry.[47]

In Spain, factoring companies which are a part of banking groups are regulated and supervised by the Bank of Spain. Capital adequacy ratio is somewhat relaxed for those factoring companies. Otherwise, for the independent factors, the minimum capital adequacy ratio is same as for banks.[48]

12.2.3. Regulation with Full Basel Approach

Under Section 1 Paragraph 1 No. 16 of the Austrian Banking Act, the purchase of accounts receivable arising from delivery of goods or rendering of services, assumption of the credit risk on such claims – exempt credit insurance – and, in connection therewith, the collection of such receivables (factoring business) is considered a banking transaction and exclusively restricted to credit institutions which must be licensed by the Financial Market Authority (FMA) to perform such activities. Austrian credit institutions, including factoring companies, are required to calculate capital requirements under the Basel framework in accordance with applicable Austrian FMA regulation.[49]

13. Proposed Georgian Regulation

When considering regulation of factoring in Georgia, one should take into account whether there is a need to impose the capital adequacy requirement upon factoring companies. In addition, the regulation should define criteria for establishing factoring companies (the form of the company allowed to provide services, control of the ownership structure, charter capital, permitted business activities and management requirements), and set rules for supervision, reporting and ensuring that certain market conduct (consumer protection) standards are met.

13.1. Capital Adequacy Requirements

In theory, the core argument for relaxed capital adequacy requirement in factoring is grounded on risk mitigation. While in case of standard loan, the default occurs in case of default of the client. In recourse factoring, both the buyer and the client should default to cause non-payment towards the factor.

Similarly, for non-recourse factoring, buyer's default risk is in most cases mitigated by the credit insurance provided to factor by a reliable insurer.

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47 Comp. ibid.

48 Comp.: *UK Factoring Association*, International Factors Group, Receivables Finance & ABL, A Study of Legal Environments across Europe, 2007, 49, <http://www.abfa.org.uk/members/newsletter/EU-LegislationReport.pdf>, [28.09.2018].

49 Comp.: *European Bank for Reconstruction and Development*, Factoring Survey in EBRD's Countries of Operation, 2018, iii, <https://www.ebrd.com/documents/ogc/factoring-survey.pdf>, [28.09.2018].

In addition, stability of factors is the precondition for their ability to attract financing as the major source of financing for factors is the banking loan. Therefore, there exists a self-regulatory element in the form of difficult access to financing for those factors, which cannot demonstrate sound financial standing.

Last, but not least, in practice, there is no commonly accepted form of capital adequacy requirement for factoring. While no regulation of capital adequacy exists in most EU countries, those few countries requiring relaxed capital adequacy requirements scale the requirements either based on source of factor's funding or based on a factor's membership in group.

In conclusion, it is not recommended to introduce capital adequacy requirement at the moment. However, it might be considered within the regulatory framework to allow Georgian regulator to introduce certain requirements in this area in future. Both for the factoring market as a whole, and/or for individual factoring companies (with increased risk identified by the regulator), it might be beneficial to empower the regulator to issue calculation and reporting requirements on capital adequacy as well as to set up certain obligatory capital adequacy ratios.

13.2. Factoring Companies

A major area for decision in any regulatory framework for factoring is defining the criteria for determining who can perform factoring activities. Clear standards should be set regarding such areas as corporate form, minimum capital, ownership criteria, scope of business and required expertise.

13.2.1. Organizational and Legal (Corporate) Form

In some countries, there are no restrictions on the type of entity that may perform factoring activities. In others, such activities are highly restricted, for example, limited to licensed banks only. These are the two extremes. However, in most countries, especially in those emerging markets where factoring is a new service and is just being introduced, there is typically a set of criteria set forth in some regulatory form which stipulates minimum capital requirements. There may also be some stipulations as to the type of company and ownership.

The desired standard for such regulation should be to permit, even encourage, the establishment of legitimate factoring businesses, while ensuring a level of professional expertise and adequate financial backing to enable such businesses to function properly. If this balance is not struck, there is a risk, on one hand, that marginal entities may promote themselves on the market as legitimate factoring companies; on the other hand, the emergence of factoring could be stifled by overly onerous regulatory requirements which create barriers to entry.

I believe that it would be expedient to regulate that a factoring company shall be a legal entity registered in Georgia (entered into the Registry of Entrepreneurs and Non-Entrepreneurial (Non-Commercial) Legal Entities maintained by National Agency of Public Registry of Ministry of Justice of Georgia (hereinafter ─ "the Entrepreneur's Registry")) and further licensed by the supervisory body. The company should be incorporated either as a joint stock company and/or a limited liability company. The term factoring and its derivatives in the company name may be recorded in the Entre-

preneur's Registry and may be used in legal transactions only by a company that has obtained a license to provide factoring services. As factoring is already a form of permitted activity for commercial banks and microfinance organizations, these entities should be entitled to perform respective services without separate registration or licensing.

Factoring activities should be permitted to be performed only by Georgian factoring companies, Georgian banks, microfinance organizations and a branch of a bank registered in a third country under terms and conditions defined in the regulations on banking operations in Georgia.

13.2.2. Supervision of Ownership

Many countries have no regulations or requirements of any kind regarding who may own a factoring company. At the other extreme, some countries permit factoring only by licensed commercial banks. A relatively restrictive set of ownership criteria limits shareholding in factoring companies to licensed banks and non-bank financial institutions or to factoring companies owned by such entities.

To permit development of factoring, this sector should be open to the participation of any investor who is able to meet certain general requirements (e.g. no bankruptcy records, money laundering or other criminal convictions, etc.). In order to allow for efficient supervision, introducing a requirement for prior approval of acquisition of a qualifying stake (10% of the voting rights or of the capital stock) in factoring companies (such approach is applicable in relation to commercial banks in Georgia) is recommended. In addition, the holder of a qualifying stake should request an approval from the supervisory body for acquiring a qualifying stake prior to any further acquisition of stakes or shares on the basis of which it exceeds 25 percent or 50 percent of the voting rights or of the capital stock (such percentages also aligned with current banking regulations).

13.2.3. Charter Capital

Required minimum charter capital is a key issue and various criteria have been set in various countries. The best guiding principle would appear to be to set minimum charter capital at a level which ensures serious shareholder backing, but not so large as to be an unnecessary barrier to entry or disproportionate to the real needs of a factoring business. Some countries have set a high minimum capital for factoring, at or near the level required for participation in Factors Chain International (USD 2 million). But this level of capital is not necessary for companies wishing to engage in the business of domestic factoring or direct import factoring.

Such a level of required minimum charter capital is excessively high and creates a barrier to entry and an impediment to the development of factoring. It is proposed to align the minimum required charter capital with the requirement for microfinance organizations in Georgia, i.e., at least GEL 1,000,000 in monetary contribution. The capital stock must be fully paid before the factoring company requests a license with the regulatory body.

13.2.4. Business Activities

Any existing or future, entire or partial, short-term receivable arising from a contract on sale of goods or provision of services may be subject to factoring. Apart from engaging in factoring, the factoring company may undertake to perform the following services as well:

1) Keeping records of and ledgering transferred receivables;

2) Collecting receivables;

3) Assuming the risk of collection of transferred receivables;

4) Discounting bills of exchange originated in the transaction of provision of services or sale of goods; and

5) Providing advice on organization of a ledger, etc.

13.2.5. Directors/Management

It may be appropriate to set some standards for experience levels of senior management of factoring companies, particularly when experience in managing financial or commercial businesses is required.

Hence, in my opinion, a law on factoring should follow the model of currently effective 2006 Law of Georgian on Microfinance Organizations, which requires that management of such entities comply with the criteria[50] as follows: university degree; corresponding expertise, skills and experience necessary for conducting the company operations; the individual should not have taken part in a transaction which inflicted significant damage to depositors or other creditors of a factoring company or credit institution (implying commercial banks, microfinance organizations or credit unions) or which resulted in insolvency/bankruptcy of such factoring company or credit institution; the individual was not convicted for serious, particularly serious heavy crimes (as defined under Georgian Criminal Code), money laundering and/or financing of terrorism and other economic crimes; the individual is not a shareholder, management member and/or a manager, member of supervisory board of another factoring company, etc.

14. Licensing, Supervision and Reporting

As current legislation factually indirectly implies supervision of factoring by the National Bank of Georgia (this is due to the fact that factoring is directly permitted for commercial banks and microfinance organizations), establishment of this institution as a regulator of factoring on legislative level seems fully expedient. However, currently effective Georgian legislation does not provide for any specific rules for supervision and reporting of factoring.

[50] Comp.: Article 7, Law of Georgia on Microfinance Organisations, 18/07/2006.

14.1. Licensing

For the purpose of perfection of local legislation on factoring, it is necessary to define National Bank of Georgia's authority in detail as well as procedures to be followed by the National Bank of Georgia and factoring companies when:

1) issuing and revoking licenses for conducting factoring activities;
2) issuing approvals for acquiring qualifying stakes in factoring companies, and
3) issuing and revoking approvals for management board members.

14.2. Supervision

The National Bank of Georgia should be authorized to exercise supervision over factoring companies except when banks or microfinance organizations perform them within the scope of their registered activities. National Bank of Georgia further shall have the power to supervise factoring companies and shall determine whether they operate in compliance with factoring laws and its implementing regulations, or with other laws and their implementing regulations that govern operations of factoring companies.

The National Bank of Georgia shall also have the power to supervise or to cooperate with other supervisory bodies in supervising legal entities affiliated with factoring companies, if necessary for performing supervision of the factoring company.

The factoring law should empower the National Bank of Georgia to request from the factoring company information about any activities which are important in determining whether they comply with the provisions of the law and its implementing regulations.

The National Bank of Georgia should have further powers to supervise factoring companies by monitoring, gathering and reviewing reports of the factoring companies; reviewing the operations of a factoring company, and imposing supervision measures. In conducting the supervision, the National Bank of Georgia should be able to perform the following actions: eliminate illegalities and irregularities (e.g. in cases when a company does not meet the conditions for conducting factoring activities; the company conducts an activity which is not allowed, the company violates regulations on bookkeeping and preparation of financial statements, and/or audit of financial statements; the company breaches the reporting regulations; etc.); revoke licenses; initiate a misdemeanour procedure; implement additional measures (e.g. to order adoption of measures in order to ensure solvency of the factoring company, to suggest appropriate decisions on increasing the share capital, to ban dealings with certain members of management, shareholders, etc., to order improvement of internal procedures, to order release of members of the management board in case of serious breach of duties, etc.); and prohibit unlicensed parties from conducting factoring activities.

The law should also set clear obligations for factoring companies to enable supervision activities on their premises, as well as on other premises where they perform their operations subject to supervision; enable review of business ledgers, business documentation and administrative records, business records within the limit necessary for conducting special supervision and/or within the limit

set in the law regulating special supervision; to submit computer generated records and/or copies of business ledgers, business documentation, administrative records and business records, etc.

Upon completion of supervision of operations of the factoring company, the National Bank of Georgia should prepare a supervisory report and submit it to the supervised company which must be entitled to file an objection regarding the supervision report to the National Bank of Georgia in accordance with the law governing administrative procedure.

14.3. Reporting

Proper management of accounts receivable (ledgering) is essential to the factoring business and systems for doing so must be part of a factoring company's knowledge base and operating procedures. The factoring company must organize its operations and maintain books, business documentation and other records in a transparent manner that enables determination as to whether the company operates in compliance with applicable regulations and industry standards.

Following the rules established for commercial banks and microfinance organizations, it seems expedient to specifically prescribe that all factoring companies (irrespective of their size, value of assets or annual income) are obligated to perform an annual audit of financial statements.

In addition, factoring companies should report changes to any basic data in the Entrepreneur's Registry; all decisions adopted at shareholders meetings, shareholders of the company and acquiring qualifying stakes and/or changes in the qualifying stakes; estimated opening, moving, closing or temporary terminating of branches or representative offices and/or other related changes; investments based on which the company acquired, directly or indirectly, qualifying stakes in another legal entity and all further investments in the same legal entity; and changes in the capital structure.

15. Market Conduct

Market conduct regulations seek to establish good business practices in disclosure of the terms and conditions of transactions so that clients can understand their rights and responsibilities in financial transactions.

I believe comprehensive overview of how various jurisdictions regulate market conduct of factoring companies would be overburdening for this article, as these vary from having the rules prescribed in special laws to more general legislation (such as consumer protection or general financial services regulation).

However, it can be stated that regardless of the approach, the following principles are generally followed:

- Fair treatment of customers (transparency of fees and charges, accessibility of general terms and conditions);
- Selling and advising in a responsible way;
- Providing adequate after sales service;
- Ensuring that product performance meets customers' fair expectations; and
- Transparent and fair handling of complaints and resolution of grievances.

A good market conduct regulation system built around these principles is especially important for fostering the general acceptance of the factoring industry as a legitimate and highly welcomed financial service by the general public. Transparent rules and regulations should make consumers confident in dealing with factoring firms.

In Georgia, the protection of individual consumer rights should be enforced in compliance with the law governing consumer protection in the field of financing services. Currently, this mainly applies to NBG regulations on Approval of Rules of Consumer Protection during Provision of Services by Financial Organizations (Order of the President of NBG № 151/04, 23/12/2016). However, the factoring law should provide that the amount, manner of calculation and payment of the fee due to the factor, as well as the entitlement of the factor to interest and any other expenses that may arise in the execution of the factoring agreement, should be clearly determined in the factoring agreement.

16. Conclusion

In the scope of this article there are considered certain specifics of factoring as a financial service, types of factoring based on international experience, current status of factoring in Georgia and perspectives of its development. Due to high global importance of factoring, Georgia cannot remain without detailed legal regulation of this field in compliance with contemporary standards. Accordingly, a number of issues have been identified which require regulation on legislative level. Among them, the main topic is adoption in Georgia of a new law on factoring, which should provide a comprehensive definition of factoring and each of its particular forms. This legislative act should refer to factoring companies; however, the majority of its provisions should further apply to factoring operations performed by commercial banks and microfinance organizations. Moreover, some definitions and references to factoring, currently envisaged under Georgian law, should be brought in compliance with the content of new factoring law, including:

- the Laws on Activities of Commercial Banks and Microfinance Organizations should reflect definitions of factoring and its forms established by new factoring law;
- after adoption of the new law on factoring Tax Code of Georgia should contain a reference on factoring as a financial service;
- Law on Licenses and Permits pursuant to which it is prohibited to introduce any licenses or permits other than those that are specifically prescribed by this Law, should regulate licensing of factoring activities;
- bylaws issued by the National Bank of Georgia in relation to accounting, classification of assets etc. of commercial banks and microfinance organizations that currently refer to factoring without defining its content, should be considered from perspective of new factoring law.

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Piercing the Corporate Veil of Shareholder in German, US and Georgian Legal Doctrine

The aim of the present article is to study the grounds and judicial practices of piercing the corporate veil in Germany and the United States, and to present the flaws and problems of the present doctrine in Georgia, while providing solutions and recommendations regarding respective issue.

The article generally discusses piercing the corporate veil as a concept, which focuses on the legal and economic approach of limited liability. Afterwards, it outlines positive and negative economic and legal dichotomy of limited liability. The article examines the forms of piercing the corporate veil in the US and German law doctrines, types of creditors, the main preconditions for the use of the doctrine and related judicial practice. Moreover, article compares and reviews the legislative regulation, its historical development and judicial practice of piercing the corporate veil in Georgia.

Keywords: *Piercing the Corporate Veil, Limited Liability, Separate Personality, Corporation, Undercapitalisation, Disregarding the Corporate Formalities, Commingling of Assets, Konzern Law.*

1. Introduction

The essential principles of corporate law, such as limited liability and separate personality, provide the so-called corporate veil[1] for a corporation,[2] whereby the corporation presents itself to third parties as a separate and distinct entity from its shareholders, and its liability is limited to assets of the corporation. Nevertheless, these principles are not absolute and piercing corporate veil is possible in exceptional circumstances.

Frequently, there are cases of misusing the principle of limited liability, such as intentionally leading company to insolvency, receiving profit by acting not in good faith, deceiving creditors, avoiding responsibility, fraud, etc.[3] Undoubtedly, frequent occurrence of such cases in practice demanded the establishment of the doctrine known as piercing the corporate veil. This concept allows creditors to pierce corporate veil in certain cases and demand direct liability of the shareholders in favour of corporate creditors.[4]

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1 In Georgia, the present name was established in 2009; *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 236 (in Georgian).

2 In present article, the concept of corporation, as the US Corporation implies only an association where the partner has limited liability. *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 14-17 (in Georgian).

3 *Burduli I.,* Authorized Capital and Its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 236 (in Georgian).

4 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 14-17 (in Georgian).

The 6th paragraph of Article 3 of Law of Georgia on Entrepreneurs indicates the direct liability of the shareholder in case one misuses the principle of limited liability,[5] though the content, framework of usage, types and common judicial practice are not defined precisely.

Therefore, the main aim of this article is to identify the fundamental and modern approach of the concept of piercing the corporate veil based on US and German practice, and to use comparative legal methodology to discuss the ongoing flaws of the principle in legislative and judicial systems of Georgia.

2. The Concept of Piercing the Corporate Veil

2.1. Legal and Economic Approach to Limited Liability

The limited liability principle has been the subject of debate since its inception. The most common, but not the unanimous opinion, is that limited liability is the main reason for the formation of modern capitalist economy.[6] Despite debates, the universal character of the corporate form today is limited liability, indicating its significant value as a unique instrument of contracting and financing.[7]

A company is often described as the union of contracts – "*nexus of contracts*" in economics. However, it would be more accurate to distinguish it as an union for contracts, "*nexus for contracts"*, since the company is rather clearly outlined with the later name as the counterparty in various contracts with employees, suppliers and clients, organizing the actions of these multiple persons through exercise of its contractual rights.[8] The corporation, which is enforced as a legal entity from the moment of registration,[9] participates in different types of relationships as an independent legal entity, separate from its shareholders. The core element of this principle is "*separate patrimony"*.[10] This later element involves a demarcation line between the shares of the corporation and the personal shares of shareholders.[11] Respectively, the corporation itself is authorised to manage property at its own discretion, including selling and pledging to creditors. The main function of "*separate patrimony"* is recognised as "*entity shielding"* – protection of corporation through a veil, which ensures the property of the corporation to be confined by the veil from the private creditors of the shareholders.[12] Unlike "*entity shielding"*, limited liability ensures protection of shareholder by veil known as "*owner shielding"*. Thus, this form guarantees security of private assets of the shareholders from the creditors of a corpo-

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5 Article 2.3., Law of Georgia on Entrepreneurs, ed. 06/06/2018, 28/10/1994.

6 *Freedman J.,* Limited Liability: Large Company Theory and Small Firms, The Modern Law Review, Vol. 63, № 3, 2000, 326-327.

7 *Armour J., Hansmann H., Kraakman R.,* The Essential Elements of Corporate Law: What is Corporate Law?, Harvard Law School, Discussion Paper № 643, 2009, 9.

8 Ibid, 6.

9 Article 8, Civil Code of Georgia, ed. 21/07/2018, 26/06/1996.

10 *Kraakman R., Davies P., Hansmann H., Hertig G., Hopt K., Kanda H., Rock E.,* The Anatomy of Corporate Law, A Comparative and Functional Approach, Oxford, 2003, 8.

11 *Armour J., Hansmann H., Kraakman R.,* The Essential Elements of Corporate Law: What is Corporate Law?, Harvard Law School, Discussion Paper № 643, № 7, 2009, 6.

12 Ibid, 9.

ration. Together, limited liability and separate personality develop a regime known as "*asset partitioning".*[13] Consequently, the influence of these principles towards creditors are contradictory, particularly, corporation creditor's right to claim only applies to the assets of the corporation, while the claim of shareholder's private creditor applies solely to the assets of the shareholder.[14]

According to *Richard Posner*, one of the founders of economic analysis of law, a corporate form is a natural solution, which means that law and business practice have developed in certain way, and got dealt with all the obstacles faced by the partnerships.[15] The economic effect of limited liability principle on private law relations is the subject of special consideration in legal literature.[16] It is assumed that limited liability is not a means for excluding the risks, but it causes shifting of the risk from an individual investor to voluntary or involuntary creditor, who carries the risk in case of failure of the corporation.[17]

2.2. The Positive and Negative Economic and Legal Dichotomy of Limited Liability

Based on economic and legal analysis, the principle of limited liability is a widely spread and accepted form in common law and continental European countries. Nonetheless, the group of scholars who believed that too much free usage of the mentioned principle by small corporations would cause undesirable results in future for business owners and creditors also, always existed. However, a second group of scholars, in contrary, believes that more individual entrepreneurs and partnerships shall change the form, as the reduction of access to limited liability will bring a bigger blow to economic development.[18]

Opposed to *Posner*, *Easterbrook* and *Fischel* consider that when limited liability firm fails, the loss is swallowed rather than shifted, because the shareholder loses its confined investment to creditor.[19] As mentioned above, *Posner* indicates that, within limited liability, the risk is transferred to the creditor, and in his opinion shareholder's right to limit his/her risk will always reflect to the risk of others, which in itself does not create a great moral threat. This result would have occurred in case of unlimited liability as well because shareholder's personal assets would eventually end, and in this regime, the creditor would have become the carrier of the risk as well.[20]

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13 *Armour J., Hansmann H., Kraakman R.,* The Essential Elements of Corporate Law: What is Corporate Law?, Harvard Law School, Discussion Paper № 643, № 7, 2009, 9.

14 *Kraakman R., Davies P., Hansmann H., Hertig G., Hopt K., Kanda H., Rock E.,* The Anatomy of Corporate Law, A Comparative and Functional Approach, Oxford, 2003, 8-9; *Makharoblishvili G.,*The Two Differentiated Elements by the Corporation's Legal Personality: Limited Liability and Entity Shielding, Jubilee Collection: Guram Nachkebia — 75, *Todua N.* (ed.), Tbilisi, 2016, 435-437 (in Georgian).

15 *Posner R.,* Economic Analysis of Law, 8th ed., New York, 2011, 535-536.

16 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 58 (in Georgian).

17 *Posner R.,* Economic Analysis of Law, 8th ed., New York, 2011, 536.

18 *Freedman J.,* Limited liability: Large Company Theory and Small Firms, The Modern Law Review, Vol. 63, № 3, 2000, 327.

19 Ibid, 329.

20 Ibid.

At the same time, it should be taken into consideration that the possibility of diversified portfolio derives from the nature of limited liability of the corporations. The investor holds less risk while having a diversified portfolio, in contrast to investing only in one corporation, because in case of the failure of the corporation, the investor would lose the entire property. Moreover, the existence of a diversified portfolio leads investors to invest in risky projects by avoiding placing entire property under one risk.[21] Without limited liability, the investor would not have been able to plan diversified investments, since one would have been liable-with all of his/her assets.[22]

In addition to this, reduction of monitoring costs is a major economic justification, which eventuates from limited liability. Under unlimited liability, the creditor would have made a claim against the shareholder with the most assets in an insolvent company. In such case, the shareholder would have been forced to control every step of the managers,[23] which would result in increased costs of management monitoring and prevent investments. At the expense of the deduction of monitoring costs for shareholders and management and diversification of investments, it is possible to increase the capital of the corporation, which has positive impact on corporation.

Consequently, economic analysis of limited liability is based on the ability of the enterprise to transfer risks to creditors. In this sense, the principle of limited liability is a mechanism of insurance for corporation risks, whose value is paid by the creditor.[24]

2.3. The Nature of Piercing the Corporate Veil

2.3.1. General Overview of Piercing the Corporate Veil

The protection obtained as a result of the combination of principles of limited liability and separate personality is not unconditional and in some cases, when shareholders abuse them, restriction of such principles is applied, which is known in the USA as piercing the corporate veil and in Germany as *Durchgriffshaftung* (literal translation is as follows: pierce through responsibility).[25] Piercing the corporate veil was developed by the judicial system of the United States, which implies that shareholder may be individually liable for damages caused by corporations to creditors in spite of its limited liability.[26] It shall be noted that piercing the corporate veil mainly concerns closely held corporations, not the widely held ones. The Georgian translation of the Doctrine *Gamtcholi Pasukhismgebloba,* which was achieved by piercing the corporate veil, has been established in 2009.[27]

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21 *Posner R.,* Economic Analysis of Law, 8th ed., New York, 2011, 535-536.

22 *Orn P.,* Piercing the Corporate Veil – a Law and Economics Analysis, University of Lund, 2009, 13.

23 Ibid, 12.

24 *Sommer J. H.,* Subsidiary: Doctrine without a Cause?, Fordham Law Review, Vol. 59, Issue 2, 1990, 230.

25 *Burduli I.,* Authorized Capital and Its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 236 (in Georgian); *Burduli I,* Fundamentals of Corporate Law, Vol. I, Tbilisi, 2010, 165 (in Georgian).

26 *Matchavariani S.,* Management of Corporate Groups in Germany and the United States and Integration of Management Principles in Georgian Private Law, Tbilisi, 2015*,* 150 (in Georgian).

27 *Burduli I.,* Authorized Capital and Its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 236 (in Georgian).

The doctrine of piercing the corporate veil is used by the courts in the United States, in spite of the fact that restriction of limited liability is not regulated under the law. In such cases, courts of equity will pierce fictions, disguises and consider the contents of the actions and not blindly follow the corporate form of limited liability.[28] One of the earliest court judgments was made in the case of *Booth v. Bunce*,[29] where the court indicated that the corporate veil would have been pierced if the corporation was created to deceive and mislead creditors. The majority of courts use piercing the corporate veil only in cases when it was impossible to distinguish between individuality of the corporation and shareholder as personal interest and assets were excessively united.[30] The Court ruled in the case of *United States v. Milwaukee Refrigerator Transit Co.*[31] that corporate form might be neglected in cases where its form is used as a means of doing injustice, fraud, crime and breaking public order.[32]

Supporters of the doctrine of "parallelism of power and liability in Germany", followers of the Freiburg Economics School, argued that those who were in power in economic process should be liable for their actions as a corrective for such power. It was believed that such ~~a~~ narrative of liability would cause more cautious and responsible allocation of capital in the market.[33]

The judgement in *Rector*[34] made by the Supreme Court (*Bundesgerichtshof*) in 1966 indicated that there was no abuse of the limited liability principle and the co-existence of this principle and supervision of the management by shareholders is acceptable. However, the existence of additional circumstances that mislead the creditor regarding the extent of the liability and financial status of the shareholder allows courts to hold shareholders personally liable despite limited liability.[35] Consequently, in order to impose piercing the corporate veil, it is necessary to have specific circumstances such as creating corporation as the facade aimed at concealing a real picture, namely, representation, fraud and injustice, during which it is compulsory to assess a corporation and its shareholders as one whole.[36]

In contrast to traditional narrative of piercing the corporate veil, where a shareholder is liable for the damages of a corporation and parent corporation for its subsidiaries, reverse piercing indicates cases in which a corporation is liable for shareholders' liabilities, while subsidiary is liable to its parent

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28 *Bangor Punta Operations, Inc. v. Bangor & Arrostook R. R. Co.,* 417 U.S. 703, 713 (1974), *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 481.

29 *Booth v. Bunce* 33 N.Y. 139 (1865).

30 *Ezzo R. P.*, Corporations, Piercing the Corporate Veil, Stockholder Liability, University of Miami Law Review, № 122, 1957, 123.

31 *United States v. Milwaukee Refrigerator Transit Co.,* 142 F. 247, 255, C.C.E.D. Wis. (1905).

32 *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 481.

33 Ibid, 485.

34 Bundesgerichtshof, W. Ger., 45 BGHZ 204 (1966).

35 *Schiessl M.,*The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 485.

36 *DHN Ltd v Tower Hamlets* 1 WLR 852, Lord Denning MR14 (1976); *Adams v Cape Industries* plc., BCC 786, 822. 50. (1990).

corporation. In spite of the differences, reverse piercing requires similar preconditions as traditional piercing.[37] Furthermore, there is a distinction between vertical and horizontal piercing the corporate veil. Vertical piercing holds a shareholder liable for the debts of the corporation while horizontal piercing involves liability of the related (affiliated) corporations for the obligation of related corporation.[38]

Hence, the principle of limited liability and separated personality is not an absolute category. Those who will use privileges deriving from these principles for personal interests, which generally results in the wrong redistribution of economic risk, as a rule will pay for such action. In such cases, the legal response mechanism is piercing the corporate veil, though it should be noted that the goal of piercing the corporate veil is not to restrict limited liability, but it is the mandatory need for the protection of public interests.[39]

2.3.2. Types of Creditors of Piercing the Corporate Veil

Within the scope of doctrine of piercing the corporate veil, the difference is made between voluntary (contractual) and involuntary (tort) creditors.[40] According to *Richard Posner*, the principle of limited liability is not an enhanced and unjustified financial risk for contractual creditors.[41] Since the voluntary creditor, unlike the involuntary creditor, has the opportunity to study the corporation and its financial condition, until ~~a~~ the creditor makes a deal with the corporation, unless there is a case of fraud or misleading the creditor.[42]

It is noteworthy that there is no division between voluntary and involuntary creditors in Germany, as it is in American jurisprudence. The court should not pierce the corporate veil, when the contractual creditor has the knowledge of the financial condition of the corporation and still voluntarily concludes the contract with it.[43] In case of involuntarily creditors, the same prerequisites are to be used as for voluntary creditors.[44]

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37 *Allen N.,* Reverse Piercing of the Corporate Veil: A Straightforward Path to Justice, St. John's Law Review, Vol. 16, № 1, 2012, 26.

38 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 21 (in Georgian).

39 *Makharoblishvili G.,* The Two Differentiated Elements by the Corporation's Legal Personality: Limited Liability and Entity Shielding, Jubilee Collection: Guram Natchkebia ― 75, *Todua N.* (ed.), Tbilisi, 439 (in Georgian).

40 *Burduli I.,* Authorized Capital and Its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 257-259 (in Georgian).

41 *Posner R. A.,*The Rights of Creditors of Affiliated Corporations, The University of Chicago Law Review, Vol. 43, № 3, 1976, 503.

42 *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 255-257 (in Georgian).

43 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 210.

44 *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 257-259 (in Georgian).

3. The Grounds of Piercing the Corporate Veil in US and German Legal Doctrine

The burden of proof is significantly hard on the party demanding piercing the corporate veil, as the role of limited liability is of high importance.[45] The American common law has established certain preconditions for imposing piercing the corporate veil, such as domination and control that may be expressed by commingling of assets between corporations and shareholders, disregarding corporate formalities, undercapitalisation, etc.[46] It shall be noted that the doctrine has same general preconditions in Germany too, namely, commingling of assets, dismissing corporate formalities and inadequate capitalisation.[47]

3.1. Control and Domination

Dominance and control means more than ordinary relationships between shareholders and companies. Parent corporations and dominant shareholders are always actively involved in the corporation's activities which is usually permitted and does not result in personal liability. Acceptable involvement includes monitoring and supervising of the finances and capital of the subsidiary corporation, expressing views concerning general policy and procedures of the corporation.[48]

Instrumentality and the alter ego theories are the mechanisms for determining domination and control.[49] The courts have developed multi-pronged mechanisms, including three-stage standard for instrumentality theory[50] and two-stage standard for the alter ego theory.

3.1.1. Alter Ego Theory

According to alter ego theory, there are two preconditions that must exist together in order to pierce corporate veil. First, the assets and interests between the corporation and the controlling shareholder are so united that it is impossible for the corporation to have a separate personality.[51] Secondly, assessment of such corporation as a separate legal entity based on the afore-mentioned facts would have resulted in fraud and unfair consequences.[52]

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45 *Smith D. G.,* Piercing the Corporate Veil in Regulated Industries, George Mason Law & Economics Research Paper, № 08, 2008, 5.

46 *Tchanturia L.,* Piercing Liability of the Shareholder for Tax Infringement of the Corporation (Innovation of Common Law), Jubilee Collection: Guram Nachkebia — 75, *Todua N.* (ed.), Tbilisi, 2016, 414 (in Georgian).

47 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 95 (in Georgian).

48 *Smith D. G.,* Piercing the Corporate Veil in Regulated Industries, George Mason Law & Economics Research Paper, № 08, 2008, 7.

49 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 69 (in Georgian).

50 *Bainbridge S. M.,* Abolishing LLC Veil Piercing, University of Illinois Law Review, Vol. 1, 2005, 87.

51 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within insolvency proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 69 (in Georgian).

52 *Figueroa D.,* Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America, Duquesne Law Review, Vol. 50, 2012, 728.

However, the majority of courts do not pursue piercing the corporate veil only on grounds of alter ego doctrine if there is no fraudulent act involved, despite the fact that the establishment of the corporation was aimed to avoid personal liability.[53] The claimant should prove that dominance and control by the parent corporation is so big that the subsidiary corporation has no independent legal significance and cases of fraudulent acts are present which mislead creditors regarding the identity of the corporation.[54]

3.1.2. Instrumentality Theory

The New York Court of Appeal was one of the first to establish an instrumentality test in the case of *Lowendahl v. Baltimore & Ohio Railroad Co.*[55] There is a three-part approach within instrumentality theory, which includes requiring the claimants to prove the following circumstances: 1) the level of control of the corporation by the defence party, which includes the complete dominance of the financial and business management of the corporation in a way that it no longer has a separate opinion, desire, therefore, it does not exist; 2) such control is used to infringe plaintiff's rights or to conduct fraud; and 3) the controlling and breaching the rights of the claimant were the cause of the damage.[56]

It should be noted that when the created corporation is only a blanket shell and it does not contain any assets, space or employees,[57] and the shareholder monitors and dominates its finances and management[58] that causes damage to creditor, then it is possible to use piercing the corporate veil doctrine.

Control and dominance, which is common in alter ego, as well in instrumentality theory, is largely relieved in the form of improper capitalisation, disregarding corporate formalities and commingling of assets.

3.2. Undercapitalisation

3.2.1. USA

The law does not the regulate matter of minimal capital in the United States, nevertheless undercapitalisation is not an accepted norm and it is considered that insufficient capitalisation is a problem beyond regulation. The courts have determined that capital should not be "inadequate", grossly inadequate or purely nominal.[59]

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53 *Ezzo R. P.*, Corporations, Piercing the Corporate Veil, Stockholder Liability, University of Miami Law Review, № 122, 1957, 122-123.

54 *Smith D. G.,* Piercing the Corporate Veil in Regulated Industries, George Mason Law & Economics Research Paper, № 08, 2008, 7.

55 *Figueroa D.,* Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America, Duquesne Law Review, Vol. 50, 2012, 721.

56 *Bainbridge S. M.,* Abolishing LLC Veil Piercing, University Of Illinois Law Review, Vol. 1, 2005, 88.

57 *Shapoff v. Scull,* 222 Cal. App. 3d 1457, Cal. Ct. App. (1990).

58 *Figueroa D.,* Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America, Duquesne Law Review, Vol. 50, 2012, 721.

59 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 202-203.

The state of California civil practice has established precise circumstances resulting undercapitalisation in business litigation cases.[60] The first one is when a corporation is organised and maintains its business activity with insignificant capital, meaning that the corporation does not have enough assets to cover its debts. Secondly, the corporation conducts business but does not possess enough financial resources to satisfy claims of creditors. Third, the shareholders have failed to put unencumbered capital under the risk of the business, which would have been reasonably adequate for future liabilities.[61] The fourth, the corporation owns capital that is illusory or trifling in comparison with the business it carries and the risk it holds. The afore-mentioned cases constitute the basis for denying the corporation as having a separate personality.[62]

In case of *Mobile Steel Co.,*[63] where shareholders owed debts to its creditors, the court rejected the concept that a shareholder is required to fill the capital of the corporation constantly to ensure the existence of the corporation. The court at the same time pointed out that adequate capitalisation is considered when a *bona fide* shareholder with general education on specific business and its accompanying risks sets reasonable capitalisation, taking into account other specific circumstances for establishing the company. Such approach is important as it focuses on the founding shareholder, and ensures more precise standards to determine undercapitalization.[64] Therefore, only plain signs of undercapitalisation are not sufficient for imposing alter ego liability and piercing the corporate veil.[65] However, undercapitalisation can become the ground for piercing the corporate veil when it was aimed for misusing the corporate form.[66]

The court in *Tanzi v. Fiberglass Swimming Pools, Inc.,*[67] case confirmed undercapitalisation as the capital of the company consisted of 3,000 dollars, while annual income amounted to 20,000 dollars. At the same time, the court found the full control of the shareholders over the company and assessed the debt they have given to the corporation as a refinancing of the capital, not a *bona fide* loan. In the case of *Sabine Towing & Transportation Co. v. Merit Ventures, Inc.*[68] the court disregarded the principle of limited liability, as the company that was operating in maritime shipping, refinanced its capital with 300,000 dollars, despite the fact that director with specific knowledge in this business advised the capital of 800,000 dollars.[69]

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60 *Stubbs L.,* Undercapitalization as an Independent Ground for Shareholder Liability: The Case for Corporate Stakeholders, Dalhousie University Halifax, Nova Scotia, August, 2016, 79.

61 Ibid.

62 "If the capital is illusory or trifling compared with the business to be done and the risks of loss", *Automotriz etc. De California v. Resnick*, 47 Cal.2d 792 (1957).

63 *In re Mobile Steel Co.,* 563 F.2d 692, 5th Cir. (1977).

64 *Gelb H.,* Piercing the Corporate Veil – The Undercapitalization Factor, Chicago-Kent Law Review, Vol. 59, Issue 1, 2013, 17.

65 *Gartner v. Snyder,* 607 F.2d 582, 588, 2d Cir. (1979), in: *Bainbridge S. M.,* Abolishing LLC Veil Piercing, University of Illinois Law Review, Vol. 1, 2005, 90.

66 *Smith D. G.,* Piercing the Corporate Veil in Regulated Industries, George Mason Law & Economics Research Paper, № 08, 2008, 10.

67 *Tanzi v. Fiberglass Swimming Pools* Inc., 414 A.2d 484, 490, R.I. (1980).

68 *Sabine Towing & Transportation Co. v. Merit Ventures* Inc., 575 F. Supp. 1442 E.D. Tex. (1983).

69 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 204.

3.2.2. Germany

In some jurisdictions, it is traditionally considered that regulated minimum capital ensures the reduction of undercapitalisation of the corporation and less shifting of the risk from corporation to the creditor.[70]

Unlike the US jurisdiction, German Corporate Law requires a minimum capital of 25,000 EUR[71] for German close corporations (*GmbH*), excluding exceptional cases. The above-mentioned corporate form is the most common form in Germany. Economists generally consider that the minimum capital that is adequate for all businesses cannot be determined. However, flexible capital based on its business size and other factors is not stipulated by the law. Nonetheless, corporate shareholders are not authorised to shift all the remaining risks to creditors after meeting the defined minimum capital.[72]

Correspondingly, according to German law, a corporation's inadequate capitalisation is apparent when current capital is not sufficient for the corporation to carry on the activities with the help of certain financial aids, which will not ensure the repayment of the corporation's debts.[73]

Due to the minimum capital, Germans distinguish between nominal and material undercapitalisation.[74] The shareholders fail to meet the minimum requirement of nominal capital during nominal undercapitalisation, whereas material undercapitalisation involves insufficient refinancing of the capital, after meeting the minimum capital requirement stipulated by the law initially. The Ulmer formula is widely established for the assessment of material undercapitalisation. According to the formula, undercapitalisation is apparent when financial instruments, including loans of shareholders, are not sufficient or adequate comparing to the operated business.[75] However, on 16 July 2007, the German Federal Supreme Court in the case of *"Trihotel"* has changed its approach regarding piercing the corporate veil, in particular, when the corporation's assets are drained, and the corporation's "economic status is destructed". The court clarified that the corporate liability of the shareholder is out of question, and denied the liability of the partner of the LLC towards creditor in the case of material undercapitalisation. Liability can only be imposed in case of deliberate damage to the corporation itself.[76]

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70 *Petroševičienė O.,* Effective Protection of Creditors' Interests in Private Companies: Obligatory Minimum Capital Rules Versus Contractual and other Ex Post Mechanisms, Social Studies Research Journal, № 3(7), 2010, 214.

71 Limited Liability Companies Act — Gesetzbetreffend die GesellschaftenmitbeschränkterHaftung (GmbHG), 20/04/1892. Section 5 (1): "The company's share capital must amount to no less than twenty-five thousand Euros." The exception rule is regulated in GmbHG, <https://www.gesetze-im-internet.de/englisch_gmbhg/>, [30.09.2018].

72 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 207.

73 *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 248 (in Georgian).

74 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 207.

75 Ibid.

76 *Knappke T. C.,* No Liability of Shareholder for Material Undercapitalization of a GmbH, Newsletter Corporate Law, October, 2008, 6.

Based on the new approach of the court to impose personal liability of the shareholder elucidates that tort law protects the creditor more adequately.[77] Accordingly, the liability of the LLC's partner in favour of the creditor arises when the partner abuses the privilege of separate personality[78] and violates this principle.[79]

3.3. Disregarding Corporate Formalities

3.3.1. USA

Disregarding corporate formalities is visible when a corporation is established by ignoring the norms of law.[80] Limited liability in the US also concerns the "promoters of the corporation"[81] that form the corporation but are not yet shareholders. Such matter is known as de facto corporation, where promoters are personally liable for obligations of the newly established corporation, until the corporation is properly established. However, since there is no legally established corporation yet, there is no corporate veil which could be pierced.[82] Nevertheless, the liability may be imposed on the shareholders based on general principles of contract law and unjust enrichment. Besides, de facto corporation is not impeded to adopt actions of promoters conducted during the de facto state of the corporation as its own.[83]

The formalities of the corporation are as follows: general meetings of shareholders and board of directors, issuance of shares and fulfilling the preconditions of issuance, selection of directors and managers, accuracy of factual and legal refinancing of signed capital, legitimacy of corporate minutes of meetings and obeying formal conditions related to them.[84] Section 303 (b) of the United States Uniform Limited Liability Company Act 1996 determines that "the failure of a limited liability company to observe the usual company formalities or requirements relating to the exercise of its company powers or management of its business is not a ground for imposing personal liability on the members or managers for liabilities of the company."[85] However, it should be noted that the violations of these

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77 *Zhen Qu C., Ahl B.,* Lowering the Corporate Veil in Germany: a Case Note on BGH 16 July 2007 (Trihotel), Oxford U Comparative L Forum 4, 2008, <ouclf.iuscomp.org>, [30.09.2018].

78 Limited Liability Companies Act, Gesetzbetreffend die GesellschaftenmitbeschränkterHaftung (GmbHG), Section 13 (2): "The company assets alone shall serve to discharge the company's obligations vis-à-vis its creditors.", <https://www.gesetze-im-internet.de/englisch_gmbhg/>, [30.09.2018].

79 *Görtz M.,* The Federal Court of Justice's Concept for Piercing the Corporate Veil due to Destruction of a German Limited Liability Company, Client Newsletter, № 9, 2007, 1.

80 *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 251 (in Georgian).

81 "A person who devises a plan for a business venture; one who takes the preliminary steps necessary for the formation of a corporation." The Free Dictionary by Farlex, <https://legal-dictionary.thefreedictionary.-com/promoter">promoter, [30.09.2018].

82 *Figueroa D.,* Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America, Duquesne Law Review, Vol. 50, 2012, 743.

83 Ibid.

84 *Burduli I.,* Authorized Capital and its Functions, Collection: Theoretical and Practical Issues of Contemporary Corporate Law, *Elizbarashvili N.* (ed.), Tbilisi, 2009, 251 (in Georgian).

85 Sec. 303 (b), Uniform Limited Liability Company Act, 12/07/1995.

formalities are only relevant when it leads to unlawful control and manipulation by the corporation shareholder.[86]

A shareholder is personally liable due to disregarding corporate formalities when such actions mislead a creditor regarding the debtor's identity. In particular, the creditor believes that he/she has a relationship with one company though another corporation is a real debtor. In *Morgan Bros., Inc. v. Haskell Corp.,* the court has decided to pierce the corporate veil, since the two corporations may not be separated from each other when the creditor contacts to the subsidiary company and the parent corporation gets directly involved in correspondence, respectively, the creditor believes that he/she is dealing with the parent corporation. Thus, the inability of following formalities has led to the impossibility of perceiving the subsidiary company as a separate legal entity.[87] Consequently, disregarding the corporate formalities plays an important role in determining the alter ego, as it is related to the separate personality of the corporation.

3.3.2. Germany

In Germany, like in United States, the court may pierce the corporate veil in case shareholder and the corporation do not protect corporate formalities, which lead to an incorrect assessment of the identity of the corporation by the creditor.[88]

The Numberg Regional Supreme Court and the German Federal Supreme Court do not have a uniform approach to the above-mentioned precondition for piercing the corporate veil. The former believes that if the corporation and shareholder cannot be distinguished between each other due to the inability of the shareholder to protect formalities, then the creditor's claim must be satisfied, even though there was no intention to mislead him/her. The latter considers that it is necessary to verify the circumstance that the creditor was not misled.[89]

Commentators use the name "*Sphaerenvermischung"* to refer to the fact when the identity of the corporation is uncertain, which was caused in above-mentioned court disputes due to failure to protect formalities.[90] It is noteworthy that just disregarding corporate formalities generally is not the ground for piercing the corporate veil, but violation of formalities, which cause more severe and undesirable result can be used as a ground to disregard limited liability.[91]

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86 *Smith D. G.,* Piercing the Corporate Veil in Regulated Industries, George Mason Law & Economics Research Paper, № 08, 2008, 8.

87 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 214.

88 Ibid.

89 Ibid, 214-217.

90 Ibid, 215.

91 *McGaughey R. J.,* Disregarding the Corporate/LLC Veil: The Most Litigated Issue in Corporate Law, Portland, 2007, 5-6.

3.4. Commingling of Assets

3.4.1. USA

In *Weeks v. Kerr* case, the court ruled that if the shareholder violated corporate formalities and used company as a channel for its personal profit, the court can also ignore the establishment of a legal entity in order to avoid unfair results.[92]

It is noteworthy that commingling of assets is often related to transferring of the assets, but unlike it the former involves the misuse of separate personality. Such picture is visible when the owner of the property cannot be determined. The inability of the corporation to protect separate personality causes losing its legal independence, resulting in considering corporation and shareholder as one subject.[93]

In order to impose piercing the corporate veil, it is necessary to have commingling of corporate accounting, records or accounts, which create the impression that a corporation and shareholder is one entity. If there is an illusion that the property belongs to the corporation, but in fact it is owned by the shareholder, then in case of bankruptcy, such assets will be assessed as the property of the corporation.[94] In *Re Kaiser* case, the court made the decision based on the above-mentioned principle.[95]

In *Penick v. Frank E. Basil, Inc.,*[96] the court refused to use piercing the corporate veil, as it found that the parent-subsidiary corporation was producing financial records separately, there was no commingling of assets and transactions between the corporations were made with "length of the arm."[97] Similarly, in *Amsted Industries, Inc. v. PollakIndustries, Inc.,*[98] where two corporations had a common shareholder, address, telephone, office and management, but maintained separate accounts, the court did not pierce the corporate veil.[99]

The claimant must also show the element of injustice and fraud since the fact of commingling of assets alone is not enough ground for piercing the corporate veil. For example, in *Palmer Trading, Inc.,*[100] the court found that the plaintiff had failed to prove the third stage of instrumentality theory, namely causality, which indicates that damage to creditor should be caused by defender. At the same time, it should be noted that the plaintiff filed a complaint against a related subsidiary instead of the parent corporation, which is not always unprofitable, when the transaction takes place between the subsidiaries and not by the dominance of the parent corporation.[101]

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92 *Weeks v. Kerr,* 486 NE2d 10, 12, Ind App (1985), *McGaughey R. J.,* Disregarding the Corporate/LLC Veil: The Most Litigated Issue in Corporate Law, Portland, 2007, 3.

93 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 145 (in Georgian).

94 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 211.

95 *In re Kaiser,* 791 F.2d 73, 7th Cir. (1986).

96 *In Penick v. Frank E. Basil, Inc,* 579 F. Supp. 160 D.C. (1984).

97 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 211.

98 *Amsted Industries Inc. v. PollakIndustries Inc.* 382 N.E.2d 393 Ill, App. Ct. (1978).

99 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 211.

100 *In re Palmer Trading Inc.,* 695 F.2d 1012, 7th Cir. (1983).

101 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 212-213.

3.4.2. Germany

The Federal Court of Justice of Germany in one of its decisions[102] stated that limited liability of the company may be neglected in case personal assets of corporation and the shareholder have been commingled.

The Karsluhe Regional Court rejected the corporation's limited liability as the shareholder announced its own property, among them several loans and house, as corporation's property, which was actually bankrupt. The court found that the shareholder failed to distinguish between two assets and could no more argue that the assets belonged to him/her. As a result, the court evaluated the shareholder and the corporation as one unity. In Germany, as in US, the bases for piercing are inaccuracy of financial accounting and records that make it impossible to distinguish the assets of corporations and shareholders from each other. Also, the property whose owner cannot be determined will be part of extended liability and the shareholder cannot claim the ownership on it.[103]

Piercing the corporate veil is not present in Germany when shareholder receives property owned by the corporation. In such situation, the corporation has the right to claim the property from shareholder, which caused inadequate reduction of capital in relation to corporate liabilities.[104]

4. Special Regulations

Piercing the corporate veil is regulated at the normative level in the USA and Germany. Such regulation is indicated in Comprehensive Environmental Response, Compensation, and Liability Act (hereinafter, referred to as *CERCLA*) in USA, whereas in Germany the Joint Stock Corporation Act regulates affiliated entities by *Konzern* law. In some cases, general principles of tort law from German civil law are applied.[105]

4.1. USA

4.1.1. *CERCLA* Comprehensive Environmental Response, Compensation, and Liability Act

CERCLA, also known as *Superfund*, came into force in 1980 to create federal regulation for problems such as the presence of harmful substances in the environment. The majority of the courts agree that the two main objectives of the Act are to restore the place damaged by the harmful sub-

[102] BGH, 22 BGHZ 226. (1956).

[103] *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 215.

[104] Section 30-31 (1), Gesetz betreffend die Gesellschaften mit beschränkter Haftung (GmbHG), 20/04/1892.

[105] "The same duty is held by a person who commits a breach of a statute that is intended to protect another person. If, according to the contents of the statute, it may also be breached without fault, then liability to compensation only exists in the case of fault." § 823 (II), Bürgerliches Gesetzbuch Deutschlands, 01/11/1937.

stances and claim reimbursement of the costs of damage from party who caused such damage.[106] *CERCLA* determines a definition of person, including any corporation and individual, but does not make a special indication about the personal liability of the parent corporation or the shareholder.[107]

The case of *United States v. Bestfoods*[108] has established a standard in which corporations and their shareholders' liability are stated. The court has determined that the shareholder is directly liable according to the sub-paragraph (a) of Section 10 of the *CERCLA*, if he/she is involved with the management of the corporation regarding the harmful substances matters or is liable indirectly by the traditional doctrine of piercing the corporate veil.[109] Corporate veil can be pierced if the use of corporate form is aimed at achieving an unlawful goal.[110]

4.2. Germany

4.2.1. Tort Liability

Paragraph 826 of German Civil Code[111] deals with tort liability ("*Sittenwidrigkeit"*) when intentional damage is made by violating economic or legal rules, which is contrary to moral standards. According to Section 2 of paragraph 823 of German Civil Code,[112] tort is used when private and public order, i.e., "*Schutzgesetz"*, which protects individuals from certain damage, is violated. To use Article 826 from German Civil Code, it is necessary to prove the intention of the shareholder.[113] The courts usually do not ask for evidence that the shareholders were actually trying to harm the creditors, but such conclusion is drawn from the presented objective facts.[114]

The German Imperial Court ("*Reichsgericht"*) ruled that the shareholders are imposed with tort liability when the decision of not financing corporation's capital properly, considering its business field, was a deliberate step so creditors would have been left unprotected during bankruptcy.[115] The

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106 *Klass A. B.,* CERCLA, State Law, and Federalism in the 21st Century, Southwestern Law Review, Vol. 41, 2012, 682.

107 *Bakst D. S.,* Piercing the Corporate Veil for Environmental Torts in the United States and the European Union: The Case for the Proposed Civil Liability Directive, Boston College International and Comparative Law Review, Vol. 19, Art. 4, 1996, 335.

108 *United States v. Bestfoods,* 524 U.S. 51, 52 (1998).

109 *De Blasi M.*, Liability of Parent Corporations, Officers, Directors, And Successors: When Can CERCLA Liability Extend Beyond the Company?, Arizona State Law Journal, № 46:0481, 2014, 481.

110 *United States v. Bestfoods,* 524 U.S. 51, 52 (1998).

111 "A person who, in a manner contrary to public policy, intentionally inflicts damage on another person is liable to the other person to make compensation for the damage.", § 826, Bürgerliches Gesetzbuch Deutschlands, 01/01/1900.

112 "The same duty is held by a person who commits a breach of a statute that is intended to protect another person. If, according to the contents of the statute, it may also be breached without fault, then liability to compensation only exists in the case of fault.", § 823 (II), Bürgerliches Gesetzbuch Deutschlands, 01/01/1900.

113 *Vandekerckhove K.,* Piercing the Corporate Veil: A Transnational Approach, Catholic University of Leuven Legal Faculty, 2007, 115.

114 Bundesgerichtshof ZIP 1992, 694, 1992; Bundesgerichtshof AG, 244, (1989).

115 *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 492.

German Federal Supreme Court ruled that Article 826 of the Civil Code of Germany is violated when shareholder of closed corporation which is not viable, continues to carry out business operations through the corporation despite the fact that it is unable to satisfy its liabilities.[116] Shareholders are also liable for putting off an announcement on bankruptcy, in order to increase the corporation's fund at the expense of creditors for the personal benefit, regardless of the corporation's condition.[117]

4.2.2. Culpa in Contrahendo

German courts also impose liability on parent corporations on the ground of *Culpa in Contrahendo*. In the framework of this doctrine, the parent corporation is liable when it is significantly involved in the signing process of the subsidiary corporation's contract, which misleads the second party or affecting the process crucially by taking into consideration only its interests.[118]

One of the categories of *Culpa in Contrahendo* is liability of the agent. At this time, an agent acting as a representative of one of the parties may be held liable if there is high interest during the signing process of the contract, or the other party has shown great trust to the agent. Unlike the US-based agent's doctrine, Germany's parent corporation is considered as an agent of the subsidiary corporation.

In several of its decisions, Federal Court of Germany stated that if a shareholder of the corporation is involved in the negotiation process and knows about the critical financial condition of the corporation, then the shareholder should notify the other party regarding the condition of the corporation, otherwise the creditor may bring claim against the shareholder in case of bankruptcy.[119] Commentators think that such decisions are supported if they are based on the significant trust of the creditor towards the shareholder. However, if a shareholder believes in his/her business decision, then in this case imposing personal liability within the *Culpa in Contrahendo* is beyond the scope of this doctrine. That is why Federal Supreme Court of Germany has explained that direct business interest means when shareholder manages the corporation as he/she would have managed his/her personal property.[120]

4.2.3. Konzern Law

The real codification regarding affiliated entities[121] law was implemented in 1965 as *Konzern* Law ("*Konzernrecht"*). *Konzern* Law, among other issues, regulates the liability of a corporation towards credi-

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116 Bundesgerichtshof, W. Ger., 1957 WM 460, 462 (1957); Bundesgerichtshof, W. Ger., 1979 NJW 2104 (1978), in: *Schiessl M.*, The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 492.

117 Ibid.

118 *Vandekerckhove K.,* Piercing the Corporate Veil: A Transnational Approach, Catholic University of Leuven Legal Faculty, 2007, 383.

119 Bundesgerichtshof, W. Ger., 1984 NJW 2284 (1984), in: *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 495.

120 Bundesgerichtshof, W. Ger., 1985 WM 1526, 1528 (1985), in: *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 495.

121 The present sub-paragraph concerns only widely-held corporation with the exception of the part of qualified de facto "Konzern".

tors. The 3rd book of Stock Corporation Act contains the rules on the conflict of interests in a group of corporations that require a special regulation according to the German legislature. The *Konzern* is created when on the one hand, there is one controlling corporation and on the other hand there are one or more controlled companies. Balance is violated when a majority shareholder has an interest in one or two corporations and there is a risk that dependent corporation is under the influence of another corporation.[122]

Control is revealed by the ownership of majority of shares. In the absence of a majority shareholder, control is considered the case when the minority conducts direct effect through contract or representation in the supervisory board.[123]

4.2.3.1. Contractual *Konzern ("Vertragskonzern")*

Within contractual *Konzern,* corporations select the agreement, considering the special legal regime of the group. There are many forms of contracts. Different agreements define different quality of economic and legal dependence, therefore, it is followed by different legal consequences.[124] Under the Domination contract ("*Beherrschungsvertrag"*), the subsidiary corporation confirms that its management will be conducted by the parent corporation. Thus, the controlling shareholder has the right to manage subsidiary company, taking into account the interests of parent and other affiliated entities, but shall not place the viability of the subsidiary corporation at risk.[125] There is also a profit allocation contract. Under both contracts, the controlling corporation is obliged to reimburse the annual losses to controlled corporation, which can be achieved if the controlling corporation creates reserve funds.[126]

In the absence of such agreements, German corporate law makes a difference between de facto and qualified de facto *Konzerns*, with the latter being developed by the commentators of the Federal Supreme Court of Germany.[127]

4.2.3.2. De Facto Konzern (Faktischer Konzern)

The corporations that are related in reality but do not have a contract, are de facto dependent on each other.[128] The imperative rules of the Stock Corporation Act[129] regulates de facto *Konzern* and obliges the parent corporation to reimburse the subsidiary any loss or damage caused by transactions where the parent

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122 *Vandekerckhove K.,* Piercing the Corporate Veil: A Transnational Approach, Catholic University of Leuven Legal Faculty, 2007, 36.

123 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 97 (in Georgian).

124 *Vandekerckhove K.,* Piercing the Corporate Veil, European Company Law, Vol. 4, Issue 5, 2007, 192.

125 *Schiessl M.,* The Liability of Corporations and Shareholders for the Capitalization and Obligations of Subsidiaries under German Law, Northwestern Journal of International Law & Business, Vol. 7, Issue 3, 1986, 497.

126 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 98 (in Georgian).

127 *Alting C.,* Piercing the Corporate Veil in American and German Law — Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 239.

128 *Vandekerckhove K.,* Piercing the Corporate Veil, European Company Law, Vol. 4, Issue 5, 2007, 192.

129 § 311, § 317, Aktiengesellschafts Gezets, 01/11/1937.

corporation was liable. To determine the damage, it is necessary to evaluate all the transactions carried out with the affiliated corporation and other legal entities where the parent corporation was involved.[130] Furthermore, it shall be explained whether the transactions were beneficial for the subordinated company.[131]

Therefore, within de facto dominance, the law defines that damages may be claimed only by a controlled corporation that must prove that certain transactions have resulted in respective damages. In most cases, it is difficult to say that the specific transaction was not beneficial for the controlled corporation and this exact transaction caused an unfortunate result. Consequently, commentators consider that the legal significance of de facto *Konzern* is less effective because of difficulty of burden of proof and the fact that it is allocated on controlled corporation.[132]

4.2.3.3. Qualified De Facto Konzern (“*Qualifizierter Faktischer Konzern”)*

Since the Stock Corporation Act does not include closed corporations and societies, German courts spread same liability when the subsidiary corporation is a closely held corporation and the parent corporation is the widely held one.

Since the 1970s, German courts have clearly intervened and developed a separate doctrine known as qualified de facto *Konzern.*[133] However, in *Bremer Vulkan*,[134] which satisfied all the preconditions of qualified de facto *Konzern*,[135] the Federal Court affirmed the new approach, according to which the parent company's liability before the creditors of the subsidiary is allowed only in the case when interference of the parent company violates the autonomous existence of the subsidiary – “disastrous involvement”.[136] Consequently, without sufficient explanation, the Federal Court changed its twenty years of practice and rejected the doctrine of qualified de facto *Konzern*.[137]

5. Piercing the Corporate Veil in Georgia

5.1. General

Piercing the Corporate Veil is actively discussed as the basis for imposing the personal liability of shareholder within the last decade in Georgia. The issue is studied both in theory and practice. Especially, the decisions made by the Supreme Court of Georgia has increased the interest towards the institute.

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130 *Alting C.,* Piercing the Corporate Veil in American and German Law ― Liability of Individuals and Entities: A Comparative View, Tulsa Journal of Comparative and International Law, Vol. 2, Issue 2, 1995, 238.
131 Ibid, 239.
132 Ibid, 238.
133 *Graefe R. R.,* The Liability of Corporate Groups in Germany, Connecticut Law Review, Vol. 37, 2005, 795.
134 *Bremer Vulkan,* BGH Sept. 17, 2001 - II ZR 178/99 (2001).
135 *Graefe R. R.,* The Liability of Corporate Groups in Germany, Connecticut Law Review, Vol. 37, 2005, 799.
136 *Zubitashvili N.,* Liability of Shareholders for Corporate Obligations within Insolvency Proceedings – Exception Cases from Limited Liability Principle, Tbilisi, 2016, 100 (in Georgian).
137 *Graefe R. R.,* The Liability of Corporate Groups in Germany, Connecticut Law Review, Vol. 37, 2005, 800.

5.2. The Development of the Concept of Piercing the Corporate Veil in Georgia

5.2.1. The Law of Georgia on Entrepreneurs

The first edition of the Law of Georgia on Entrepreneurs, adopted on 28 October 1994, contained regulation regarding personal liability of shareholders. Namely, according to Article 3.4.,[138] shareholders were directly liable before the creditors, "if the form of limited liability was misused."[139] In particular, the abuse was considered "first and foremost commingling of assets or the undercapitalization of the company required for its functioning." Therefore, due to the terminology of the law, abuse could have been considered other cases as well.[140]

Under the Law on Entrepreneurs, adopted on June 9, 1999, the rule of piercing the corporate law has become more specific and the grounds for using the doctrine has been determined. In particular, abuse was considered "if there was no bookkeeping of accounting, which clearly defines which assets and obligations belong to which corporation."[141]

Under the Law on Entrepreneurs, adopted on March 14, 2008, the special framework of piercing the corporate veil has been replaced by the general abstract provision. Therefore, the definition of the term of misuse has been removed from the law,[142] which meant that courts have broad discretion to flexibly define and determine what the misuse is based on every specific case.[143] Obviously, it would have been impossible to define every single case by specifying the law. Consequently, according to this article, liability shall be imposed on the limited shareholder (limited partner, partner of the LLC and the shareholder of the JSC) in case one abuses the legal forms of limited liability.[144]

At the same time, it should be noted that the original version of the Law on Entrepreneurs included Article 17, which regulated *Konzerns* and affiliated entities. The article regulated that *Konzern* was present, if one enterprise participated in another enterprise with more than twenty-five percent.[145] In accordance with one of the paragraphs of this article, in case one enterprise held at least fifty percent of another enterprise in Georgia, then the principal enterprise (enterprise holding majority of shares[146]) had to reimburse annual losses of the non-principal enterprise (second collaborator enter-

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138 Article 3.4., Law of Georgia on Entrepreneurs, ed. 28/10/1998, 28/10/1994.

139 *Tchanturia L.,* Piercing Liability of the Shareholder for Tax Infringement of the Corporation — Attempt to Implement Piercing the Corporate Veil in Judicial Law, The Grounds of Civil Law in Georgian Judicial Practice, *Zarandia T.* (ed.), Tbilisi, 2016, 280 (in Georgian).

140 *Zubitashvili N.,* Evaluation Standard of Paragraph 6 of Article 3 of the Law of Georgia on Entrepreneurs, through the Doctrine of Piercing the Corporate Veil, Journal of Law, № 2, 2014, 107.

141 Article 3.4., Law of Georgia on Entrepreneurs, ed. 09/06/1999, 28/10/1994.

142 *Tchanturia L.,* Piercing Liability of the Shareholder for Tax Infringement of the Corporation — Attempt to Implement Piercing the Corporate Veil in Judicial Law, The Grounds of Civil Law in Georgian Judicial Practice, *Zarandia T.* (ed.), Tbilisi, 2016, 280 (in Georgian).

143 *Zubitashvili N.,* Evaluation Standard of Paragraph 6 of Article 3 of the Law of Georgia on Entrepreneurs, through the Doctrine of Piercing the Corporate Veil, Journal of Law, № 2, 2014, 107.

144 Article 3.6., Law of Georgia on Entrepreneurs, ed. 06/06/2018, 28/10/1994.

145 Ibid, Article 17.1., ed. 28/10/1994.

146 Ibid, Article 17.2.

prise[147]). Principal enterprise also had to compensate to outside shareholders the losses of the non-principal enterprise, which resulted from the agreements of the principal enterprise or other events, etc.[148]

This method is similar to the German *Konzern* Law, where the interference of controlling corporation and quality of control played a crucial role in imposing liability by piercing the corporate veil. Moreover, within the scope of the above mentioned article, in case of participation with seventy-five percent share, the law defined that the limited shareholders of the corporation are liable as solidary debtors together with the enterprise before non-principal enterprise and third parties. There would not have been a liability if the manager of the independent enterprise acted the same.[149] Consequently, like in German *Konzern* law, it was necessary to perform the fiduciary duties in good faith in Georgia as well. However, as a result of the reform of the Law on Entrepreneurs in 2008, Article 17 has been abolished and the issue of damaging creditors as a result of domination by one enterprise on another has remained without regulation.

5.2.2. Judicial Practice

The Supreme Court of Georgia made two decisions on 6 May, 2015. Based on enforced ruling of the criminal court, shareholders of limited liability company, among them director of the company, have been accused of deliberately avoiding payment of extremely large amount of taxes.[150]

The Court used the Article 3.6. of the Law on Entrepreneurs and did not consider an Article 992 of the Civil Code of Georgia and ruled out the tort liability, which was unexpected, as there was unlawful action, damage and causal connection. However, it should be noted that the Court of Appeals had satisfied the claimant's request with tort liability.[151]

The Supreme Court has given preference to Article 3.6. of Law on Entrepreneurs, which considers piercing the corporate veil. The court found that that the misuse of the limited liability form shall be widely interpreted and it shall cover cases, when the partner of the LLC aims to avoid the payments of taxes, i.e., a corporation is used as the means of undeclared income by the shareholder. Under Article 3.6. of Law on Entrepreneurs, the shareholder may be personally liable before the creditors for damages that occurred as the result of the afore-mentioned matter.[152]

At the same time, the court discussed the form of liability of the shareholder, as well. In spite of the fact, that the Court of Appeal used the solidary liability, which was also indicated as the form of liability in the 1999 edition of the Law on Entrepreneurs, the Supreme Court found that the form of vicarious liability was reasonable,[153] which lacked arguments in the ruling.

147 Ibid, Article 17.2.
148 Ibid, Article 17.3.
149 Ibid, Article 17.4.
150 Decision of May 6, 2015 № AS-1307-1245-2014, Supreme Court of Georgia; Decision of May 6, 2015 № AS-1158-1104-2014, Supreme Court of Georgia.
151 *Tchanturia L.,* Piercing Liability of the Shareholder for Tax Infringement of the Corporation — Attempt to Implement Piercing the Corporate Veil in Judicial Law, The Grounds of Civil Law in Georgian Judicial Practice, *Zarandia T.* (ed.), Tbilisi, 2016, 277 (in Georgian).
152 Ibid, 278.
153 Ibid, 279.

6. Conclusion

The main flaws and problems associated with the concept of piercing the corporate veil have been identified in the present article. Piercing the corporate veil restores fair balance, in particular, in case of relevant circumstances and imposes personal liability on the shareholder.

The practices of leading countries, such as Germany and the United States, shall be implemented in Georgia. It is necessary to use piercing the corporate veil doctrine accurately, which is possible with the general normative regulation of Law on Entrepreneurs and sharing methods and approaches based on practice by the legal systems of different countries.

Afore-mentioned approach would have ensured the rapid and correct development of piercing the corporate veil in Georgian legal space, which is mandatory because of the popularity of the doctrine. In conclusion, it should be noted that it is necessary to establish uniform approach of court practice, as well as frequent research with new perspectives in legal literature, considering the achievements of other countries.

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Regulation of the Risk of Negative Occurrences at the Stage of Contract Performance –Reference to Economic Analysis of Law

This paper focuses on the determination of regulation of potential risks at the stage of contract performance during the development of law-of-obligations relations. It examines the allocation of risks related to the performance of obligation. The paper discusses approaches of Anglo-American (common law) and German legal systems; however, the leading role is accorded to economic analysis of law-of-obligations relations, which mainly concerns the determination of practical importance of legal regulation. Within the scope of this area of research, the paper offers an analysis of respective articles of the Civil Code of Georgia in conjunction with comparable or similar solutions of common law or German law systems.

Key words: *Performance of a Contract, Economic Analysis, Behavioural Standard, Risk Allocation, Substantial Performance, Impossibility of Performance, Interpretation of a Contract.*

1. Introduction

Contemporary civil transactions give rise to different interests of persons and it becomes necessary to create various legal, political and economic mechanisms to balance them. The instrumentality function of law is accomplished through its legal mechanisms of regulation, which create the single concept of risk allocation. Presently, the foregoing has become the focus of economic analysis of law, the current methodology of the study of law. Economic thinking was brought into the field of legal studies during the 1910s and 1920s. In 1970s, it was established as a separate trend, when legal community addressed the question of efficiency of legal rules. This methodology investigates practical importance of legal rules and employs economic categories to this end.[1]

The paper aims at discussing the aspects of risk allocation and thus enhancing the systemic vision of legal challenges, elucidating the practical importance of balancing the interests of the parties and interdisciplinary nature of the problem through comparison of traditional and modern opinions, and relevant comparative analysis. Identification of the risk of occurrence of a negative event at the stage of performance of obligation and efficient regulation of this risk are of particular importance for the whole system of private law relations as the allocation of risk between the parties to a civil transaction is the precondition of balancing their different interests. Based on this, the paper focuses on regu-

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1 *Kornhauser L.*, The Economic Analysis of Law, Stanford Encyclopedia of Philosophy, 2001, 2, <https://plato.stanford.edu/entries/legal-econanalysis/>, [17.07.2017].

lations concerning law-of-obligations relations in close connection with economic analysis of law. Furthermore, it will also discuss various cases of allocation of risk envisaged by Georgian civil law.

The process of performance of a contract and the problem of regulation of potential negative consequences are discussed in the paper on a step-by-step basis. Initially, attention is paid to economic categories of a contract, practical importance of the terms and conditions of a contract for its classification and the principle of risk allocation. At the next stage, the concept of an average reasonable person is described, which in fact is the manifestation of the duty of bona fide behaviour. This concept is unconditionally meaningful for every case of development of contractual relationships, amongst them, for the assessment of performance of an obligation. Consequently, the paper discusses the question of exercise of its civil law right by the party in the course of performance of a contract, within the framework of this very concept. A separate chapter is dedicated to the concept of impossibility of performance or frustration, as it can be said that this concept is the most topical performance-related risk factor. The same chapter discusses the standard of allocation of the risk of accidental loss/damage of a property. Incomplete nature of modern contracts or high level of their dependence on external factors obviously complicates the process of performance, which, in its turn, provides for the necessity of interpretation of the will of the parties. The scope and alternatives of interpretation of the will are regarded as one of the most important challenges of modern reality and can even be presumed as a risk-factor, distinctive to performance phase. Hence, these issues are discussed in a separate chapter of the paper allowing for clear visualisation of different complications arising during the performance of an obligation. The last part of the paper focuses on the specific nature of contractual relationship in a non-routine situation, upon the participation of a third person in the course of performance, which makes evident the practical implication of this external factor and specific nature of general standard of behaviour for the purpose of performance of a contract.

2. Process of Performance of a Contract

Performance of a contract covers three components, viz., time of performance, place of performance and quality of performance. Each of these components is provided for by the Civil Code of Georgia (CCG). However, the issues that are of major importance for the purpose of ensuring contractual equilibrium and fair allocation of contractual risk should be regulated in detail. Hence, the chapter below aims at identifying legal and economic benchmarks crucial for the process of performance of an obligation.

2.1. Contract and its Constituent Terms and Conditions

The main function of a contract is to ensure the performance of a promise/assumed obligation. As a general rule, a contract provides for the standard of performance and responsibilities of the parties. At the same time a contract serves the purpose of advance allocation of potential risks and selection of legal remedies for default cases. And lastly, a contract is the instrument for the reconciliation of potentially conflicting individual interests.[2]

[2] *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 3.

2.1.1. Types of Contracts according to Economic Analysis

For the purpose of economic analysis of law[3] (hereinafter – the economic analysis), a contract is a transaction for the exchange of resources and its main function is efficient allocation of these resources. Consequently, the key aspect of a contract is securing the efficient behaviour of the subjects, participating in the process of exchange. When searching for efficient behaviour, the set of circumstances is evaluated from two perspectives, viz., from that of an individual, who is the maximiser of personal proprietary interest, and from the viewpoint of contracting parties with common interest. Common will of the parties is the key standpoint of legal protection for traditional doctrines of law – both common-law and European. As per the definition of economic analysis,[4] without legally protected and enforceable rights, the persons face the risk of making inefficient decisions as it is possible for this preference to be given to obligations, subject to immediate or concurrent performance.[5] Legal protection of a contract aims at excluding mala fide behaviour of a person against a counter party, provision for efficient terms and conditions, identification of the party bearing the highest risk and oversight of contractual negotiations or further judicial proceedings. From the perspective of neoclassical economics,[6] a contract is an autonomous agreement and essentially is the risk allocation mechanism.[7] Specifically, when agreeing upon mutual rights and obligations and their validity period, the parties also create the system of allocation of risks associated with the performance of obligations.

In economic analysis, where the notions of a consumer and a manufacturer are dominating, a distinction is made between discretionary and relative contracts. A contract is discretionary when its content is isolated and does not depend on circumstances. It is relative when its content and further development depends on created circumstances or external factors. Furthermore, most of the contracts executed in modern civil relations are of relative nature.[8] This differentiation is based on various criteria: 1) Commencement, duration and accomplishment; 2) Measurability and predictability; 3) Planning; 4) Allocation of resources vs. Distribution of gain/burden; 5) Mutual dependence, future cooperation and solidarity; 6) Number of participants and their personal relationship; and 7) Power.[9] For example, a contract is discretionary when the beginning and the end thereof are easily definable. Also, discretionary is the contract in the case of sales between two persons when immediate performance is required from each party. Furthermore, as already mentioned, mostly the relative contracts are distinctive of modern civil transaction, when it becomes necessary to separately assess each of the above components. However, overall, a relative contract has three main components: certainty of the content, validity period and type of investment.

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3 *Posner R. A.,* Economic Analysis of Law, 7th ed., US, 2007, xxi.

4 Ibid.

5 *Posner R. A.,* Economic Analysis of Law, 7th ed., US, 2007, 93.

6 For the analysis of neoclassical economics, see *Arnsperger C., Varoufakis Y.,* What is Neoclassical Economics? The Three Axioms Responsible for its Theoretical Oeuvre, Practical Irrelevance and, thus, Discursive Power, Savez ekonomista Vojvodine, Vol. 53(1), 2005, 6.

7 *Macneil I. R.,* Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a Rich Classificatory Apparatus, Northwestern University Law Review, Vol. 75, № 6, 1980-1981, 1020.

8 Ibid.

9 Ibid, 1025.

Some authors[10] differentiate between classical, neoclassical and relative contracts. Specifically, if in classical system, a contract is being assessed for a specific moment, the identity and status of a party are of less importance, the list of remedies is limited and the focus is shifted to formal documentary part. In neoclassical system, it is already possible to speak about predictability. In this case, a contract is being assessed with its full development. Owing to the duration and complexity of a contract, the classical and neoclassical models were gradually substituted by the above model of relative contract, where the analysis of contract-related costs and specificity of governance of contractual relationships are of importance.

2.1.2. Practical Importance of Contract Terms and Conditions

Of the criteria mentioned above, attention should be paid to allocation of gain and burden, which is quite different in each case. Allocation of risk, related to the object of performance, is the case of distribution of burden, which is apparent in terms and conditions of a discretionary contract, as each party is accorded the ordinary risk, inherent to his/her share of performance. Specifically, market risk associated with the ownership of a property (e.g., change of market price of a property) passes to the buyer upon execution of a contract and the one associated with physical condition of a property – after handing over thereof. In its turn, the risk associated with delivery/handing over/shipment of a property is associated with a seller. However, such allocation of burden may change when, for example, the performance is deferred. This means that there are circumstances which affect the ordinary process of allocation of contractual risk. E.g., the absence or ambiguity of consideration[11] makes due performance by the respective party less guaranteed and hence the deterioration of financial standing gives rise to a legitimate claim for the allocation of risk for the counterparty. A separate mention can be made of contracts that depend on customer-demand, when production expenses of goods (if there are any) also become subject to allocation as a result of the decrease in market demand, unlike large production relations when the conveyer principle is mostly employed for the process of distribution of gain/burden.

The cost of contract execution or transaction is the component which plays an important role at the stage of formation of a contract. Transaction costs also include the costs of governance of contractual relationships,[12] which is important from the point of view of practical organisation. Transaction costs differ according to the contract to be executed. Also, important components are the identity of the counterparty, existence of demand and alternative means of supply, risk related neutrality and intensity of negotiations. E.g., in commercial contracts, one of the leading contracting factors is the economy of production costs.[13]

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10 *Willimason O. E.,* Transaction-Cost Economics: The Governance of Contractual Relations, The Journal of Law and Economics, Vol. 22, № 2, 1979, 236.

11 *Quid pro quo* (something for something) — for more details about the doctrine of consideration, see *McGovern W. M.,* Contract in Medieval England: The Necessity for Quid pro Quo and a Sum Certain, The American Journal Legal History, Vol. XIII, 1969, 5.

12 *Coase R. H.,* The Nature of the Firm, Economica, New Series, Vol. 4, № 16, 1937, 394.

13 *Willimason O. E.,* Transaction-Cost Economics: The Governance of Contractual Relations, The Journal of Law and Economics, Vol. 22, № 2, 1979, 237.

Based on the complexity of performance, i.e., action(s) to be performed, contracts can be differentiated as follows according to their content: 1. complex or mixed contract, which includes several actions independent from each other; 2. contract, the performance of which requires the performance of several, interrelated actions aiming at a single purpose; and 3. contract, for the performance of which only a single action is to be performed.[14] The nature and complexity of the action to be performed affects the allocation of contract risk. Specifically, if the obligation is undividable, in this case, as a general rule, it is the obligor who assumes the risk of negative consequence of faulty/undue performance, including the obligation to bear the expenses of correcting the fault. This is particularly topical in the case of the contractor's agreement, when the motive of due performance of work should be ensured. However, it should as well be taken into consideration that, in the case of partial performance, allowing for refusing the compensation of performed work definitely generates unfair contractual consequence as neither of the aggrieved party can be enriched unjustly.[15] Consequently, if the contract was not essentially violated, the obligation of acceptance of performed share arises. Concurrent with this reasoning is the stipulation of Article 405 of the CCG, under which if obligation was breached only partially the obligee may refuse the performance of the contract only when the performance of the remaining share of the obligation became meaningless for him/her. However, it is not clear whether this stipulation implies the obligation to accept performed share, provided that the action to be performed is dividable. Furthermore, it is a separate issue whether this obligation can arise only in the case of short-term scheduled performance or long-term recurrent performance as well. Furthermore, no matter whether the obligation is dividable or not, the implied obligation to perform it duly and in good faith remains unchanged.

The contract period is one of the key components of the content of contractual relationships. The contracts are divided into term contracts, viz., made for a certain period and contracts made for an indefinite period. Furthermore, term contracts can be further subdivided into short-term and long-term contracts. In economic analysis, contracts made for an indefinite period are called contracts with indefinite future. It is worth mentioning that pre-contractual relationships that are traditionally regarded as independent legal relations constitute the beginning of a contract as per economic analysis. Here, the commencement, flow or termination of contractual relationships is not strictly delimited, accounting for the complicated process of contract planning. Hence, from economic point of view, the moment of execution of a contract and the expiry of contract term are of a formal nature. This formality is noticeable in certain provisions of the effective Georgian civil law. E.g., Article 605 of the CCG,[16] under which a contract made for three years can be extended for an indefinite period; or the existing practice of contracts revolving on a yearly basis. In certain cases, ambiguity in a contract term can be explained through placing the contract within the framework of the legal regime of a conditional transaction, provided that contract termination/extension is associated with occurrence or non-occurrence of a certain condition (for example, change in market price). The provisions of the CCG which provide for the right to claim the extension of contractual relationships is also worth mentioning. Mention should be

14 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 510.
15 Ibid, 514.
16 Civil Code of Georgia, Parliament of Georgia, Parliamentary Gazette, № 31, 24/07/1997.

made of Articles 559, 560, 569 and 593 of the CCG about long-term rent and contractual lease. The analysis of these articles demonstrates that in the case of existence of a bilateral will – acceptance of an offer – contractual relationships are extended. Furthermore, also admissible is the presumption on the extension of a contract for an indefinite period, which evidences the will of the legislature to maintain contractual relationships even in the case of ambiguity of the will of the parties. In conclusion, it should be said that all the above-mentioned points demonstrate how practically important and essential a certain term or condition of a contract can be for the outcomes of a contract. Furthermore, unlike the traditional approach, quite often the essentiality of the term or condition is defined by a set of internal or external factors, for which only the law and will of the parties are decisive sources.

2.2. The Concept of an Average Reasonable Person

Performance of an obligation is the key standard of performance of an obligation with due care and diligence both in continental and common law systems. This chapter discusses an objective standard of behaviour regarding each component of performance and describes respective consequences in the context of risk allocation.

2.2.1. Notion of an Average Reasonable Man

The notion of reasonability or rationality of a person is worthy of note to the extent that it depends on a set of circumstances and does not constitute an abstract category. It is somewhat delimited from the concepts of good faith and contractual equity.[17] The concept of a reasonable, commonsensical person serves practical purposes of an action in the course of performance. Modern philosophy sometimes refuses to admit the direct connection between reasonable and rational.[18] Specifically, the choice of behaviour, which is logical and rational, can at the same time be reasonable for a specific case and vice versa. The possibility of convergence of these categories is mostly visible in contract law. Some believe that reasonability is morally motivated rationality.[19] It should be mentioned that this notion goes back to sixteenth and seventeenth century England, where the phrase "beyond reasonable doubt" first originated.[20] As per modern understanding, reasonability implies indefinite future, alternatives of human behaviour and potential mistakes as well. Reasonability means *recta ratio*[21] of an action. It can be said that the notion of an average reasonable person is a fiction of law. In economic analysis this notion is equalled with socially desirable behaviour as reasonable means averaged and balanced at the same time. However, if a rationally acting person is the maximiser of own interest and

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17 *Zorzetto S.,* Reasonableness, The Italian Law Journal, Vol. 01, № 01, 2015, 107.
18 Ibid, 110.
19 Ibid, 117.
20 Ibid, 119.
21 It should be mentioned that Dutch scholar of the sixteenth century, *Hugo Grotius*, who first voiced the idea of rational *ius naturale*, would explain, that *ius naturale* dictates *recta ratio*, when an action, be it rational or not, has moral basis; see *Rommen H. A.,* Natural Law: A Study in Legal and Social History and Philosophy, *Hanley Th. R.* (trans.), US, 1998, 71.

is oriented towards balancing the allocation of burden/gain, an average reasonable person cooperates with others and is also interested in attaining fair terms and conditions. Consequently, as far as the consequences of human behaviour for others are concerned, the notion of an average reasonable person can easily be added to the obligation of good faith.[22] To sum up, it can be said that the notion of an average reasonable person constitutes a category reflecting objective values in one case and subjective equity in the other. In this light, two main categories of contract risk are identified: a) risk associated with an event and/or situation being independent from human behaviour; and 2) risk associated with human behaviour, capabilities or mental or other condition of a person.

2.2.2. Behavioural Standard in the Performance of Obligation

In certain cases, the standard of human behaviour is embodied in the respective rules of the CCG. At the same time, it is natural for optional rules of the law of obligation,[23] providing for exemplary behaviour, to contain a stipulation that something else may follow from the content of the contract or essence of the obligation/circumstances. Respectively, during the performance of an obligation, the law, party agreement and essence of the obligation/contract related circumstances are the alternative sources for determination of human behaviour. E.g., a condition related to the time of performance can be presumed to be essentially based on contract related circumstances, irrespective of whether the parties made a stipulation in this regard. Also, if the parties have not agreed about the priority order of performance, it depends on the content of the obligation, whether it should be performed first or not. Specifically, in this case, the content of the obligation concerned is considered, i.e., conditioning or conditioned. Unless otherwise agreed, the obligations covered by a sales contract, as a general rule, are concurrent and competitive. In the case of, a labour contract, for example, performance of work is a precondition for the payment of remuneration.[24] Determination of the foregoing is also important for the identification of the breach of obligation.

As regards the place of performance, Georgian legislature decided that preference is to be given to the obligor's place of business or habitual residence. However, the contrary is admissible if the foregoing is not directly envisaged by a contract. Respectively, an obligee is required to take a property away from the obligor and the former becomes the bearer of the risk of performance from the moment of transfer of the property. This mode of risk allocation changes when the obligor is ready to hand over the property, but the obligee delays its acceptance.[25] The approach is different with the performance of a money obligation as in this case the obligor is responsible for the performance at his/her own risk and expense.[26]

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22 For further details, see: good faith — *Kereselidze D.,* Most General Systemic Notions of Private Law, Tbilisi, 2009, 83 (in Georgian).

23 See CCG, Articles 362 and 365.

24 *Anson W. R., Corbin A., Arthur L.,* Principles of the Law of Contract with a Chapter on the Law of Agency, NY, 1924, 3.

25 See CCG, Article 393.

26 *Pieck M.,* A Study of the Significant Aspects of German Contract Law, Annual Survey of International & Comparative Law, Vol. 3, 1996, 118.

When there is no expressed agreement of the parties, the content of the contractual relationship becomes the source for determination of contract terms and conditions. Hence, the legislature obliges an average reasonable observer and judicial practice to generalise the performance distinctive to the contract and relevant risks. E.g., in English legal system, it is characteristic for a sales contract that it is the buyer's obligation to organise the acceptance of a property.[27] In Georgian civil law, the criterion for the determination of the place of performance is said to be the type of the property subject to transfer/acceptance – whether it is individual or generic. In the case of an individual property, the place of performance is the location of the property, which guarantees the safety of the object of performance and passing of the risk from the obligor to the obligee upon its transfer/acceptance.

The behavioural standard regarding the quality of the object of performance is mainly determined by party agreement. Otherwise, the focus is made on the fitness of a property for the purpose of the contract or average consumption fitness. It should be mentioned here that Section 434.1(2) of the German Civil Code[28] (BGB) stipulates that it is the direct obligation of the seller (producer/a person involved in selling process) to communicate the objectively available information about the specific characteristics or condition of the property to the buyer. This stipulation is absent in the relevant article of the CCG.[29] Faulty performance, including the delivery of a different property or lesser amount thereof, is present when there is no agreement on accepting other performances. Furthermore, such an agreement can be reached either before or after the performance. In the case of delivery of the other property, practical connotation of the autonomy of the will of the parties for legal consequence is apparent as one and the same action may constitute both the breach of obligation and termination of obligation through acceptance of another performance.

Contractual circumstances may also provide whether it is possible for a third person to execute the performance and stipulate the legal status of the latter. According to general behavioural standards, when business and professional characteristics of a person constitute grounds for the execution of a contract with him/her, this person cannot enjoy the right to delegate performance. This is evidenced by Article 371.1 of the CCG, according to which when it does not follow from a law, a contract or nature of the contract that the obligor is supposed to personally perform the obligation, this obligation may also be performed by a third person. Regulation of the risk associated with the performance under the involvement of a third person is contained in Article 398 of the CCG, under which article an obligor should be liable for the actions of his/her lawful agent and those other persons he/she employed for the performance of his/her obligation, to the same extent /she would have been liable in the case of own faulty actions.

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27 *Anson W. R., Corbin A., Arthur L.,* Principles of the Law of Contract with a Chapter on the Law of Agency, NY, 1924, 8.

28 German Civil Code BGB, Federal Ministry of Justice and Consumer Protection in cooperation with juris GmbH, 18/08/1896, <http://www.fd.ulisboa.pt/wp-content/uploads/2014/12/Codigo-Civil-Alemao-BGB-German-Civil-Code-BGB-english-version.pdf>, [01.01.2018].

29 Comp. Article 488, part 1 of the CCG: "A thing is flawless in title if it is of the agreed quality. If the quality is not agreed in advance, the thing shall be deemed flawless if it is suitable for the use stipulated in the contract or for ordinary use".

Therefore, as far as the assessment of behaviour in the course of performance of an obligation is subject to discussion of a specific case, provision for the duty of due care and due diligence of a party in the course of exercising the right is of paramount importance.

2.2.3. Unilateral Discretionary Power of a Party

Exercise of civil power by a party is one of the pressing questions of modern contract law. Unilateral power can be understood as a lawful option of a party to influence the counterparty or the outcome of contracts. Economic analysis identifies unilateral and bilateral power of a party.[30] The source of unilateral power is absolute ownership (fee simple absolute), whilst the source of bilateral discretionary power is a contract as this power is realised during the exchange of wealth. In this case, the term "discretion" is used to express potential unilateral will. The factors conditioning this will partially constitute the contract terms and conditions concerning time, place and quality. In effect, the unilateral power of a party is created by default and/or undue performance of an obligation. Economic analysis calls the secondary right to claim, originating after the execution of a contract, unilateral power of the party. Finally, there is an opinion about the fluctuation of the equilibrium of interests of the parties as it is presumed that contractual positions exist only for a given moment.

Provision for the right to alternative performance or alternative obligation can be regarded as a manifestation of discretionary power of a party during the performance of an obligation. The first case, as a general rule, concerns the object of contractual obligation and the other concerns some term or condition of performance. The right to alternative performance is in play when, even if the agreed performance is predominant, a stipulation about the option of substitution of the object of obligation or its essential characteristic within a reasonable period (performance option) is provided for at the same time. Furthermore, a party enjoying performance option is not required to take account of the interests of the counterparty about the enjoyment of the option. However, if it is deemed impossible to perform the priority action, the obligor is not liable to refer to an alternative performance to maintain contract and not have it terminated on the basis of impossibility of performance.[31] In the case of enjoyment of performance option, the object of performance is being substituted and in this case the obligation is exhausted through acceptance of the other performance.[32] The content of performance option is included in Article 428 of the CCG, according to which the obligation relationship terminates when an obligee accepts some other performance in lieu of performance envisaged by the obligation. Acceptance of other performance is interpreted in Georgian legal literature as innovation,[33] when an obligor is entitled to carry out and the obligee, on his/her part, is entitled to accept the other performance. It is noteworthy that the above article does not contain any reference to the necessity of provision for

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30 *Macneil I. R.,* Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a Rich Classificatory Apparatus, Northwestern University Law Review, Vol. 75, № 6, 1980-1981, 1032.

31 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 507.

32 *Martin S., Randall L. A. E.,* Law of Contracts, NY, 1912, 602.

33 *Chanturia L., Zoidze B.,* Commentary on the Civil Code of Georgia, Third Book, Tbilisi, 2001, 517 (in Georgian). Comp.: *Dzlierishvili Z., Tsertsvadze G., Robakidze I., Svanadze G., Tsertsvadze L., Janashia L.,* Contract Law, Tbilisi, 2014, 351 (in Georgian).

such a possibility/option from the very outset as well as its connection with any objective circumstance. The analysis of the provision evidences that the case concerns the change of basic feature of the object of performance, which was not agreed upon from the very outset and, hence, it is possible for the foregoing to be done even in the course of performance. Under similar Section 364 of the BGB, acceptance of another performance and termination of performance claim may be conditioned by the circumstances of the case. Furthermore, it is possible to provide for the right to do some other performance in lieu of assumed obligation at the very beginning of contractual relationships. In the commentary of the German Civil Code, the foregoing is nominated as the right to substitute performance.[34] Part 2 of the above article[35] regulated the obligor's right to offer alternative performance to the obligee to cover the assumed obligation. At the same time, attention is paid to the obligee's obligation to exercise due diligence for the satisfaction of his/her claim through alternative performance. The above legal option is an apparent example of identification of the priority of the purpose of obligation and clarifies to what extent the necessity of legitimating reliable behaviour of the parties is upheld by Georgian or German legislature.

The situation is different with alternative obligation. In this case, several performances are allowed, when each of them constitutes due performance of obligation. The obligor is given the option to choose among alternative actions from the very outset. Alternative obligation is regulated by Article 376 of the CCG, under which the selected obligation is regarded as an obligation to be performed from the very outset. Furthermore, all prescribed alternatives of the performance should be exhausted as the impossibility of performance of any of the actions does not constitute the right to leave the contract. This stipulation is further reinforced by Article 375 of the CCG, under which, if it turns out that the obligor can refuse one of two obligations, the obligation to perform the other action remains. It is important that the right to choose one from two potential actions is vested with the obligor as the provision for performance related risk, viz., performance costs, shipment/delivery of goods and deterioration of the quality of performance, falls within his/her terms of reference. However, it is worth mentioning that Georgian legislature stipulates that this option exists unless something else stems from the contract itself, the law or essence of the obligation. Hence, the viewpoint of an average reasonable person remains pressing with regard to the choice of the action to be performed, which naturally aims at ensuring contractual equilibrium.

2.2.4. Substantial Performance of Contract

Substantial performance of a contract does not exclude the legal regime of walking out of the contract and assignment of respective negative consequences to any of the parties. Hence, it is important to assess whether what criteria is employed for the determination of the substantiality of performance. In common law space, the question is resolved through the option of enforcement of specific statement of claim. Respectively, here an obligee is taken as an aggrieved party, who has the obliga-

[34] *Kropholler J*., German Civil Code, Study Comments, *Darjania T., Tchetchelashvili Z.* (trans.), *Chachanidze E., Darjania T., Totladze L.* (eds.), Tbilisi, 2014, 664 (in Georgian).

[35] Comp. Article 379 of the CCG: "An obligee is not obliged to accept the other performance other than the one, prescribed by contract. The same rule applies when performance is of great value."

tion to pay for a substantially performed part on the one hand and on the other the right to counter claim for compensation of damages incurred as a result of deficient performance. Determination of substantial performance is largely associated with economic category. Specifically, in the case of deficient performance, the obligation is substantially performed unless the costs and expenses of making good the flaw(s)/deficiencies are disproportionally higher than contract price. This principle is embodied in Article 490.3 of the CCG, under which a seller is entitled to refuse the elimination of a defect as well as substitution of the object, if these actions involve disproportionately high expenses. It can be said that, in this case, the obligor is granted with certain contractual discretion at the stage of breach of obligation. This stipulation is directly linked with the economic analysis of consequences of the breach of an obligation. In fact, the above article declares the principle of efficient breach, known to economic analysis, under which principle an obligor may prefer not to perform the obligation and not to compensate damages incurred to the counterparty through non-performance.[36]

In common law, the concept of substantial performance is mainly applied with regard to contract for work. In common law space, since early 1920s,'performance against consideration' was the name of the case, when a defect/unfitness of a transferred property is determinable and of minor importance, because of which it is still possible to efficiently use transferred property. In this case, English courts regard contract as a contract enforceable on condition of payment of respective compensation. Substantial performance is established by the fact that buyer's expectation is satisfied to a substantial extent. Respectively, a buyer, as an average reasonable person, is free in his/her choice to accept deficient performance and respective compensation or walk out of the contract. It is worth mentioning that English courts do not extend this reasoning to a flaw in title.[37]

Within the framework of economic analysis, the main question is who is to be assigned the trivial risks of incompatibility of performance with the agreed one – to the promisor or the promisee. In this case, the following legal circumstances are of decisive importance: whether the obligation is dividable or not, or to what extent is the consideration related to the condition of due performance of obligation. In this context, an example of the balance of interests of the parties is Section 323 of the BGB, which concerns the performance not in conformity with the contract. Specifically, Section 323.5 differentiates between performance in part and non-performance in conformity with the contract. In each of these cases, the German legislature makes assessments from the standpoint of an average reasonable person because it allows the revocation of a contract only when the obligee has no interest in a part of performance or the breach of obligation is trivial. Both these preconditions are the bearers of the concept of substantial performance. It should as well be mentioned that delimitation between performance in part and deficient performance becomes particularly pressing for a long-term contract. It is also noteworthy that stipulation about trivial nature of a breach of contract shifts focus to the position of the obligor, when, upon assessment of the interest towards the remaining part of the contract, the obligee's position prevails. In any case, the concept of substantial performance conveys mainly the economic interests of the parties and aims at comparison of the costs borne by the obligor for due per-

[36] For details, see: *Macneil I. R.*, Efficient Breach of Contract: Circles in the Sky, Virginia Law Review, Vol. 68, № 5, 1982, 947.

[37] *Martin S., Randall L. A. E.,* Law of Contracts, NY, 1912, 612.

formance on the one hand and the costs to be borne by the obligee for obtaining the object of performance from an alternative source on the other hand. According to economic analysis, the reasonability of performance is assessed from the perspective of both parties with due consideration of performance related costs and expenses for a seller and value of performance for a buyer.[38] It should be mentioned that the above differentiation is stressed in parts 1 and 3 of Article 405 of the CCG and the preconditions of substantiality of the breach of obligation are not presented within the single system. Furthermore, in the case of deficient performance, the standard of obligor's behaviour is defined under the provisions regulating a sales contract. Therefore, in the case of in-part/deficient performance, the question of balancing the legitimate interests of the parties becomes particularly pressing. It is important for the respective legal regime to be adequately presented in general provisions of the law of obligation.

3. Economic Analysis of Impossibility of Performance/Frustration

Upon negotiation of contractual terms and conditions, the parties take account of circumstances that may affect the value of performance. In most cases, the parties agree on the risk of accidental damage/loss of a property or excusable cases when parties can be exempted from liability. When setting certain terms and conditions, the parties aim at offsetting contractual imbalance or informational asymmetry. Economic analysis is oriented on promoting search for optimal outcome for the parties. The chapter below aims at the analysis of the doctrine of impossibility of performance/frustration for securing the best economic interests. Also, it should be mentioned that the main subject of analysis is non-faulty impossibility of performance.

3.1. Doctrinal Thesis about the Impossibility of Performance

Common law system differentiated between subjective impossibility created by a party and impossibility occurring because of external factors/objective circumstances. In the first case, the breach of obligation is in play and impossibility to attain the purpose of the contract in the other. Culpability implies the actions of both the obligor and the obligee, if the latter is not cooperating with the obligor. Under common law doctrine on frustration, quite frequently a faulty action is negligent or inconsequential. Impossibility of performance may arise both before and after maturation of performance. Impossibility occurring before the maturation of performance is the case of potential breach of obligation. In German civil law,[39] impossibility of performance means the breach of obligation in any case; however, it differs from the other cases of the breach of obligation according to its consequences as this is the only case which exempts a party from the obligation to perform.

Some practical cases fall within the framework of the impossibility of performance. Hence legal regulations that were developed within the framework of common law about absolute impossibility of

[38] *Posner E. A.,* Economic Analysis of Contract Law After Three Decades: Success or Failure?, U Chicago Law And Economics, Olin Working Paper, № 146, 2002, 9.

[39] Comp. *Lowisch M.,* New Law of Obligations in Germany, Ritsumeikan Law Review, № 20, 2003, 17.

performance, impracticability of performance and frustration are conditioned by different cases and individuality, despite the necessity of a common theoretical frame. Specifically:

- Impossibility of performance means when performance is no longer physically possible;

- Frustration means that performance is physically possible, but the underlying purpose of the contract is no longer attainable; and

- Impracticability of performance means that performance is physically possible, underlying purpose is achievable, but the foregoing would entail a much higher cost and efforts than originally contemplated.[40]

It is distinctive of the doctrine of impossibility of performance/frustration that a negative event could occur because of objective and unforeseeable circumstances beyond the control of the parties without a fault of either of the parties. Respectively, this concept falls within the category of realisation of an objective risk-factor, independent from the behaviour of a person. Initially, in English judicial practice, cases of faultless impossibility were discussed in the field of marine shipments.[41] Later, this doctrine covered cases when performance was to be carried out by a specific person and he/she died,[42] when changes of normative framework left the obligation, subject to performance, beyond the control of the party,[43] the cases of non-occurrence of circumstance(s) underlying contract, etc. Furthermore, in the latter case, breach of legitimate contractual expectation should concern both parties.[44] Hence, common-law doctrine united cases of objective nature.

Maintenance of equilibrium in force-majeure circumstances is one of the key issues for a legal system. Initially, it was believed that[45] normal flow of circumstances underlying a contract should have been taken into account to maintain initial intention of the parties. The foregoing would become particularly important upon assessment of commercial/practical impossibility. By 1960s, common law gave preference to the theory of radical change[46] of obligations subject to performance. Specifically, it is excluded to demand such performance which cannot be claimed from a party based on initial terms and conditions of the contract. However, the main criterion of assessment is the change of the content of the obligation and not its complexity or related high costs.[47] It is worth mentioning that the doctrine of impossibility of performance does not cover dramatic change of performance costs and expenses (change of market price), as it is believed that this does not impair the purpose of the contract. The opinion regarding the rule of performance is similar. Respectively, the above negative events fall within the scope of the obligor's risk.

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40 *Posner R. A., Rosenfield A. M.,* Impossibility and Related Doctrines in Contract Law: An Economic Analysis, The Journal of Legal Studies, Vol. 6, № 1, 1977, 84.

41 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 530.

42 See CCG, Article 453, part 1.

43 *Anson W. R., Corbin A., Arthur L.,* Principles of the Law of Contract with a Chapter on the Law of Agency, NY, 1924, 530.

44 Worth mentioning is a parallel with Articles 73 (c) and 360 of the CCG, as mutual mistake in transaction related circumstances, which is regarded as potential impossibility, constitutes grounds for voidance of the contract in German and Georgian codes.

45 Opinion about implied term – the so-called fiction of term.

46 Theory about the construction of a contract.

47 *Beatson J.,* Anson's Law of Contract, 28th ed. US, 2002, 544.

According to economic analysis, in the case of non-faulty impossibility of performance, the question arises as to which party is to assume the risk of occurrence of an event and respective consequences? Or, is the foregoing possible? In this case, the first property to verify is whether the contract itself regulates the consequences of negative occurrences. The discussion of the question of maintenance or termination of the contract should remain within the scope of common will of the parties. The question whether the situation should be unforeseeable or it can be foreseeable for the parties is a subject of discussion. According to economic analysis, a judge is required to focus mainly on the commercial activities of a party.[48]

Disputed cases are differentiated according to who is responsible for the risk of occurrence of a negative consequence. E.g., if performance becomes not cost-effective for an obligor, then should he/she bear the risk or is it possible for the latter to be exempted from the performance of assumed obligation? Exemption of an obligor from performance obligations means passing risk to the obligee, while refusal of exemption means assignment of this risk to the obligor. Performance is not cost-effective when expenses become so high because of unforeseen and unregulated cases that exceeded potential gain from the contract. A promisor/obligor should be exempted from the obligation when the addressee of the promise is the best bearer of the risk. In economic analysis, there are two main criteria for the determination of the "best risk-bearer party": 1) a person is capable of preventing risk at relatively small cost (this option does not actually exist in the case of faultless impossibility); and 2) a person is the best one to compensate risk. However, a person may meet only the second criterion as it is the case with insurance companies.[49] As already mentioned, a promisor/obligor can be exempted from performance obligation only when the addressee of the promisee/obligee is in the better position to insure the negative consequences of an event as the latter is in the better position to assess the potentiality or scope of a risk.[50] However, in common law space, there is a presumption that a promisor/obligor is more capable of prevention or insurance of an event, which makes performance not cost-effective.[51] Exemption from performance obligation is allowed only when counterparty is in a better position to foresee, assess and insure the risk, which again leads us to the concept of a reasonable observer.

As a general rule, a party is ready to pay high price for performance to get rid of the burden of risk, meaning that risk is a measurable category. Performance risk consists of the probability of its occurrence and its scope. It is necessary to know these features to define compensation in lieu of risk assumed by a party. Hence the simplest and most cost-effective means of risk allocation is claiming high contract price, the so-called risk insurance premium. According to economic analysis, there are two fundamental methods of minimisation of potential damage, viz., prevention and insurance. When it is possible to prevent damage at minimal cost one faces preventable risk. However, when this is not

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48 *Beatson J.,* Anson's Law of Contract, 28th ed. US, 2002, 546.

49 *Posner R. A., Rosenfield A. M.,* Impossibility and Related Doctrines in Contract Law: An Economic Analysis, The Journal of Legal Studies, Vol. 6, № 1, 1977, 90.

50 Ibid, 92.

51 Uniform Commercial Code, 1952, <https://www.law.cornell.edu/ucc>, [01.01.2018]. § 2.615 of the UCC focuses on the impracticability of performance and the non-occurrence of a contingency should be basic assumption for the parties upon execution of the contract. It should be stressed that only the seller is entitled to employ this legal remedy.

the case, the risk of suffering property loss and the necessity of reduction of costs, related to its occurrence, are in play. In this case, the simplest model of risk allocation is the correction of price in accordance with the amount of expenses to be borne to compensate potential loss.[52] In other words, the economically attainable purpose is securing the compensation of property loss that was suffered as a result of realisation of risk, which depends on who is the best bearer of the risk. In the case of economic impossibility, the main purpose of an adjudicator is to establish those contract terms and conditions the parties agreed upon to foresee the realised risk. Furthermore, it is believed that the parties are entitled to agree on the performance of impossible, what in fact means the agreement on the payment of compensation. As far as the impossibility to prevent damage is a precondition of application of the doctrine of impossibility of performance, demonstration of due care and due diligence is one of the qualifying circumstances in this case as well.

Section 275 of the BGB – exclusion of the duty of performance – regulates the concept of impossibility of performance. Here, the impossibility of performance is detailed according to types (objective-subjective, factual-legal and initial-further) both at legislative and doctrinal levels. The German code integrates the issues of exclusion from the duty of performance and refusal of performance by the obligor in this general paragraph. In the context of securing contractual equilibrium, the right of the obligor to refuse performance is of particular importance. The foregoing is equalised to the case of practical impossibility when performance becomes disproportionately complicated (unreal impossibility).[53] Precondition for the application of the right to refuse performance (practical impossibility) is the necessity of grossly disproportionate expenses or unreasonable efforts on the part of the obligor. One of the measurements of the disproportionality of costs and expenses/efforts is an obligee's interest in the performance of the obligation. Furthermore, a reference is made to the content of the law-of-obligations relation and good faith principle. Even in the case of impossibility for the obligor to render performance in person, part 3 of the above section provides whether the obligor should be obliged to perform the obligation, taking account of mutual weighing of the obstacle to the performance and the interests of the obligee. It is stressed in BGB commentary[54] that temporary impossibility can be taken as a permanent one when an obligee cannot be obliged to remain contractually bound until the removal

[52] A very good example of the practice of transformation of risk into value is the activities of insurance companies. The example of delay of marine shipment due to the deterioration of weather conditions well demonstrates the problem of allocation of risk in the case of faultless delay. Specifically, the cargo shipment contractual relationships are aware of the so-called delay fee. The bearer of risk for unloading a train-car due to the deterioration of weather conditions can be the sender in one case and the recipient in the other. The foregoing is established according to who is the payer of delay fee and on what condition. If it is agreed that the fee is paid by the recipient and the latter is exempted from fee due to the deterioration of weather conditions, it turns out that the bearer of the respective risk (the case of faultless delay/temporary impossibility) is the sender of the train; and if it is agreed that there is no excusable reason for the delay and the sender received certain amount for unloading the train-can as scheduled or earlier, it turns out that in this case the bearer of the risk is the recipient and the amount received by the latter for unloading train on time is a kind of compensation for that. Consequently, essential is which of the parties is the bearer of the risk. For details see: *Posner R. A.,* Economic Analysis of Law, 7th ed., US, 2007, 105.

[53] *Kropholler J*., German Civil Code, Study Comments, *Darjania T., Tchetchelashvili Z.* (trans.), *Chachanidze E., Darjania T., Totladze L.* (eds.), Tbilisi, 2014, 150 (in Georgian).

[54] Ibid.

of the obstacle. To sum up, it can be said that the basic principle is to guarantee the proportionality between costs and expenses to be borne by the obligor on the one hand and obligee's interest in performance on the other.[55] It should be mentioned that in this case the contractual price of performance remains unregulated, which is one of the leading criteria for economic analysis. In this respect, worth mentioning is the fact that BGB regulates the case of change of the basis of a contract (changed circumstances) by the separate Section 313, which implies economic impossibility when the legitimate interest of the obligor predominates.

The interpretation made in Georgian legal literature[56] focuses on objective absolute impossibility caused by unforeseen circumstances, the so-called force-majeure circumstances. It turns out that obstruction/complication of performance, i.e., economic impossibility falls within the scope of the concept of changed circumstances and contract adjustment,[57] unlike the above-discussed common-law doctrine, which *inter alia* also covers the cases of practical impossibility. In the CCG, Article 401 is the only one mentioning the impossibility of performance as such. Specifically, the case of non-faulty delay, discussed therein, is qualified as impossibility of performance. The main criterion for exemption of an obligor from the performance of obligation is the absence of his/her fault and less importance is accorded to allocation of risk between the parties in the case of contingencies. It should as well be mentioned that with such scarce regulation, provision for contractual equity is an ambiguous issue when the impossibility of performance is disputed, except for the cases when disputed circumstances will be placed within the framework of the institute of complication of performance and resulting from the foregoing adjustment of a contact.

3.2. Accidental Loss/Damage of an Object of Contract

The risk of accidental loss/damage of a property is particularly topical in the context of impossibility of performance. In common-law space, this case is known as destruction of goods. Furthermore, for such qualification, the object of a contract should be a special property with an individual feature, which was destructed without seller's fault and before the moment of transfer of the relevant risk to the buyer. In this case, setoff of contractual obligations is the single-option legal consequence.[58] Under the Unified Commercial Code (UCC),[59] in sales-shipment contracts, the risk of accidental loss of goods is borne by the seller until the transfer of goods to the carrier. In sales-delivery (delivery to the place of destination) contract, it is again borne by the seller, but this time until the delivery of goods to the place of destination. Hence, as a general rule, the best bearer of the risk is the seller as it is believed that the bearer of the risk is the one who ensures carriage/conveyance of goods.[60]

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55 Comp. CCG, Article 490, part 3: "A seller may refuse to eliminate the defect or to replace the property if either action would require disproportionately high expenses."

56 *Chanturia L., Zoidze B.,* Commentary of the Civil Code, Third Book, Tbilisi, 2001, 371 (in Georgian).

57 CCG, Article 398.

58 Sale of Goods Act, 06/12/1979, <https://www.legislation.gov.uk/ukpga/1979/54>, [01.01.2018].
See § 2.509., Short Uniform Commercial Code, 1952, <http://www.casefilemethod.com/statutes/-short%20ucc.pdf>, [01.01.2018].

60 *Posner R. A., Rosenfield A. M.,* Impossibility and Related Doctrines in Contract Law: An Economic Analysis, The Journal of Legal Studies, Vol. 6, № 1, 1977, 108.

In the case of damage or partial destruction of an object of contract, the key principle of the doctrine of impossibility of performance about exemption of a buyer from the duty of performance remains valid, provided that the buyer, if that is his/her will, is entitled to accept the undamaged/remaining part of goods.[61] Furthermore, the scope of the duty of the latter to pay for goods will depend on the divisibility of the object of performance. The foregoing can be determined through the establishment of the intention of the parties. Specifically, it should be determined whether the partially performed share is separable and whether it is possible to accept partial performance. In any case, this option is a certain privilege of the buyer. This privilege can be proved by the fact that the destruction of goods, including partial destruction, sets off seller's any right to claim against the buyer. Despite the foregoing, in practice, it is difficult to explain the degree of damage of goods for full exemption of the buyer from the duty of performance. Widely explained, even when goods cease to exist only from a commercial point of view, when it is not of agreed quality, this is equated to physical destruction from legal viewpoint.[62] Furthermore, this negative event should occur before the transfer of title to the buyer.

The question of refund of advance payment made by the buyer prior to destruction/damage of goods is an important issue for common-law judicial practice.[63] Initially, it was presumed that the set-off of a mature obligation was not possible, and parties could have been exempted only from future obligation. Therefore, the risk of a negative occurrence was vested with the party who first performed the obligation. However, later it was clarified that the amount paid by the buyer in advance was subject to refund in any case and the foregoing was to be done through filing a claim for restitution. However, a precondition for restitution was non-performance of an obligation to the full extent, which left the cases unregulated when the buyer had borne expenses for the purposes of performance or came into possession of a property that was useless for him/her or/and the buyer received remaining/undamaged share of performance.[64] Hence, the UK Frustrated Contract Act 1943[65] introduced the principle of inadmissibility of unjust enrichment. The foregoing becomes particularly pressing when the action carried out before frustration of a contract gives certain benefit to a party. Specifically, a

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61 Comp., Uniform Sales Act, 01/01/1906, <http://source.gosupra.com/docs/statute/221>, [01.01.2018]. Worth mentioning are Sections 7 and 8 of the USA, under which sections, if at the moment of execution of a contract or after the execution thereof the object of sale does not exist or has perished without the knowledge of the seller, the contract is void. If goods have perished in part or have wholly or in a material part so deteriorated in quality as to be substantially changed in character, the voidance of the contract is the choice of the buyer, falling within the scope of the freedom of will. In other words, the buyer is entitled to regard contract as void or accept undamaged part of goods as performance and maintain law-of-obligation relations with the seller pro rata to carry out performance. The above sections contain direct reference to the moment of transfer of risk, which should stem from the contract or/and its interpretation. The foregoing again makes clear the importance of allocation of the risk of occurrence of a negative event for legal consequence. Furthermore, voidance of a contract due to non- existence of the object of fulfilment is a general legal consequence and the precondition of the foregoing can be either the impossibility of performance or mutual mistake in the basis of the transaction. See *Williston S.,* Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act, NY, 1909, 190.

62 Comp. *Francis B. T.,* Handbook of the Law of Sales, US, 1895, 196.

63 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 541.

64 Ibid, 534.

65 The Frustrated Contracts Act, 05/08/1943, <http://www.bclaws.ca/civix/document/id/complete/statreg/-96166_01>, [01.01.2018].

person liable for restitution, in his/her turn, is entitled to file a defence against compensation of expenses incurred. In this case, mature claims can be mutually set-off. The foregoing proves again that, in the case of impossibility of performance, one of the key goals is provision for the equilibrium of the interests of the parties.[66]

Under Section 446 of the BGB – Passing of Risk and Charges – passing of the risk of accidental destruction and accidental deterioration is associated with the delivery of the goods sold. In other words, this is called performance hazard/risk. Transfer means handing over a property into the direct possession of a buyer and does not imply granting indirect possession. Furthermore, if an obligor can refuse performance by reason of impossibility of performance pursuant to Section 275, then under part 1 of Section 326, he/she is not entitled to claim consideration from the obligee. This means that the obligor bears the risk for a negative occurrence during performance. Furthermore, both in common-law and German civil law, impossibility of performance (frustration) is established with regard to an individually defined property and the seller is required to accomplish performance through any means if the property is a generic one. Passing of the risk of performance is quite topical in the case of conditional sale when there is a certain period between delivery of goods and full payment of the value.[67] Also, separate regulation of the question of passing the risk of shipment of goods should be accounted for time factor necessary for the delivery. Specifically, in the case of sending goods to some other place on the request of the buyer, the risk passes to the buyer from an earlier moment, i.e., from the moment of handing over the goods to a dealer by the seller. Hence, when there is no agreement on sending goods to the other place, the risk passes to the buyer only from the moment of transfer of the goods under the direct ownership thereof. Furthermore, reference to sending the goods to the other place is an exemption and supply/delivery of the goods should be subject to the common rule of passing risk at the place of performance. Also worth mentioning is the fact that, according to common opinion, a carrier will not be considered as a person assisting performance, even if the sales object is carried by a seller's employee and the object is accidentally destroyed at that moment. Even if the carrier is at fault, the seller will not be liable for the action committed by the former, as a person assisting the performance. There is an obligation to send, which means that the seller is excluded from liability from the moment of handing the property over to the carrier.[68] For the purposes of passing on the performance risk, the situation where the buyer is late with acceptance is equalised to the transfer of the goods. Articles regulating sales contracts and work contracts in the CCG contain stipulations that are similar to those of the German code.[69] In this light, Article 402 of the CCG which provides for an obligor's liability for the consequences of overdue performance is worth mentioning. Specifically, in the case of overdue performance, the obligor is responsible for any negative consequence, including for damage resulting from impossibility of performance due to delay/accidental damage. Under Article 401 of the same code, strict liability of the obligor is linked with faulty action of the latter as non-faulty non-performance of an obligation within agreed timeline is not qualified as an overdue performance of the obligor. Therefore, the risk of occurrence of every negative consequence of delay is vest-

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66 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 558.

67 *Kropholler J*., German Civil Code, Study Comments, *Darjania T., Tchetchelashvili Z.* (trans.), *Chachanidze E., Darjania T., Totladze L.* (eds.), Tbilisi, 2014, 341 (in Georgian).

68 Ibid, 343.

69 See Articles 482 and 651 of the CCG.

ed with the obligor, except for the case when the latter successfully proves that there is no causal link between inflicted damage and overdue performance. The foregoing stems from Article 394.1 of the CCG, as in the above case the legislature focuses on the necessity of conditioning the consequences of overdue performance by overdue performance.

4. Complexity of Interpretation of a Contract through Dispositional Norms

Division of legal norms into dispositional and imperative ones is inherent both for European and case-law systems. Imperative norms, which mainly aim at ensuring contractual equilibrium, are also the norms that limit freedom to contract. However, the scrutiny of application of dispositional norms is a particular focus of economic analysis. The main criterion for the selection of these norms is said to be the will the parties should presumably have upon the execution of a contract. These norms are regarded as a variety of certain standard terms and conditions. However, the question of how stable the determination of potential common will of the parties in each case from conceptual point of view is still pressing. Drafting of a contract and its enforcement are key stages in contract law. It is practically impossible to fully predict potential challenges and provide for countervailing measures.

4.1. Economic Analysis of Contract Interpretation

A question arises within the framework of the economic analysis as to which regulation would have been preferred by the majority of negotiating parties in the case concerned. There is a discretionary rule that contains a sanction in common law, which does not imply the proposed model of behaviour. An example of the foregoing is the legal solution of the UCC,[70] under which solution a contract is not enforceable unless the parties had agreed upon the number of the object of performance. Hence, no option of correction/ interpretation of defect is envisaged. As it turns out, the case concerns the term of a contract which is decisive for the existence thereof. In this context, a parallel should be made with Article 53 of the CCG, under which a transaction does not exist when its content cannot be ascertained from its form of expression or from other circumstances. Part 3 of Article 477 of the CCG may also provide for the consequence related to non-determination of the number of the object of performance, but this provision mentions only the price. This approach is justified by a stipulation that it is difficult and expensive for the court to determine the reasonable number of the object of performance. Hence, minimal determinability of a contract appears to be the precondition for its existence.

When a term or condition is not determined *ex ante*, the contract is to be amended with due consideration of legal status existing before its execution, which excludes mala-fide behaviour. As far as the cost of *ex ante* anticipation and evaluation of potential occurrences/circumstances during the lifetime of a contract are disproportionally high, it naturally becomes necessary to interpret the contract later. Thus, the thesis – agreeing to disagree – is admissible.[71] According to economic analysis, the

[70] See UCC § 2.201.

[71] *Posner R. A.,* The Law and Economics of Contract Interpretation, The Chicago Working Paper Series, Vol. 83:1581, 2004, 5.

preconditions of interpretation of a contract are as follows: risk-neutrality of the parties, symmetrical information, contractibility of all variables and absence of additional costs and expenses. It is necessary to determine the will of the parties, viz., when did they provide for specific terms and what broad norms were left and where. Therefore, the interpretation becomes necessary not only for filling gaps, but also because the parties consider it possible from the very outset, leaving room for interpretation.[72]

There are four main methods of interpretation in common-law space,[73] viz., the "four corner" rule, mutual mistake rule, *contra proferentem* rule and extrinsic non evidence rule.[74] Economists offered several interpretive strategies to the courts. The first strategy is majoritarian default – the meaning that most parties to contracts would use should be considered, which will often be the same as the customary meaning or trade usage. The second strategy is penalty default (less priority interpretation) – the meaning/interpretation should be found, which most parties to a contract would not use. This strategy provides for two incentives, viz., the parties try to make their contract terms less ambiguous and the parties cooperate in a most open manner and disclose all the available information. The foregoing comes close to word-for-word or literal interpretation. The third strategy is to determine which term would be efficient in a specific case for the parties despite the possible position of the majority of the parties. In this case, the expectations of specific parties are subject to assessment. The court interprets a circumstance/situation for a specific case and not for the majority of similar contracts. It should be said that it is difficult to determine attributes that speak for the efficiency of the above strategies and rationality of the consequence.[75]

When parties are reasonable and fully informed, they purposively draft contract terms and conditions to foresee every potential consequence. In economy, this situation is called equilibrium, when neither of the parties is interested in avoiding the agreement of contract terms and conditions and improve own position at the expense of the other. Furthermore, the cost of detailed drafting of a contract may exceed the expected gain, which should as well be taken into account. Non-regulation of an issue *ex ante ex post* results in a dissonance between the parties with regard to agreed rights and obligations. Here the question arises as to what contingent rights should be conferred and what contingent obligations should be imposed on the parties. The traditional answer is as follows: *ex post* a party may be imposed with only those rights and obligation, he/she would have reasonably agreed to *ex ante* had he/she predicted the potential situation. This is called the rule of "hypothetical contract theory"; this is the contract the parties would have agreed upon *ex ante*, if the cost of agreement had not made such a specification irrational.[76] According to hypothetical contracting or consent theory, the parties should be imposed with the same relevant obligations/liability as in the case of express consent as they allowed for the problem from the very outset. The problem is that contingent obligations are imposed on

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72 *Shavell S.,* On the Writing and the Interpretation of Contracts, The Journal of Law, Economics and Organization, Vol. 22, 2006, 290.

73 For details, see: *Posner R. A.,* The Law and Economics of Contract Interpretation, The Chicago Working Paper Series, Vol. 83:1581, 2004, 1.

74 *Smeenk B. P.,* Ambiguities and Extrinsic Evidence, Advocates' Quarterly, Vol. 12, 1990, 237.

75 *Posner E. A.,* Economic Analysis of Contract Law After Three Decades: Success or Failure?, U Chicago Law And Economics, Olin Working Paper, № 146, 2002, 14.

76 *Coleman J. L., Heckathorn D. D., Maser S. M.,* A Bargaining Theory Approach to Default Provisions and Disclosure Rules in Contract Law, Harvard Journal of Law and Public Policy, Vol. 12, № 3, 1989, 640.

the parties independently from them, after the execution of the contract. However, the economic arguments about utilisation and consensus speak for the necessity of efficiency of court decisions. Ultimately, the theory of hypothetic consent/contracting essentially reflects rational self-interest. It is believed in economic analysis that different stages of a contract require different levels of rationality and respectively the measures against ambiguity should also be different. The above strategies of contract interpretation evidence that the methodology oriented on practical consequence of interpretation of contract terms and conditions may override classical deliberations about the contradiction between the inner will of the declarer of the will and perception of the addressee of this declaration of will, when the inevitability of interaction between the declarations of will is commonly recognised.

Summing up, it can be said that according to the approach distinctive of the common-law legal system, only that contract can be interpreted which directly mentions or indirectly implies the option of interpretation of a term or condition. Otherwise, a contract does not exist or is unenforceable. Hence, the maxim of law is that only what can be defined is subject to interpretation.[77] It is worth mentioning that the thesis contained in Article 327.1 of the CCG about the necessity of agreement about essential terms and conditions coincides with the above maxim. Furthermore, all those criteria that are important for the interpretation of the declaration of will and developed in judicial practice – including the importance of the process of negotiation, existence and content of the usages of trade, general standard of reasonability, already implemented transactions, etc. – are reflected in separate provisions of the Georgian code.[78]

4.2. Scope of Interpretation of a Contract — Parol/Extrinsic Evidence Rule

Upon interpreting a contract/declaration of will, a question arises about the type and scope of the rights and obligations or contractual liability that may be granted and imposed upon a party by a court of law. The latter is to determine the rights and obligations the parties would have reasonably agreed upon had relevant negotiations been conducted. Hence, when the execution of a fully detailed contract is associated with unreasonably high expenses, this burden passes to the court, which interprets the agreement through dispositional norms and creates the so-called hypothetical contract. Because of the impossibility in predicting every cost or expense related to the process of execution of a contract or every risk-bearing situation, contracts are incomplete from the perspective of economic analysis and the parties allow for their completion/interpretation on the bases of business usages or judicial practice. According to economic analysis, a Pareto-Optimal contract[79] should be made a contract, to which the parties would agree upon had there been no contingent transaction costs.

Parol evidence rule, according to which a party was not entitled to use some oral stipulation, interpretation or testimony made during the pre-contractual phase for his/her own benefit and thus challenge the terms and conditions contained in final document, is important for the purposes of interpret-

[77] *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002, 60.

[78] See Articles 52, 337-340 of the CCG.

[79] Pareto-Optimal situation: a state of affairs in which no person in society can have his utility increased by redistribution of resources without making someone else worse off. See *Gordon D.,* An Introduction to Economic Reasoning, Alabama, 2000, 183.

ing a contract.[80] This rule was later applied to written evidences as well. Hence, focus was made on the initial character of the contract and its form, i.e., the later agreement prevails over the earlier one. Of course, the limitation cannot cover the agreements reached after the execution of the contract. In other words, the question of impact of earlier interpretations/agreements of the parties on final document drafted by them became the focus of common-law legal system. The above rule, in the case of its unconditional application, became a serious barrier for the court in the course of interpretation of final contracts.[81] Hence, it was presumed that a contract abandons earlier terms and conditions only when they are controversial, and the final contract directly provides for their invalidation. Hence, the application of this rule has no grounds until the contract is agreed with its detailed content. It comes to effect when a court identifies terms and conditions, subject to enforcement for the moment concerned. To sum up, it can be said that parol evidence rule should not be applied in the course of interpretation of a contract as in certain cases the precedent circumstances are particularly important. Furthermore, the purpose of interpretation is the clarification of the content of the contract and not its amendment or contradicting it. Parol evidence rule does not apply in proving an essential mistake, abuse of influence and also with regard to conditional contracts.[82] It is a separate matter for economic analysis as to who should allow such evidence – the court or the parties. Furthermore, the existence of the possibility to control parties in the process of interpretation of a contract is a separate issue. Specifically, considering mutual interests, it may be reasonable for the parties to define which contract term or condition should be left beyond interpretation. Furthermore, discussion of an evidence of pre-contractual period is an expensive process. Therefore, efficiency of scrutiny of this stage during judicial proceedings is subject to separate assessment. It may be functional for the parties to have certain control over the process of interpretation In this case as well in order to personally determine the reasonability of reviewing some evidence.[83]

5. A Third Person in the Course of Performance

One of the major factors providing for performance process is the involvement of a third person in the course of performance. The chapter below focuses on the assessment of actions carried out by a third person in the course of performance. We will examine the following questions: what is the risk inherent to the employment of a third person in the course of performance and what is the duty to duly select the latter is associated with? What are the legal consequences of negative occurrences, caused by a negligent action of a third person?

The common-law doctrines of contract privacy and consideration considerably restricted the option of participation of a third person outside contractual relationships. However, Contracts Act

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80 The word 'Parol' means 'spoken' (in English — Spoken, in French — Parler), *Corbin A.,* The Parol Evidence Rule, The Yale Law Journal, Vol. 53(4), 1944, 610.

81 Ibid.

82 Evidence, Outlines, 2016, 29-30, <http://www.lexisnexis.com/documents/pdf/20160617015319_large.pdf>, [01.01.2018].

83 *Shavell S.,* On the Writing and the Interpretation of Contracts, The Journal of Law, Economics and Organization, Vol. 22, 2006, 310.

(Rights of Third Parties[84]) 1999 allowed the foregoing in cases when a contract expressly provided or indirectly implied this option. Although the extension of contractual terms and conditions to a third person are still complicated in practice, such a solution may be provided by the contract itself as mentioned above.[85]

Particularly pressing is the question of participation of a third person in the case of transfer of a property. In this case, the obligor's risk is associated with the transfer of the object of performance by a third person as a negative consequence caused by the fault of the third person; this is a risk-factor associated with the actions of the obligor. The question of limitation or exclusion of the risk of contractual liability is subject to a separate discussion. Because, when providing for this stipulation, the obligor may extend it to a subject that is not a party to the contract but participates in the course of performance. It should be mentioned that when an assistant third person is not protected by such stipulation, he/she enjoys the right to certain recourse (right of contribution) against the obligor.[86]

At any stage of performance of obligation, upon some negative occurrence conditioned either by a negligent action of a third person or by an objective factor, the risk-bearing subject is the obligor. In the present case, the centre of attention is only that category of third persons who share the action to be performed with the obligor. Under Section 278 of the BGB, the actions of a person assisting a debtor in the performance of an obligation is regarded as the action of the latter; however, in fact this is the case of a debtor's liability for other person's action (vicarious liability). It should be mentioned that Section 831 of the same code separately mentions the case of a performer of the assignment, an agent, and bases an obligor's liability on insufficient prudence of the latter in selecting a performer of the obligation and thus on the faulty action of the obligor. In common law, the foregoing is embodied in the concept of *Respondeat Superior*,[87] and the principle of liability without fault, underlying this concept, is proved by economic analysis as well. Specifically, it is presumed that liability should be imposed on the person who is in the position to prevent an error or negative consequence at lesser cost.

An assistant in performance is a person who is involved in the performance at the obligor's discretion. Such a person, *inter alia*, may be the railway, postal service or a similar organisation. As already mentioned, in the case of any such involvement, the bearer of non-performance risk is the obligor himself. It should be mentioned that a producer does not fall within the scope of the notion of such a person and respective regulation. Furthermore, Section 278 of the BGB considers it admissible to agree about the exemption of the obligor from the liability for a wilful action of the person assisting him/her in the performance, in advance, what is excluded by Section 276.3 in the case of fault on the part of the obligor himself/herself. To compare, the similar Article 396 of the CCG, which does not provide for the option of prior agreement of the obligor's exemption from the liability in the case of wilful action of a third person should be mentioned here.

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84 Contracts (Rights of Third Parties) Act, 11/11/1999, <http://www.legislation.gov.uk/ukpga/1999/31/-pdfs/ukpga_19990031_en.pdf>, [01.01.2018].

85 *Beatson J.,* Anson's Law of Contract, 28th ed., US, 2002,182.

86 Ibid.

87 Respondeat Superior – Let the Master Answer. See *Thompson S. D.,* Respondeat Superior, 1879, 238, <http://heinonline.org>, [14.08.2018].

To demonstrate the difference, part 2 of Article 371 of the CCG can be mentioned, which, according to opinions expressed in Georgian legal literature,[88] should include the assisting third person involved in the performance. This part mainly regulates the performance of another person's obligation at the discretion of the third person. Whether it is possible for a third person to act independently from the will of the obligor is evidenced by the fact that the obligee is entitled not to accept performance offered by a third person if the obligor is against it. This wording gives rise to a question, viz., what is the motive of the obligee to accept performance and that of the third person, to perform an obligation against the will of the obligor. In the interpretation of Section 257 of the BGB,[89] such a person is denominated as a person hired to render some service, an agent, depositee and a partner doing business. These persons may be performing the so-called alien obligation at their own free will. In the case of absence of the component of will or making a mistake, an option of claiming the restitution of initial condition from the third person based on unjust enrichment provisions is provided.

The answer with regard to the motive of the action is relatively clear upon analysis of the case, envisaged by Article 374, when a third person is driven by a legitimate right/interest in a property, which is facing enforcement on the part of the obligee. There should be a property under the possession of the obligor, encumbered by a third person's right. The legal consequence of satisfaction of the obligee by a third person is also logical, as, according to subrogation rule, the obligee's claim against the obligor passes to the former, which cannot be said when analysing the case envisaged by Article 371. Exemption of the obligor from specific performance obligation may constitute the subject of legal relationship existing between the latter and the third person. To sum up, it can be said that in cases envisaged by Articles 371 and 372 of the CCG, the third person is the subject acting with specific legal interest and is not just a subject involved in the performance, who is used by the obligor for the performance of his/her obligation. Consequently, the principle of debtor's liability without fault, envisaged by Article 396 of the CCG, should not apply to these cases. This means that the third person should be the subject bearing the risk of negative occurrence in the course of performance, independently from the obligor.

6. Conclusion

The paper focused on the vision of current and concurrent processes of performance of obligation from the position of economic analysis, which allows for comparison with traditional legal visions. In conclusion, the following issues could be identified:

1. Economic analysis regards the behaviour of a subject, party to a contract, as the action of the maximiser of individual gain, whilst legal protection of wealth is common legitimate contractual expectation of the parties for traditional legal doctrines – both common-law and German ones;

2. Economic analysis delimits between discretional and relative contracts. In a relative contract all the values are variable and are evaluated on a case-by-case basis. Furthermore, unlike traditional

[88] *Chanturia L., Zoidze B.,* Commentary on the Civil Code of Georgia, Third Book, Tbilisi, 2001, 302 (in Georgian).

[89] *Kropholler J*., German Civil Code, Study Comments, *Darjania T., Tchetchelashvili Z.* (trans.), *Chachanidze E., Darjania T., Totladze L.* (eds.), Tbilisi, 2014, 142 (in Georgian).

vision, where a party is accorded ordinary risk inherent to his/her share of performance, economic analysis identifies circumstances, which changes the risk allocation standard in principle. These circumstances can be: time scheduling of performance, disproportionality, ambiguity or absence of consideration, change of customer's demand, complexity of production of goods, large cost of execution or renegotiation of a contract, identity and legal/economic status of the party, difficulty of contract administration and a party's attitude towards the risk;

3. Concept of an average reasonable person, which is topical for traditional legal doctrines and is the leading concept both for the legislature and judiciary for the identification of correct behaviour, acquires different practical connotation in economic analysis. Here, it is attempted to delimit the concept of average reasonable person from general duty of good-faith behaviour and to incorporate the element of economic rationality to a greater extent;

4. Economic analysis creates the concept of unilateral discretional contracting power of a party in civil-law relations, which is well demonstrated in the course of performance of an obligation. The source of this power is both initial terms and conditions of the contract and consequences of default. Furthermore, economic analysis allows for the existence of changing equilibrium between the interests of the parties, as according to elaborated opinion, contractual positions can exist only for a specific moment;

5. The concept of substantial performance is the manifestation of the judgements of economic analysis. E.g., in the case of faulty performance, the obligation is substantially performed if the cost of removals of the defect is not disproportionally higher than contractual price of performance. Hence, due performance of obligation is regarded as a situation which influences initial value of performance and exempts the obligor from performance obligation. This concept responds to well-known economic analysis principle of efficient breach, according to which principle an obligor should have the right not to perform an obligation and compensate damages incurred to the counterparty through non-performance;

6. In the case of impossibility of performance, a result of a risk-bearing event, it is important to maintain contractual equilibrium. Here the question arises as to who is to bear the risk of occurrence of the event and whether proprietary liability should be borne by either party. Impossibility of performance is one of the concepts associated with the allocation of risk. Exemption of a promisor/obligor from performance obligation means passing the risk to the addressee of the promise and refusal of exemption and allocation of this risk to the promisor/obligor. An economically attainable purpose is to secure the compensation of property loss caused by the realisation of risk, which depends on who is the best bearer of the risk. Furthermore, traditional common-law doctrine of impossibility of performance/frustration of purpose of the contract coincides with the purpose of economic efficiency of a contract, which is proved by economic analysis;

7. Within the framework of economic analysis, the preconditions of interpretation of a contract are as follows: risk-neutrality of the parties, symmetrical information, contractibility of all variables and absence of additional costs and expenses. When parties are reasonable and fully informed, they purposively draft contract terms and conditions to foresee every potential consequence. In economy this situation is called equilibrium. However, the cost of detailed drafting of a contract may exceed the expected gain, which generates a necessity for the parties to leave some gaps. It should be stressed that

classical theory of hypothetical consent/contracting essentially coincides with the idea of protection of rational idea, which is widely discussed in economic analysis;

8. Economic analysis gives autonomous importance to certain factors conditioning performance process. One such factor is the participation of a third person in the course of performance. The negative consequence caused by the fault of a third person, involved in performance, is a risk factor related to the actions of the obligor; and

9. When some negative occurrence is conditioned either by a negligent action of a third person or by an objective factor, the risk-bearer subject is the principal/obligor. In the first case, the action of an assistant/agent performing obligation is regarded as the action of the obligor himself/herself and in the second case, it is presumed that the third person cannot be liable for an objective obstacle to performance. According to economic analysis as well, liability may be imposed on the person who can prevent the mistake or negative consequence with relatively less expenses.

Based on the foregoing, it becomes apparent that, as of to date, complicated contract-law relations are viewed in different light according to different economic concepts and categories. This, in turn, promotes the determination of the efficiency and social importance of current concepts of law and identification of new solutions for the assessment at legislative and judicial levels.

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Spread of the Audiovisual Works in the Social Network and its Legal Consequences

This article discusses the typical cases of spreading audiovisual works and their legal consequences. The frameworks of spreading audiovisual works are an interesting topic in a contemporary reality. The issue concerning the certain cases of spreading the audiovisual works in the social network (uploading, sharing a link, expressing position with sharing) is mostly interesting. In this regard, the article discusses the legal backgrounds concerning the freedom and restriction of spreading the audiovisual works in the social network.

Key words: *Audiovisual Works, Social Network, Media, Group, Spread, Copyright, Copyright Law.*

1. Introduction

Audiovisual works are spread and used quite often in the contemporary period. The development of social network has increased the amount of the users who shares such works. The users are sharing certain video files and other works for several reasons. The aims of sharing differ from each other, according to the certain cases.

As the audiovisual works are widely spread, the danger of infringing copyright is also increasing. The legal solution of the problems existing in the social network is considered as one of the biggest challenges of the contemporary lawyers. Technological changes should be followed by the legal amendments, which do not always coincide with each other. Accordingly, the development of the court practice is important in this regard, while the practice is able to overcome this challenge more quickly and efficiently.

Together with preventing the infringement of copyright it is also important to maintain the balance between the interests of the copyright holders, on one side, and the users, on the other, which is also another important challenge of contemporary copyright law. In this regard, it is one of the aims of the development of legislation and court practice to reach this balance between the different interests.

Within the framework of this research, the examples are taken from the activities mostly performed in the social network, particularly – *Facebook*, also considering their legal consequences. We discuss the issue of freedom of the actions performed in this social network and the necessity of the higher level of the legal protection (considering the increased activities of the users).

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2. Audiovisual Work as the Object Protected by the Law

Considering audiovisual works among the list of the objects protected by copyright, which initially considered only the "classical" sorts of scientific, literary and artistic works, is the result of the technological progress. The development of internet and social network in the recent decades, which also follows the technological development, creates modern platform of spreading the audiovisual works. Accordingly, legal protection of the audiovisual works spread in the social network is characterized by a number of specificities, derived from its notion.

2.1. Notion of the Audiovisual Work

The unified definition of audiovisual work has not been created yet, neither on the international (i.e. Berne Convention for the Protection of Literary and Artistic Works, 09/09/1886 (hereafter – Berne Convention)) nor on the regional (i.e. EC directives) level. Accordingly, overview of the copyright legislations of certain coun tries is necessary in order to identify the main elements of the notion of audiovisual works.

2.1.1. Legal Regulation of the Audiovisual Works in the International Legal Acts

The unified definition of audiovisual work is not provided in the international legal acts.[1] Berne Convention refers to "cinematographic works to which are assimilated works expressed by a process analogous to cinematography",[2] but not to the audiovisual works. Accordingly, Berne Convention does not refer to the audiovisual works into more details, nor does it specify the "process analogous to cinematography", while such specification would have been useless because of the increased tempo of developing technologies and cinema industry, so the wider and more 'flexible' definition has been selected on purpose.[3] The definition of audiovisual works is not provided in the EC directives regulating the certain issues related to copyright.[4]

2.1.2. Definition of the Audiovisual Work According to the Copyright Laws of the Certain Countries

As the unified definition of the audiovisual work does not exist, this term is defined in various manners in the national copyright legislations. For example, German Copyright Act uses the term

1 Such as: Berne Convention for the Protection of Literary and Artistic Works, 09/09/1886; World Intellectual Property Organization (WIPO) Copyright Treaty, 06/03/2002; Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), 15/04/1994.

2 Article 2(1), Berne Convention for the Protection of Literary and Artistic Works, 09/09/1886.

3 *Stamatoudi I.,* Audiovisual works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 106.

4 I.e. Rental and Lending Rights Directive defines "film" as the audiovisual work (Article 2.1.(c)), but the definition of "audiovisual work" is provided neither in this, nor in other EU directives; see Art. 2.1.(c), Directive 2006/115/EC of the European Parliament and of the Council, 12/12/2006.

"moving pictures" instead of "audiovisual work"[5]. Code of the Intellectual Property of France defines the audiovisual work in the following manner: "the works containing the sequence of moving pictures, with or without voice".[6] More detailed definition is provided in the US Copyright Act, according to which the audiovisual works "are works that consist of a series of related images which are intrinsically intended to be shown by the use of machines, or devices such as projectors, viewers, or electronic equipment, together with accompanying sounds, if any, regardless of the nature of the material objects, such as films or tapes, in which the works are embodied".[7] Accordingly, the definitions provided in the French and US copyright legislations can be considered as the examples of the brief and detailed definitions.

2.1.3. Definition of the Audiovisual Work According to Georgian Legislation

Audiovisual work is defined in the following manner according to the Georgian law on Copyright and Neighboring Rights: "a work consisting of a series of images wheather or not accompanied by sound that imparts the impression of motion and can be seen and/or heard."[8] As we can see, Georgian legislation reflects the established standard according to which the element of "motioned sequential pictures" is necessary, but the existence of voice is not. According to the law, "Audiovisual work includes cinematographic and other works expressed by means analogous to cinematography (tele-, video films, film strips, etc.)".[9] Similarly to the copyright legislation of the United States, the material form of expression of the work is not decisive in the Georgian copyright legislation as well.

2.2. Specificities of the Audiovisual Work and its Legal Regulation

Although the definitions provided in the copyright legislations of the various countries are not homogeneous, there are certain basic elements which unify the definitions mentioned above. These definitions cause the specific character of the audiovisual work and, accordingly, specificity of its legal regulation.

2.2.1. Basic Elements of the Notion of Audiovisual Work

Because of the non-existence of the unified notion defining audiovisual work, copyright legislations of the numerous countries define this term in various manners – some of them use alternative names,[10] some do not define them at all[11]. Some of the definitions are broad and detailed,

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5 § 95, Gesetz über Urheberrecht und verwandte Schutzrechte, 09/09/1965.
6 Article L112-2,6°, Code de la Propriété Intellectuelle, № 92-597, 01/07/1992.
7 § 101, US Copyright Act, № 94-553, 19/10/1976.
8 Article 4, part "b", Law of Georgia on Copyright and Related Rights, 22/06/1999.
9 Ibid.
10 I.e. "moving pictures" in § 95, Gesetz über Urheberrecht und verwandte Schutzrechte, 09/09/1965.

others are brief and laconic[12]. In spite of all the differences, there is an element common for every definition and this is "moving sequential pictures". The term 'audiovisual' semantically implies the existence of picture and voice as well. However, according to the definitions discussed above, picture is an essential element of the audiovisual work, while the voice is not, the existence of which is not necessary. The term "picture" should be used in its broader sense in this regard: it refers to the pictures of not only the 'real' things, but also all of the other pictures which can be projected and viewed by means of screen and projector.[13] The pictures have to be more than one at the same time,[14] they have to be motioned and sequential. 'Sequential' character in this regard refers not to the random gathering of the pictures but also the logically connected unity, within the context of which the pictures are perceived as the parts of the unified scenario.[15]

2.2.2. Legal Regulation of the Audiovisual Work

The specific character of the audiovisual work, which differentiates it from the other types of literary and artistic works, is the reason of the specificity of its legal regulation. The common principle of the copyright law – requirement of originality – refers also to the audiovisual work: the work has to be the result of the intellectual-creative activity.[16] The Copyright, Designs and Patents Act 1988 of the UK directly states that the film, or its part, which is a copy of another film, is not subjected to the copyright protection.[17]

An essential element causing the specific character of the audiovisual work is the issue of its authorship. As a rule, several persons are participating in the creation of the audiovisual work.[18] The common law and continental European rules have to be differentiated in terms of regulating authorship in this regard: according to the Copyright, Designs and Patents Act 1988 of the UK, producer is considered as an author of the film;[19] in continental Europe, however, the rights of the producer of the film are rather restricted[20]. Georgian legislation mostly shares the continental European regime,[21] it

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11 *Stamatoudi I.,* Audiovisual Works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 104.

12 Georgian legislation is intermediate in this regard: the definition provided by the Georgian law consists of the basic elements of the audiovisual work and name the forms of their expression at the same time, see: Article 4, part "b", Law of Georgia on Copyright and Related Rights, 22/06/1999.

13 *Stamatoudi I.,* Audiovisual Works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 111.

14 In the illustrated definitions the word "picture" is always in plural.

15 *Stamatoudi I.,* Audiovisual Works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 113.

16 Article 5, part 1, Law of Georgia on Copyright and Related Rights, 22/06/1999.

17 Section 5B(4), Copyright, Designs and Patents Act, 15/11/1988.

18 *Stamatoudi I.,* Audiovisual Works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 120.

19 Sec. 9(2)(ab), Copyright, Designs and Patents Act, 15/11/1988.

20 *Stamatoudi I.,* Audiovisual Works, in: Copyright and Multimedia Products: A Comparative Analysis, *Stamatoudi I.* (ed.), Cambridge, 2001, 120.

21 However, according to the decision made by the shareholders' meeting of Joint Stock Company "Georgian Film" and the general partners 2 years before the adoption of the Law of Georgia on Copyright and Related

regulates the issue of authorship of the audiovisual work and considers the producer, as well as author of the plot, author of the dialogues and author of musical works, with or without texts, created especially for this audiovisual work, as the authors (co-authors).[22] Generally, the multitude of authors and, accordingly, the special rule of regulating copyright is the specificity which differentiates audiovisual work from the other sorts of copyrighted works.

2. 3. Audiovisual Media Service and its Regulation According to the EU Law

The issue of spreading the audiovisual work in the media has initially been connected to the technological development and, due to the increasing character of the latter, the necessity of legal regulation of this issue has been created. With this purpose the Audiovisual Media Services Directive has been adopted by the EU in 2007.[23] It has to be mentioned that the initial purpose if the European Commission had been full liberalization of the spread of such product, but such approach was strongly opposed by the member states and, finally, more balanced and compromise version has been adopted.[24] The directive defines the definition of "audiovisual media service"[25] and regulates it into details. In this case 'media' refers to the traditional TV broadcast as well as to the internet media, which was a novelty by that time. The increasing development of the latter after the year 2010 brought new challenge for the European Commission and made the amendment of the directive inevitable. Nowadays the negotiations between the European Parliament, Council and Commission concerning the new text of the directive are officially completed, which will make the legislation more flexible and guarantee its responsiveness to the modern challenges.[26] Generally, the history of adopting and amending the Audiovisual Media Services Directive by the European Union[27] highlights once again the dynamic character of the audiovisual work and its spread in the social media.

3. Freedom of the Spread of Audiovisual Works in the Social Network

Audiovisual works can be spread in the form of video clip as well as in spontaneous created form.[28] The first case refers to the certain video clip and to music, which can be taken from another

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Rights (minutes of shareholders' meeting № 4, 10/11/1997), the rights of ownership of the films produced before the year 1990 have been granted to the producers of the films, which is in compliance with the "common law" model.

22 Article 15, part 1, Law of Georgia on Copyright and Related Rights, 22/06/1999.

23 Directive 2007/65/EC of the European Parliament and of the Council, 11/12/07.

24 *Bushati E.,* "Product Placement": The Harmonization of the New Albanian Media Law with the European Audio-Visual Media Services Directive, Academicus, 2011, Issue 4, 62.

25 Art. 1.1.(a), Directive 2010/13/EU of the European Parliament and of the Council, 10/03/2010.

26 European Commission – Press Release, Audiovisual Media Services: Breakthrough in EU Negotiations for Modern and Fairer Rules, Brussels, 2018, <http://europa.eu/rapid/press-release_IP-18-3567_en.htm>, [26.03.2019].

27 The directive has been adopted in 2007 and amended in 2010 at first, nowadays its second amendment has been prepared.

28 *Vormbrock* U., Gesamtes Medienrecht, Hamburger Kommentar, 3 Aufl., *Paschke M., Berlit W., Meyer B.* (hrgb.), Baden-Baden, 2016, Rn. 55. Abschnitt, Teil 6, Kapitel 1, 23.

web site (such as *YouTube*), or spread by a certain person. Copyright protection also covers the work created spontaneously (such as on *Instagram*). Such possibility is provided by the technical characteristics of the social network. Although such works belong to the area of copyright protection, its protection is still connected to certain difficulties.[29] In terms of copyright protection it should be equaled to the work uploaded by the certain person.

3.1. Spread of the Work in a Form of Posting a Link on the Timeline

The most frequent form of spreading audiovisual works by the user of the social network on his/her own timeline is sharing a link. However, in practical terms it is more common case when a person shares *YouTube* link on his/her own timeline. It is a matter of discussion, whether such case might be referred as an infringement. However, it can be safely said that the right is protected only in the case when the author of the work expresses his/her consent.[30]

3.2. Spread of the Work by Means of Uploading

In terms of protecting copyright, upload in the social network has the same content as sharing.[31] In such cases a consent from the entitled person is an essential precondition. Unlikely to spread of the link, in this case the uploader has to refer to the appropriate initial source, if such notification is necessary.

3.3. Position Expressed by Means of Posting

It occurs quite often that, together with spreading the work, personal comments/opinions are also posted together with the work. It can be expressed in positive as well as negative opinion, when the user announces his/her position to the definite or indefinite circle of the persons. In this regard it is important to differentiate the results caused by the spread from each other: the issues of infringing copyright, personal rights and, accordingly, imposition of responsibility.

3.3.1. Approval Expressed by Posting

Approval, positive comment, consent, or any other action which can be perceived as 'positive spread', is directed to the certain circle of the natural persons. It is possible that a person does not spread certain work for this reason, but it is not important in terms of legal consequences. For example, a *Facebook* user is spreading an opus of a famous musician (*Michael Jackson*, *Freddie Mercury*, *John Coltrane*, etc.) and indicates in the comment that this opus encourages people and creates good mood.

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[29] *Vormbrock* U., Gesamtes Medienrecht, Hamburger Kommentar, 3 Aufl., *Paschke M., Berlit W., Meyer B.* (hrgb.), Baden-Baden, 2016, Rn. 55. Abschnitt, Teil 6, Kapitel 1, 23.

[30] Even if the source is protected, it is also possible in certain cases to create a problem.

[31] *Katko P., Kaiser D.,* Immaterialgutrechte (kapitel 4), in: Praxishandbuch Rechtsfragen Social Media, *Splittgerber A.* (hrgb.), Berlin, 2014, 193.

The aim can be 'positive' and, moreover, author of the work (or material copyright holder) might like the post, but it does not mean that the copyright is protected in the case of expressing certain emotion concerning the copyrighted work.

3.3.2. Negative Opinion Certified by Posting

Another occasion is the case when a person expresses his/her opinion by means of so-called 'negative posting'. Likely to the case discussed above, this person posts a comment together with spreading a musical opus, but in this comment it is stated that the work is very weak, there is no professionalism expressed in it, etc. Such comments usually refer to the beginners in music industry (whose names are not known to the public), or to the opuses which have negative reputation in the audience. In such cases it is also possible to infringe the immaterial rights of person, together with copyright.

3.3.3. Difference between Copyright and other Immaterial Personal Rights

Negative or positive opinion of the user about the opus spread by him/her does not play a decisive role in terms of copyright. With regard to comments, it is possible to claim for defamation or degrading reputation,[32] but even if such claim is satisfied by the court, it does not have any influence on the copyright protection.

In this case the following circumstance is important: if, together with the infringement of copyright (spread of the work without consent), the personal immaterial right of a person such as business reputation is also violated (opinion concerning the posted work is infringing), would then the author be able to raise both of the claims at the court?

Legislative regulation gives a possibility to have positive response to this question. More precisely, the issue concerns not with two different responsibilities for one single action, but to infringing two different rights with one action,[33] since both of these rights are recognized and guaranteed by the Constitution (Articles 23 and 17 of the Constitution of Georgia, 2018 version of the year 2018 before the presidential election), their protection should also be guaranteed by the law. Accordingly, such action can be considered as absolutely admissible.

3.3.4. Admissibility of the Different Position

As long as the internet is not considered as a personal space, it is possible that such kind of publicly stated position refer to the persons having different opinions. In this regard, the argument of the opponents should be based on the demarcation of the personal space. Imposition of certain additional

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[32] In this case it is important to find out, whether the case concerns with the freedom of expression, or other action, which is proportional to the infringement of the right.

[33] In certain cases it is possible to have an infringement of one more right. Namely, it refers to the identification of a person in the work. In this regard, audiovisual works are regulated by the same rule which regulates the appearance of a person in the photo (considering public space and all other preconditions), *Schirmbacher M.,* Online-Marketing- und Social-Media-Recht, 2. Aufl., Frechen, 2017, 203.

precondition is possible in this regard: is the user committing such action for friends, for public, or for personal use? Difference between the opinions can occur in this regard. Moreover, after spreading the information on the own timeline, the person should not have a logical expectation that his/her friend would hesitate to re-share this work and carefully check the area of initial spread. Accordingly, this issue can become an object of dispute, the resolution of which should be based on the existence of certain content and circumstances.

3.4. Interim Summary

Infringement of right (derived from the non-existence of license) in the case of sharing a link is possible in the same ways.[34] In this regard it is implied that a person makes a work publicly accessible.[35] Especially, when the spread (sharing) of the link is not connected to the commercial aims, the person needs to be careful in this regard.

In order to make it more clear, an allegorical example can be provided: a person detects certain item in the street (either luxurious or not, price is not important). The item does not contain the information about the aim of locating it in the street (there is no invitatio ad offerendum, or any similar content). If the person likes it and decides to consume it without asking anyone – in such case the infringement of the right can easily be identified. Moreover, because of the absolute nature of the property right, its creation requires certain preconditions (Article 190 Georgian Civil Code - Acquiring the ownership of ownerless movable things, Article 191 – Finding). Simultaneously we can discuss the possibility existing in the web space: there is a work in the internet; while 'wandering' in the web space, certain person finds this work, likes it and wishes to use it without asking. Also in this case, when there is no precondition accompanied to the work, there is no text concerning invitatio ad offerendum, etc. then such work is not aimed at wide consumption by the public.

One difference can be mentioned between these two cases: aim of personal use. If the use of the item found in the street is not allowed, the law allows such usage in case of the work. However, the essence of personal use is the matter of another discussion and we will discuss it below.

4. Possibility of Infringement of the Right – Sharing Modern Tendency

4.1. Sharing in certain Group and Aim of the User

Upload of the work in the certain group is possible to be considered as a personal use.[36] This is the difference between sharing to friends (on the so-called "timeline") publicly, where the sharing of information equals to publication.[37] In such case the type of the group is important, as well as the aim of sharing and the possible outcomes, which should be considered clearly by the user.

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34 EuGH, Urteil vom 08.09.2016 – C-160/15.

35 AG Leipzig, Urteil vom 21.12.2011 – 200 Ls 390 Js 184-11.

36 *Katko P., Kaiser D.,* Immaterialgutrechte (kapitel 4), in: Praxishandbuch Rechtsfragen Social Media, *Splittgerber A.* (hrgb.)*,* Berlin, 2014, 189.

37 Ibid.

4.1.1. Type of the Group

If we consider *Facebook* groups, sharing the work in the closed group can be considered as sharing for private use. Closed groups, as well as secret groups are used for communication.[38] Open group is a different case and sharing an information there is equaled to the public sharing, where the stated position does not contain any secret information, or a statement directed to the certain group of people.[39]

4.1.2. Inadmissibility of Discussing the Issue in Formal Approach

Closed (secret) groups can be considered within the framework of the exceptional case. It can depend on the type of the group or the number of members of this certain group.[40] For example, when 400 users are registered as the members of the closed group and the uploader has a communication only with few from these 400 users, then there would not be any essential difference from the public sharing.

4.2. Specificity of the Commercial Aim

Any action, such as sharing a link, uploading it or posting it publicly, or in a closed group, should be subjected to legal qualification. It should be found out, whether this action has private or commercial aims.[41] In case of commercial use the law defines more restrictions, which can also be imposed for the broadcaster.[42] In certain cases it is possible to infringe the rights aimed at advertising (inappropriate advertisement, etc).

4.3. Challenge of Identifying the Violator

The biggest challenge created by the social networks is the identification of the violator. Namely, definition of the person who stands behind this action. In this regard it is possible to preform certain procedural actions such as guaranteeing the evidences, etc. Besides that, identification of the addressee can last during unexpectedly long time.

5. Analyze of the Result

Correlation between the private use, on one hand, public sharing and commercial aims, on the other, is reflected as follows: in the first case the right is not infringed,[43] while in other cases the raise

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38 LG Oldenburg, Urteil vom 11.01.2006 – 5S740/05.

39 *Jorbenadze S., Bakhtadze U., Macharadze Z.,* Media Law, Tbilisi, 2014, 90 (in Georgian).

40 *Bauer J. -H., Günther J.,* Kündigung wegen beleidigender Äußerungen auf Facebook, Vertrauliche Kommunikation unter Freunden?, NZA, Heft 2, 2013, 70.

41 *Schirmbacher M.,* Online-Marketing- und Social-Media-Recht, 2. Aufl., Frechen, 2017, 204-205.

42 Regarding this issue an appropriate regulation is defined by Georgian Copyright Association, which covers *inter alia* the spread of audiovisual works by media.

43 Even if the work is downloaded, *Katko P., Kaiser D.*, Immaterialgutrechte (kapitel 4), in: Praxishandbuch Rechtsfragen Social Media, *Splittgerber A.* (hrgb.), Berlin, 2014, 191.

of the claim is justified. While sharing the link, existence of the right on the spread work is below the frameworks of the "legal trust". It means that even if the person does not know about the existence of such right, he/she would be able to find out about such right by means of internet (the final result would be that this person "should have known" about such circumstance[44]).

6. Conclusions

International legislation does not define a unified notion of the audiovisual work, which gives possibility to certain countries to impose such definitions of audiovisual works in their national legislations. Accordingly, such definitions are not homogeneous, but each of them consists of the basic elements which are essential for the notion of the audiovisual work. These elements cause the specific character of this type of work, which, in itself, lead to the specific character of the legal regulation of audiovisual work. Posting audiovisual work in a social network has mostly specific character. In spite of the certain functional abilities of the social network, the consent of the copyright holder is necessary for the absolute protection of copyright.

It is true that the use of social network is conditioned by the 'personal reason'. However, while spreading the audiovisual work, it is directed to such a wide spectrum (indefinite group of people) that it is possible for the public use to be replaced by the private use. Granting such qualification is a result of examining each case.

While spreading the audiovisual work with public aim, it is possible to infringe the right, if the uploader did not have the initial consent from the copyright holder. The issue is more disputable when the work has not been spread for the commercial use.[45] For example, when the audiovisual work is shared on the web page, published in the social network on the timeline of certain person, then this person makes such work publicly accessible. It means that the uploader should have initial consent from the copyright holder for such sharing.

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8. Directive 2007/65/EC of the European Parliament and of the Council, 11/12/07.

[44] *Grünberger M.,* Zugangsregeln bei Verlinkungen auf rechtswidrig zugänglich gemachte Werke, ZUM, Heft 11, 2016, 914.

[45] While spreading the work with commercial aim the issue of infringing copyright is raised (when the uploader does not have such right).

9. Directive 2010/13/EU of the European Parliament and of the Council, 10/03/2010.
10. Gesetz über Urheberrecht und verwandte Schutzrechte, 09/09/1965.
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Decentralization Dilemma
(The Main Concepts, Practice and Georgian Reality)

The concept of decentralization is still disputable until now, while the decentralization process has become the global trend. However the outcomes of the decentralization are far from straightforward and besides the successful ones, there are also a lot of failure cases. The presented paper is analyzing the main concept of decentralization, its positive and negative impacts and discusses the challenges and the results of the decentralization reforms.

In Georgia, the decentralization reform appeared in all new government's agenda, however, the decentralization level still low. Today the need of the further decentralization reform is a subject of the debates within the political and civil actors, but considering the negative past experience, nobody really believes in the reform's future success. The paper is analyzing what may be the main root causes of this scepticism, what can be learned from the past experience and how to avoid the usual outcome - the reforms "without the results".

Key Words: *Decentralization, Local Self-Government, Devolution, Deconcentration, Delegation, Decentralization Reform.*

1. Introduction

In 2008 the World Bank's evaluation group admitted that the decentralisation has become the global trend and "everyone is doing it."[1] The waves of the decentralization reforms emerged all over the world, however, the reform's had different outcomes. Apparently, the process was not going smoothly and soon, besides the positive assessments, the calls about the dangers of the decentralization were heard.[2] This controversial reality led to the questions about the real value of the phenomena, which stipulated the interest of its re-evaluation.

The goal of the paper is to summarize the different views expressed about the advantages and pitfall of the decentralization and analyse the reasons and conditions, which can lead to the reform's different outcome.

The level of decentralization in Georgia is quite low. This was the conclusion produces by various local and foreign experts' studies. According to the results of the latest research conducted by European scholars, Georgia was placed in the group of countries with the lowest local government autonomy.

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1 *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 5.

2 See *Treisman D.*, The Architecture of Government: Rethinking Political Decentralization (Cambridge Studies in Comparative Politics), Cambridge, New York, Melbourne, Madrid, Cape Town, Singapore, São Paulo, Delhi, 2007; *Prudhomme R.,* The Dangers of Decentralization, The World Bank Research Observer, Vol. 10, № 2, 1995; *Tanzi V.,* Pitfalls on the Road of Fiscal Decentralization, Working Papers Economic Reform Project, Global Policy Program (Carnegie Endowment for International Peace), 2001.

Georgia was ranked at 36th among 39 countries.[3] Thus the decentralization promises are not quite evident in the country, however, neither are the signs of the negative impact too. Therefore, the aim of the paper is to analyse the decentralization process characteristics in the country.

The paper has the following structure: The first part is devoted to the review of the concept of the decentralization and some other related concepts. The second part will discuss the different views about the advantages and pitfalls of the decentralization; The third part will analyse the challenges of the decentralization process and the fourth and final part will summarize the main features of the decentralization reforms in Georgia.

2. The Main Concepts

Decentralization is a broad concept, and there are a lot of definitions inspired by different theoretical conceptions. As some of the scholars admitted "Decentralization seems often to mean whatever the person using the term wants it to mean"[4] "Yet grappling with the difference in kinds and degrees of decentralization has produced a conceptual muddle."[5] It is not possible to discuss all these definitions in details in the paper, as it is a subject of the separate research, however, here there are presented the definitions which are important to explain the main issues of the article.

One of the complete and early definitions of the decentralization is suggested by Professor *Rondinelli*. "Decentralization is defined as the transfer or delegation of legal and political authority to plan, make decisions and manage public functions from the central government and its agencies to field organizations of those agencies, subordinate units of government, semiautonomous public corporations, area-wide or regional development authorities; functional authorities, autonomous local governments, or nongovernmental organizations[6]."[7] United Nations Committee of Experts on Public Administration proposed the following definition: "In governance and public administration, decentralization is commonly regarded as a process through which powers, functions, responsibilities and resources are transferred from central to local governments and/or to other decentralized entities. In practical terms, decentralization is a process of striking a balance between the claims of the periphery and the demands of the centre… It implies a transfer of political, financial, administrative and legal authority from the central government to regional/sub-national and local governments."[8] Pursuant to the World Bank's def-

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3 See *Ladner A., Keuffer K., Baldersheim H.,* Measuring Local Autonomy in 39 Countries (1990-2014), Regional and Federal Studies, Vol. 26, № 3, 2016, 321-357.

4 *Bird R. M.,* Threading the Fiscal Labyrinth: Some Issues in Fiscal Decentralization, National Tax Journal, Vol. 46, № 2, 1993, 208.

5 *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 34.

6 In the text the term ― nongovernmental organizations, includes non-government associations and enterprises.

7 *Rondinelli D.,* Government Decentralization in Comparative Perspective: Theory and Practice in Developing Countries, International Review of Administrative Sciences, Vol. 47, № 2, 1981, 137.

8 *UN,* Economic and Social Council, Committee of Experts on Public Administration, Definition of Basic Concepts and Terminologies in Governance and Public Administration, UN Secretariat E/C, 2006, 8, <http://unpan1.un.org/intradoc/groups/public/documents/un/unpan022332.pdf>, [20.09.2018].

inition: "Decentralization is the transfer of administrative and financial authority and responsibility for governance and public service delivery from a higher level of government to a lower level."[9]

According to these definitions, the concept of decentralization includes two main elements: functional – transfer of function and spatial – transfer of function from the centre to the periphery. However, there are cases when decentralization includes only functional element,[10] e.g., transferring function to the semi-autonomous public organization (agency).[11] Considering this variety the first case can be called vertical decentralization (functional and spatial) and the second – horizontal decentralization.

The broad nature of the concept of decentralization produces different forms (kinds) of decentralization. According to the most accepted view, there are the following forms of decentralisation: deconcentration, delegation, and devolution. However, some scholars also suggest one additional form – privatization. [12]

Pursuant to the World Bank's definition "Deconcentration is the lowest form of decentralization, in which responsibilities are transferred to an administrative unit of the central government, usually a field, regional, or municipal office."[13] "Deconcentration is shifting the workload from central government ministries to headquarters to staff located in offices outside of the national capital."[14] From a practical point of view, decentralization serves for functional discharging of the central government and for increasing responsiveness of the governance. In this case, the territorial unit remains within the structure of the central body under its strict hierarchical control (administrative control). The transferred function still is regarded as a central government's function. In addition, the territorial unit has no discretion to decide how to execute the relevant function or this discretion is extremely limited. This feature also defines the different levels of deconcentration.[15] In the case of Georgia, as a sample of deconcentration can serve the territorial body of the Ministry, which has minimal autonomy, another sample is the State Representative-Governor, which has some level of autonomy (regarding the issues of human resources

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9 *The World Bank,* Decentralization in Client Countries, An Evaluation of World Bank Support, Washington, 2008, 3.

10 See *Conyers D.,* Decentralisation and Development: A Framework for Analysis, Community Development Journal, Vol. 21, № 2, 1986, 88; *Rondinelli D.,* Government Decentralization in Comparative Perspective: Theory and Practice in Developing Countries, International Review of Administrative Sciences, Vol. 47, № 2, 1981, 137.

11 In the case of Georgia the sample may be a legal entities of public law.

12 See *Rondinelli D., Nellis J., Cheema S.,* Decentralization in Developing Countries, A Review of Recent Experience, World Bank Staff Working Papers № 581, Management and Development Series, № 8, 1983, 13-32; *The World Bank*, Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4; *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 32-56.

13 *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

14 *Rondinelli D.,* Government Decentralization in Comparative Perspective: Theory and Practice in Developing Countries, International Review of Administrative Sciences, Vol. 47, № 2, 1981, 137.

15 Ibid, 137; *Rondinelli D., Nellis J., Cheema S.,* Decentralization in Developing Countries, A Review of Recent Experience, World Bank Staff Working Papers № 581, Management and Development Series, № 8, 1983, 14-19.

management or in other decision-making processes within his/her competence), however his/her general status is the territorial representative of the Government of Georgia.

Delegation is defined as "delegation of decision-making and management authority for specific functions to organizations that are only under the indirect control of central government ministries."[16] In the case of delegation, the recipient organization has considerable decision-making autonomy. The central government executes only indirect control over the respective unit. Recipient organization may be out of the structure of the Government or any other public organizations, however, the function still remains as the government's function. The goals of the delegation of function can be a decrease in the bureaucracy, adaptation to local conditions or incorporating the business like management models in public administration, specifically, introducing the user pay mechanisms for the public services, distribution of revenue within the employees, or abolishing public servant status of the employees in public organizations and etc.[17] Delegation occurs at the horizontal level of the government and also at vertical – regional or another sub-national territorial level.[18]

In Georgia delegation of functions are practised in the case of e.g. Legal Entities of Public Law. The delegation also includes the cases of transferring public services to private organizations (e.g. United Water Supply Company of Georgia). The sample of the vertical delegation is also a delegation of powers to local self-government's units or to the certain territorial agencies, e.g. Regional Development Agencies in Poland or Lithuania and etc.

Some scholars define the Privatization as a separate form of decentralization. In this case, the term does not mean privatizing public property (however, the process may include the public property privatization too) but the process of transferring to or sharing the function with the private sector. Privatization takes place when the government completely or partially abandons the function in favour of the private sector. After this the government loses responsibility over function (it's out of its competence) or partially keeps it but it is not the only responsible body (shared function), in other words, in the case of privatization the execution of the function is either completely depends on private initiatives or the government partially keeps it and also allows the private initiatives referring the function (e.g. existence of the public and private elderly care homes or public and private schools). [19]

"Devolution is the deepest form of decentralization, in which a government devolves responsibility, authority, and accountability to lower levels with some degree of political autonomy."[20] Devolution is a transfer of decision making, financial, and administrative functions to the sub-national public

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16 *Rondinelli D.,* Government Decentralization in Comparative Perspective: Theory and Practice in Developing Countries, International Review of Administrative Sciences, Vol. 47, № 2, 1981, 138.

17 See *Rondinelli D., Nellis J., Cheema S.,* Decentralization in Developing Countries, A Review of Recent Experience, World Bank Staff Working Papers № 581, Management and Development Series, № 8, 1983, 19-24; *The World Bank*, Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

18 It should be noted that these are only conceptual definitions. These definitions may not be coinciding with the terms used in Georgian legislation.

19 *Rondinelli D., Nellis J., Cheema S.,* Decentralization in Developing Countries, A Review of Recent Experience, World Bank Staff Working Papers № 581, Management and Development Series, № 8, 1983, 28-32.

20 *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

bodies, which are not the structural parts of the central government. These may be the local self-government or regional autonomies. These units are the autonomous governments within the political system of the country. This means that the discretion over its execution and the respective political responsibility are completely transferred to the sub-national government.[21] In this case, the central government usually keeps very limited supervision powers over the sub-national government. [22] Considering these specific features some scholars argue that the devolution is not the form of the decentralization. In their point of view, devolution is completely different and separate form of power execution.[23]

The main point of the interest of the paper is decentralization form – devolution. However, before the start of the discussion about this topic one more theoretical issue needs to be specified.

Scholars *Parker* and *Schneider* admit that the scientific analysis of the different concepts and forms of decentralization are generally provided in three dimensions, these are: political, fiscal and administrative. Consequently, they suggest definitions of political, fiscal and administrative decentralization. [24] It should be mentioned that this approach is shared by the World Bank too. We also agree that the dimensional approach simplifies the decentralization research, therefore, we will frequently apply to this approach during our future discussions.

"Administrative decentralization means how the responsibilities and authorities for policies and decisions are shared between levels of government and how these are turned into allocative outcomes."[25] The administrative dimension of decentralization is interested in the territorial distribution of powers and function and also issues regarding the executive autonomy of the relevant bodies. Administrative dimension is "focused on the administrative effects of granting local jurisdictions autonomy from central control. This autonomy is constituted by general policymaking authority and personnel control, as well as control over public finances."[26]

Political decentralization "means how the voice of citizens is integrated into policy decisions and how civil society can hold authorities and officials accountable at different levels of government."[27] "Under politically decentralized systems citizens define interests and form identities on the basis of local

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21 *Rondinelli D., Nellis J., Cheema S.,* Decentralization in Developing Countries, A Review of Recent Experience, World Bank Staff Working Papers № 581, Management and Development Series, № 8, 1983, 28-32.

22 See *Kakhidze, I.,* Administrative Supervision over Local Self-Government Bodies, Comparative Analysis, Tbilisi, 2012, 31-44 (in Georgian).

23 See *Sherwood P. F.,* Devolution as a Problem of Organization Strategy, Comparative Urban Research, *Daland R. T.* (ed.), Beverly Hill, 1969, 60-87.

24 See *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 32-56; *Parker N. A.*, Decentralization The Way Forward for Rural Development, Policy Research Working Paper 1475, The World Bank Agriculture and Natural Resources Department Sector Policy and Water Resources Division, 1995; *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

25 *The World Bank*, Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

26 *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 37.

27 *The World Bank*, Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

concerns, and organizations such as parties and social movements operate locally and compete over local issues and in a local election."[28] The political decentralization exists when local politics at least partially is separated from the central politics and local political actors possess the certain level of discretion. Here, the most important thing is the location of the accountability centre. If it is presented at the local level, it means that it is inclined toward the local citizens if it is located at the upper territorial level it means that it is deviated toward the upper level of the government. The best indicator of political autonomy is the presence of the elected local authorities. [29]

"Fiscal decentralization means the assignment of expenditures, revenues (transfers and/or revenue-raising authority), and borrowing among different levels of governments." [30] The main challenge of the fiscal decentralization "is to locate resources at the level of government that optimizes social welfare. Systems which are fiscally decentralized locate a greater proportion of fiscal resources at a level rather than the centre."[31] Thus the fiscal dimension of the decentralization means the amount of public finances, which is available for local government's disposal and the level of control over them.

3. Decentralization Advantages and Pitfalls

3.1. Decentralization Advantages

There are ongoing debates about the importance and advantages of the decentralization. The idea of decentralization has recruited a lot of academic supporters. It also achieved recognition at the international level. Powerful international actors such as the World Bank, United Nations Organization, and USAID became the strong lobbyists of the decentralization.

The most important idea which stands behind the concept of the decentralization is the Principle of Subsidiarity. The main essence of the Principle of Subsidiarity is very well reflected in the European Charter of Local Self-Government. According to the Charter "Public responsibilities shall generally be exercised, in preference, by those authorities, which are closest to the citizen. Allocation of responsibility to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy." [32] The main idea of this principle is the belief that the government which is closer to the citizens is more aware of the local needs and conditions, better controlled by the citizens and consequently

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28 *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 14.

29 Ibid, 39-40.

30 *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 4.

31 *Schneider A.,* Decentralization: Conceptualization and Measurement, Studies in Comparative International Developments, Vol. 38, № 3, 2003, 36.

32 *Council of Europe*, Explanatory Report, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://conventions.coe.int/Treaty/EN/Reports/HTML/122.htm>, [15.04.2018].

more capable of providing efficient and high-quality service.[33] Potsdam University's Professor *Fuhr* writes that: "The clearest, and most important, is that public goods and services should be provided by the lowest level of government that can fully capture the costs and benefits."[34]

There can be identified two groups of arguments while arguing about the advantages of the decentralization: political and economic. Historically the main arguments for decentralization had been political, however, later the number of economic arguments also emerged.

The political arguments for decentralization emphasize on decentralization as a democratic method of governance, specifically, the main accent is made on the advantages caused by increased participation, accountability and balanced central power.

The World Bank indicates that decentralization can enhance political stability, increase efficiency and accountability of the government and stipulate the equal territorial development.[35] The *USAID* Handbook of Democracy and Governance states that the "Decentralization of government authority and responsibility can increase the competence and responsiveness of public agencies by reducing the burden on those at the centre and allowing those most affected by an issue to make decisions about it. It enables citizens who are most directly concerned to influence decision-making by putting the source of the decision closer to them."[36]

Professor *Illner* suggests that decentralization can contribute to the democratic transformation of the country, specifically decentralization: increases citizens participation in local administration; stipulates local political elite formation; provides check and balance of the central power by the subnational government; improves participation opportunities for local and regional actors in the process of local economic and social development, and discharges overloaded center.[37]

Crook and *Manor* identified 14 reasons for decentralization. They believe that decentralization: Improves the process of governance, as the government is more informed and has better position for effective administration; increases citizens participation intensity and gives the sense of ownership of the public projects; contributes to the greater coordination of policies and personnel from numerous line ministries, (this tends to happen with decentralization at intermediate levels); breaks up bottlenecks and reduces delays in decision making; enhances local political participation and strengthens local associational activity; encourages partnerships between the government agencies and the private sector; makes the governance processes more transparent; creates greater opportunities for local government to

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33 *Nemec J.,* Decentralization Reforms and their Relations to Local Democracy and Efficiency: CEE Lessons, Uprava, Vol. 5, 2007, 8-9; *The World Bank,* Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 3.

34 *Fuhr H.,* Institutional Change and New Incentive Structures for Development: Can Decentralization and Better Local Governance Help?, Welt Trends, № 25, 1999, 28.

35 *The World Bank,* Entering the 21st Century, The World Bank Development Report 1999/2000, Oxford, 1999, 107-111.

36 *USAID,* Handbook of Democracy and Governance Program Indicators, Technical Publication Series (Center for Democracy and Governance Bureau for Global Programs, Field Support and Research, U.S. Agency for International Development, 1998, 153, <http://www.managingforimpact.org/sites/default/files/resource/handbook_of_democracy_and_governance_program_indicators.pdf>, [20.09.2018].

37 *Illner M.,* Issues of the Decentralization Reforms in Former Communist Countries, Informationen zur Raumentwicklung, Vol. 7, 2000, 391.

influence the central decision-making process; enhances the accountability; reduces the overall corruption; increases citizens' understanding of the government's (health, education, and sanitation) programs; helps programs be more responsive and appropriate to local conditions; increases the legitimacy of the government and trust; helps to scale up successful practice and replication.[38]

In addition to the above arguments, decentralization is discussed as a mechanism for conflicts prevention. Specifically, the different researches indicate that decentralization may become an effective ethnic and regional conflicts prevention instrument.[39]

As it has been mentioned above, besides the political approval there are also economic arguments for decentralization. Economic arguments imply the advantages like the improvement of the public services, increase of government's effectiveness and encouragement of the equal territorial development of the country.

From this point of view the various studies indicate to the following advantages of the decentralization: Professor *Klugman* argues that "In principle, decentralization may promote economic activity via several routes including an increased infusion of capital and other resources, the more extensive provision of infrastructure, and a more effective enabling environment that would have been the case under a centralized system."[40] *Martinez-Vazquez* and *McNab* claim that decentralization supports economic growth as it improves macroeconomic stability.[41] A study conducted by *Ezcurra* and *Pascual* proves that fiscal decentralization may contribute to a better-balanced distribution of the resources across the country and reduce regional disparities.[42] Oates and Tiebout believe that fiscal decentralization supports economic and political development. [43]

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38 *Crook R., Manor J.,* Democratic Decentralization, OECD Working Paper Series, The World Bank, Washington, 2000, 23-24.

39 See *Von Braun J., Grote U.,* Does Decentralization centralization Serve the Poor? Paper presented at the IMF Conference on Fiscal Decentralization, November 20-21, Washington, 2000; *Smoke P.,* The Role of Decentralisation/Devolution in Improving Development Outcomes at the Local Level: Review of the Literature and Selected Cases, Local Development International LLC, New York, 2013, 3; *Brosio G.,* An Evaluation of the World Bank Support for Decentralization in the Middle East and North Africa Countries of Algeria, Egypt, Morocco, Tunisia, West Bank, Background Paper for Independent Evaluation Group, The World Bank, Washington, 2002; *The World Bank*, Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 5; *Grasa R., Camps A. G.,* Conflict Prevention and Decentralized Governance: Some remarks about the State of the Art in Theory and Practice, 2nd ed., Barcelona, 2010.

40 *Klugman J.,* Decentralisation: A survey of Literature from a Human Development Perspective, United Nations Development Programme Occasional, Human Development Report Office, Paper № 13, 1994, 3, <https://ssrn.com/abstract=2294658>, [20.09.2018].

41 See *Martínez-Vazquez J., McNab M. R.,* Fiscal Decentralization, Macrostability, and Growth, Hacienda Pública Española/Revista de Economía Pública, Vol. 179, 2006, 25-49.

42 See *Ezcurra R., Pascual P.,* The Link between Fiscal Decentralization and Regional Disparities: Evidence from Several European Union Countries, Environment and Planning, Vol. A40, № 5, 2008, 1185-1201.

43 See *Oates W.,* An Essay on Fiscal Federalism, Journal of Economic Literature, Vol. 37, № 3, 1999, 1120-1149; *Tiebout C.,* A Pure Theory of Local Expenditures, Journal of Political Economy, Vol. 64, № 5, 1956, 416-24.

3.2. Decentralization Pitfalls

Notwithstanding, the above-discussed impressive list of decentralization advantages its real capacity is still limited. There are a number of studies which indicate the possible pitfalls of decentralization, especially in the developing countries. Therefore positive promises of the decentralization should not be assessed excessively or overwhelmed expectations created. "Demand for decentralization is strong throughout the world. But the benefits of decentralization are not … obvious … and there are serious drawbacks that should be considered in designing any decentralization program."[44] – admits the World Bank's expert *Prudhomme*.

American Professor of political science *Treisman* in his book – "The Architecture of Government: Rethinking Political Decentralization", presented a sceptical view about the decentralization. The author discussed the most "advertised" decentralization advantages and argued that none of them can claim to be a general truth or provide with the convincing arguments. He developed the idea that the importance of decentralization is exaggerated mainly because of a bad cliché of centralization, which comes from the historical experience, where centralization was usually associated with dictatorship, and fascist's regimes. In his opinion, decentralization should be regarded as neutral phenomena rather than declaring it as a cure for all problems. He also indicated two evident "bad" sides of the decentralization. These are increased fiscal pressure (e.g. increased administrative expenses) and reduced fiscal coordination (e.g. the problem of mobilization of the financial resources to a specific sector).[45]

Crook and *Manor* pointed to the following possible limitations of the decentralization: decentralization does little to encourage long-term development perspectives and it also doesn't increase economic growth rate. In addition, it is vulnerable to corrupted political elite capture.[46] Correlation between decentralization and economic growth was not proved also by the study conducted by *Ezcurra* and *Rodriguez-Pose's*.[47] *Prudhomme* warns us about four "dangers" of decentralization: "Decentralization can increase disparities;", "Decentralization can jeopardize stability"; "Decentralization can undermine efficiency," and it can create a good ground for the corruption.[48] *Estache* and *Sinha* concluded that decentralization could increase both state's aggregated and subnational infrastructural expenditures.[49]

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44 *Prudhomme R.,* The Dangers of Decentralization, The World Bank Research Observer, Vol. 10, № 2, 1995, 201.

45 *Treisman D*., The Architecture of Government: Rethinking Political Decentralization (Cambridge Studies in Comparative Politics), Cambridge, New York, Melbourne, Madrid, Cape Town, Singapore, São Paulo, Delhi, 2007, 11-21.

46 *Crook R., Manor J.,* Democratic Decentralization, OECD Working Paper Series, The World Bank, Washington, 2000, 24.

47 See *Ezcurra R., Rodriguez-Pose A.,* Political Decentralization, Economic Growth and Regional Disparities in the OECD, Regional Studies, Vol. 47, № 3, 2013, 388-401.

48 See *Prudhomme R.,* The Dangers of Decentralization, The World Bank Research Observer, Vol. 10, № 2, 1995, 202-220.

49 See *Estache A., Sinha S.,* Does Decentralization Increase Public Expenditure in Infrastructure?, Policy Research Working Paper 1457, The World Bank, Washington, 1995.

Generally, the most critic comes toward the fiscal dimension of the decentralization. Numerous articles refer to the problems caused by fiscal decentralization in developing countries. The main emphasis is made to the following risks of the fiscal decentralization: fiscal imbalance and over-borrowing;[50] territorial disparities;[51] institutional capture by local elite groups and corruption;[52] efficiency decrease and reduction of the economic growth.[53]

In conclusion, the positive promises and pitfalls of decentralization usually are controversial and even contradictory, especially when it comes to the economic development and fiscal aspects of the decentralization (See, Table № 1). The American scholar *Smoke* admits that "Assessing outcomes associated with decentralization is far from straightforward. Many relevant constraints are empirical. There is no escaping the fact that decentralization – both conceptually and practically – is a highly complex and diverse phenomenon."[54]

Therefore, before the decision, whether decentralization is "good" or "bad" it would be appropriate to analyses the specific cases of the decentralization. In addition, it is interesting to identify the factors which had the decisive role for the reforms success or failure cases in the different countries. The next part of the paper will discuss the above-mentioned subjects.

Table № 1. Decentralization advantages and pitfall compared.

Advantages	Pitfalls
o Check and balance of the central power	o Reduced fiscal coordination
o Formation of the local political elites	o Increased fiscal disbalance and over borrowing
o Increased participation in the decision-making process	o Hampered economic growth
o Development of the civil society	o Decreased efficiency

[50] See *Tanzi V.,* Fiscal Federalism and Decentralization: A Review of Some Efficiency and Macroeconomic Aspects, Annual World Bank Conference on Development Economics 1995, *Bruno M., Pleskovic B.* (eds.), Washington, 1996, 295-316

[51] See *Rodriguez-Pose A., Ezcurra R.,* Does Decentralization Matter for Regional Disparities? A Cross-country Analysis, Journal of Economic Geography, Vol. 10, № 5, 2010, 619-644; *Jorge M., McNab R.,* Fiscal Decentralization and Economic Growth, World Development, Vol. 31, № 9, 2003, 1597-1616.

[52] See *Prudhomme R.,* The Dangers of Decentralization, The World Bank Research Observer, Vol. 10, № 2, 1995, 201-220; *Treisman, D.,* The Causes of Corruption: A Cross National Study, Journal of Public Economics, Vol. 76, № 3, 2000, 399-457.

[53] See *O'dwyer C., Ziblatt D.,* Is Decentralised Government More Efficient and Effective?, Commonwealth & Comparative Politics, Vol. 44, № 3, 2006, 326-343; *Tobin I.,* Does Decentralization Reform Always Increase Economic Growth?: A Cross Country Comparison of the Performance, International Journal of Public Administration, Vol. 10, № 33, 2010, 508-520; *Davoodi H., Zou H. F.,* Fiscal Decentralization and Economic Growth: A Cross-country Study, Journal of Urban Economics, Vol. 43, № 2, 1998, 244-257.

[54] *Smoke P.,* The Role of Decentralisation/Devolution in Improving Development Outcomes at the Local Level: Review of the Literature and Selected Cases, Local Development International LLC, New York, 2013, 2.

o Increased transparency	o Increased risks of corruption
o Enhanced public sectors accountability	o High territorial disparities
o Unburdened the overloaded central state	
o Reduced bureaucracy	
o Adaptation to the local needs and conditions	
o Increased economic growth	
o Absorbed regional and ethnic conflicts	
o Improved quality of public services	
o Reduced territorial disparities	

4. The Challenges of the Decentralization Process

In 2008 the World Bank published the evaluation report on the results of decentralization reforms supported in Client Countries. The report analyzed the reforms implemented from 1990 to 2007. The overall conclusion was that the two third of the reforms were successful. The reforms "was most successful in strengthening legal frameworks for decentralization and intergovernmental relations, improving public financial management at the local level, and helping central governments establish transparent fiscal transfer systems. It was much less successful in helping to enhance own-source revenue at the local levels, clarifying responsibilities of different levels of government, and strengthening citizen oversight."[55]

OECD experts' research which analysed the decentralization process in 19 developing countries, showed the mixed results. In one-third of the studied countries, decentralization reform was evaluated as successful. However, in the majority cases, it had neutral results. Generally, the reform was not successful in the countries, with poorly developed public institutions and post-war situation.[56]

The interesting results had American Professor *Boex*, who analysed fiscal decentralization reforms in developing countries. According to his conclusion although there are some successful decentralization reform cases within the developing world (e.g. Poland, Indonesia, and South Africa) it is hard to come up with the examples where "fiscal decentralization reforms have been an indisputable success story."[57]

Completely opposite results had one of the latest decentralization research conducted in 2017. The study covered 23 OECD's countries. The research showed that fiscal decentralization has a positive impact on the government's quality. The positive trend was caused by better informed sub-national authorities and enhanced inter-jurisdictional competition. The research also indicated that the countries with low government's qualities (corrupted and non-stable government institutions and etc.) are more tend to the

[55] *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, ix.

[56] *Johannes J., Kauffman C., McDonnell I., Osterrieder H., Pinaud N., Wegner L.,* Decentralisation and Poverty in Developing Countries: Exploring the Impact, Working Paper, Development Center, № 236, 2004, 22.

[57] *Boex J., Martinez-Vazquez J., Schaeffer M*., An Assessment of Fiscal Decentralization in Georgia, Problems of Economic Transition, Vol. 49, № 1, 2006, 3.

fiscal centralization. The inefficient and corrupted government didn't want to lose control over public resources caused by decentralization. The results also supported the view that fiscal decentralization can lead to equal territorial development.[58]

Although decentralization reforms had not the equivocal results, it still takes a high place in many developing countries' reforms agendas. Decentralization reforms "have an enormous potential and could, if properly designed and implemented, significantly improve the efficiency of the public sector. Decentralization measures are like some potent drugs, however: when prescribed for the relevant illness, at the appropriate moment and in the correct dose, they can have the desired salutary effect, but in the wrong circumstances, they can harm rather than heal."[59] – explains *Prudhomme*. Czech scholar *Nemec* after the study on decentralization reforms in post-communist countries came to the following conclusion: Decentralization reforms, if it is wrongly designed and implemented, may deepen the existing problems, as it "opens additional space for many forms of "government failure."[60]

Therefore, one of the main goals of the decentralization research is the precise identification and analyses of the main factors which can lead to the reform's success or failure. The different scholars and international organizations indicate the following challenges of the decentralization reforms in the developing countries: limited financial and administrative resources (both at central and sub-national level), weak civil society, strong rent-seeking local elites, short democratic governance history, lack of the reform's ownership[61] and a weak political commitment. It is logical that these weaknesses make developing countries more vulnerable in front of the decentralization pitfall. There are much less of these problems in developing countries.[62]

Quite often the governments of developing countries don't meet decentralization reforms with a great enthusiasm, decentralization is perceived as a "tribute" which should be paid to the international organizations in a change of various forms of support. Moreover, there are many cases when despite declared formal readiness and political will the strong resistance against the reform emerges within the government itself. Sometimes the problems are also stipulated by the unwillingness of coordination and cooperation between the central and sub-national levels of government.[63]

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58 See *Kyriacou A., Muinelo-Gallo L., Roca-Sagalés O.,* Regional Inequalities, Fiscal Decentralization and Government Quality, Regional Studies, Vol. 7, № 6, 2017, 945-957.

59 *Prudhomme R.,* The Dangers of Decentralization, The World Bank Research Observer, Vol. 10, № 2, 1995, 201.

60 *Nemec J.,* Decentralization Reforms and their Relations to Local Democracy and Efficiency: CEE Lessons, Uprava, Vol. 5, 2007, 33.

61 Lack of the reform's ownership means the situation when the reform doesn't consider the positions of the different relevant actor(s) (in the text – ruling political elite) or/and the reform is forced by the third party.

62 See *The World Bank,* Entering the 21st Century, The World Bank Development Report 1999/2000, Oxford, 1999, 121-22; *The World Bank*, Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 4-5; *Cheema S., Rondinelli D.,* Decentralizing Governance: Emerging Concept and Practice, Washington, 2007, 9; *Crook R., Manor J.,* Democratic Decentralization, OECD Working Paper Series, The World Bank, Washington, 2000, vii, 3-5; *Smoke P*., Implementing Decentralization: Meeting Neglected Challenges, In Making Decentralization Work: Democracy, Development, and Security, Making Decentralization Work: Democracy, Development, and Security, *Eaton E., Smoke P., Connerley K.* (eds.), London, 2010, 198-205.

63 Ibid.

The different experts provide the governments with following general recommendations for successful decentralization (See, Table № 2)[64] reform: Firstly, the context of the particular country should be considered, as what can work in one country and in a certain situation can fail in another. Consequently copying from other countries' successful cases needs local adaptation. "Thus, whether and how to decentralize or not is a question that can be answered only against the background of country-specific contexts and institutions."[65] "No grand generalizations emerge — as with much research on decentralization, outcomes depend on political, institutional and socio-economic context, which vary and often interact in different ways."[66] Secondly, decentralization reform is incremental[67] process, especially it is true for developing countries, where respective capacities (human, financial resources and etc.) usually don't pre-exist, and thus it needs step by step development. Consequently, radical and swift decentralization reform is less expectable to succeed. Thirdly, decentralization is about behavioural change and it demands transformation not only from the government but from the society too. "Decentralization is not an instantaneous act; on the contrary, it is typically a complex and lengthy process that often involves basic changes in attitudes and behaviours by actors at all levels of government as well as by citizens."[68]

There is a lot of suggestion about how decentralization can be managed effectively. Here we shall discuss only some of them. *Nemec* formulated four principles, which should be considered before the decentralization: "First, decentralization should be understood as a tool and not as the definite goal. Second, decentralization is not a simple and one-dimensional strategy, and its outcomes and impacts will differ according to concrete time and environment. Third, to decentralize, opportunity (the right time selection), capacity and preparedness are needed. Fourth, decentralization strategies have to take account of all the main involved elements – especially legal, financial, territorial, and ownership aspects of the process."[69]

The World Bank identifies three elements for successful decentralization reform: "These include adequate financial resources, accountability for the use of resources, and government commitment and ownership. If decentralization takes place without these three conditions, diffused accountability and poor service delivery are likely to result."[70] *Rondinelli* claims that "the ability of government to implement decentralization programs depends on the existence of, or the ability to create, a variety of political

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64 The table № 2 summarizes the results of the discussions below and presents the main ingredients for successful planning and implementation of the decentralization reform.

65 *The World Bank,* Decentralization in Client Countries an Evaluation of World Bank Support, Washington, 2008, 5.

66 *Smoke P.,* The Role of Decentralisation/Devolution in Improving Development Outcomes at the Local Level: Review of the Literature and Selected Cases, Local Development International LLC, New York, 2013, 19.

67 Incrementalism – gradual, step by step change.

68 *Smoke P.*, Implementing Decentralization: Meeting Neglected Challenges, In Making Decentralization Work: Democracy, Development, and Security, Making Decentralization Work: Democracy, Development, and Security, *Eaton E., Smoke P., Connerley K.* (eds.), London, 2010, 213.

69 *Nemec J.,* Decentralization Reforms and their Relations to Local Democracy and Efficiency: CEE Lessons, Uprava, Vol. 5, 2007, 34.

70 *The World Bank,* Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 5.

administrative, organizational and behavioural conditions, and to provide sufficient resources at the local level to carry out decentralized functions."[71] Other researchers admit that "Decentralisation process is more likely to have a positive impact … if the central government is committed to the purpose of decentralization, the involved actors have the capacity (financial and human) to participate in decision making, checks and balances are established at a local level to control for rent-seeking and corruption, and policies – internal and external – are sufficiently coherent with the decentralisation policy."[72]

To sum up, we have mixed results about decentralization reforms, and we have no consensus concerning the pros and cons of decentralization. "The debate on whether decentralization is "good" or "bad" is unproductive since decentralization is a political reality worldwide - one that varies greatly in form within and among countries."[73] Thus, we can share the following positions referring the decentralization reforms: "Most if not all experts would agree that decentralization is important … but also … it does not represent unique "all treating" medicine. Decentralization has the same character as most of the other reform mechanisms – it can bring both positive and negative effects, depending on local conditions, environment and connected complementary measures."[74] "Although evidence can be found for both beneficial and negative consequences of decentralization among and within countries, many of the failures of decentralization are due less to inherent weaknesses in the concept itself than to government's ineffectiveness in implementing it."[75] Logically the country, with poor government quality and weakly developed public institutions, has limited capacities to design and effectively implement any kind of reform.

Table № 2. The main ingredients for successful planning and implementation of the decentralization reform.

Decentralization Process	
Planning	**Implementation**
o Consider the local context	o Political will
o Define the definite goals	o Right sequence
o Incrementalism	o Human resources
o Create reforms Ownership	o Financial resources
o Choose the right time	o Stipulation of the behavioural change
o Involve all relevant actors	

71 *Rondinelli D.,* Government Decentralization in Comparative Perspective: Theory and Practice in Developing Countries, International Review of Administrative Sciences, Vol. 47, № 2, 1981, 142.

72 *Johannes J., Kauffman C., McDonnell I., Osterrieder H., Pinaud N., Wegner L.,* Decentralisation and Poverty in Developing Countries: Exploring the Impact, Working Paper, Development Center, № 236, 2004, 22.

73 *Litvack J., Ahmad J., Bird R.,* Rethinking Decentralization in Developing Countries, Washington DC, 1998, 3.

74 *Nemec J.,* Decentralization Reforms and their Relations to Local Democracy and Efficiency: CEE Lessons, Uprava, Vol. 5, 2007, 33.

75 *Cheema S., Rondinelli D.,* Decentralizing Governance: Emerging Concept and Practice, Washington, 2007, 9.

5. Decentralization Process in Georgia (Problems and Challenges)

As it has been already mentioned in the Introduction the level of decentralization in Georgia is very low. Thus the potential promises of decentralization are not quite evident, however, there are no signs of the negative impacts too. Therefore this part of the paper will mainly focus on the decentralization process assessment and review in the country.

Decentralization process in Georgia can be divided into three main periods. Decentralization reforms in each period were characterized by specific features and can be called as three reforms' generations. The first generation of decentralization reform had begun in 1995 and continued until 2003.[76] This is the period when the basic institutional foundations of the local self-government formed. Second generation reforms emerged after the Rose Revolution in 2003. During this period Georgia ratified the main local self-government standard-setting international treaty – European Charter of Local Self-Government. Third generation reforms born in 2012 after the new coalitional government came to power. Strengthening of the local government was among its main pre-election promises.

Due to the range of the topic, it is impossible to do a complete and detailed analysis of the past period. Therefore, the paper has systematized and analysed the existing local and foreign scholars' studies and international organizations' reviews and conclusions referring this period. It worthy to mention that although some of this assessment and conclusion were made 10 years ago, they have not lost actuality even now. After the systematization and analysis of the collected information, 11 groups of challenges/problems of the decentralization process in Georgia have been identified. For simplification, each of them was granted its separate name. The analysis below will be presented according to these groups:

First, the challenge of the post-communist state. Hyper centralize model of governance inherited from the Soviet Union time still strongly persists in Georgia. Local government generally is understood as a part of the central government. Moreover, this perception is accepted both by the central and local governments. While studying decentralization processes in Eastern Europe Professor *Illner* admitted that in the post-communist country the local government "follows the practice inherited from the communist regime, accepting, if not seeking the direction and instruction of the upper levels of government."[77] As it is evident, the challenge has not been losing its actuality in Georgia until now. "Local politics are still hampered by Soviet-era political mores. Local power brokers often dominate their areas, and many local

[76] The starting point for the beginning of discussions about the decentralization reforms in Georgia is 1995. During 1991-1995 Georgia undergone the civil war and territorial conflict provoked by the Russian Federation, thus during the period decentralization policy had a little attention and only a short-term purposes. There are a few studies about the assessment of the period too. From 1995 the overall situation in Georgia stabilized, which was followed by the adoption of the Constitution of Georgia. The constitution envisaged the first short article about local self-government. In 1997 the Parliament of Georgia adopted the first more or less codified law — the Organic Law on Local Self-Government and Governance of Georgia.

[77] *Illner M.,* Devolution of Government in the Ex-Communist Countries: Some Explanatory Frameworks, Local Democracy in Post Communist Europe, *Illner M., Wollmann H. Baldersheim H.* (eds.), Opladen, 2003, 327.

officials are accustomed to taking their cues from the central government."[78] – wrote the *Freedom House* in 2015 report about Georgia.

Local government has no initiatives and involvement in the central decision-making process. This problem is underlined in the recommendations of the Council of Europe's Congress of Local and Regional Authorities in 2015, which emphasize the need for the establishment of a more effective and comprehensive mechanism for enhancing the local government's participation in the central decision-making process concerning to local affairs. [79]

It should be specified that the centralized governance model is not an "evil" itself and it can be used in the process of governing the democratic state. However, the view presented by American scholar *Treisman* should be taken into account: "centralized governance is not a "bad" itself, especially when it is used to improve the governance efficiency and effectiveness in providing public services. However, its positive effects are not quite evident when it becomes the mechanism of the ruling elites' political dominance,"[80] Unfortunately, in "Eastern Europe, it remains true even now that the most important influence is not" Western European model of governance "but the Russian/Soviet model." [81]

Second, the syndrome of the post-communist society. Within Georgian society, the knowledge about the importance and role of the local government stands very low. Usually, people don't even distinguish between local and central governments. "Local autonomy is not a typical Georgian tradition. Consequently, Georgian citizens do not pay proper attention to local self-government, and they do not differentiate between central and local administrations."[82]

According to the *National Democratic Institute* (*NDI*) survey results conducted in 2015: 60% of citizens admit that they don't know the functions of the local government and 83% of respondent don't know their Local Council Members. Only 6 % of Georgians report having contacted with the Local Council's officials, 3 % of Mayors' offices.[83] What is more, the majority of the local residents have the problem of distinguishing between the local and central government. The same conclusions were made by other independent studies.[84] As one Georgian expert indicated in 2010: "People still believe that

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78 *Mitchel L.,* Nations in Transit, Georgia, Freedom House Report, 2015, 258-259, <https://freedomhouse.org/sites/default/files/NIT2015_Georgia.pdf>, [20.09.2018].

79 *CLRA,* Congress of Local and Regional Authorities, Post-monitoring Georgia, Final Roadmap Chamber of Local Authorities, Rapporteurs: Nigel Mermagen, United Kingdom and Helena Pihlajasaari, Finland, CG/MON/2015(27)15, 2015, <https://rm.coe.int/16807195fd#_ftn1>, [20.09.2018].

80 *Treisman D*., The Architecture of Government: Rethinking Political Decentralization (Cambridge Studies in Comparative Politics), Cambridge, New York, Melbourne, Madrid, Cape Town, Singapore, São Paulo, Delhi, 2007, 40-41.

81 *Pollitt C.,* An Overview of the Papers and Propositions of the First Trans-European Dialogue (TED1), NISPACEE Journal of Public Administration and Policy, Special Issue: A Distinctive European Model? The Neo-Weberian State, Vol. 1, № 1, 2008, 10.

82 *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 182.

83 *NDI,* National Democratic Institute, NDI Poll: Low Awareness and Approval for Constitutional and Legislative Changes; Average Assessment for Local Government, Tbilisi, 2015, <https://www.-ndi.org/August-2015-Public-Opinion-PressRelease-Georgia>, [20.09.2018] (in Georgian).

84 *Salamadze V.,* Citizen Participation in Self-Governance, Civil Society Institute, Tbilisi, 2009; *Swianiewicz P.* Public Opinion about Local Government in Georgia, Tbilisi, 2011.

everything that should be done, even in the small villages somewhere in the mountains, by the president. If they don't have power, if they don't have a water supply, if a local shop doesn't work, they are ready to write a letter to the president of the country; "he should take care of us."[85]

Third, the syndrome of the post-conflict society. Usually, the term decentralization causes negative perceptions within the politicians and citizens in Georgia, as it is associated with the division of the country. "Georgian society historically has always faced the danger of territorial disintegration, and all Georgian culture and ideology are based on the idea of a unitary and strong state." [86]

There is a dominant belief within the society that decentralization could stipulate separatism. The country lost two regions at the beginning of the 1990s. Thus the fear of decentralization has become a kind of phobia in Georgian society.[87] However, this cautious is mainly exaggerated and far from reality. The situation is usually wrongly interpreted also by politicians. As Polish experts once admitted that it is "more of an excuse than a real obstacle to the devolution of powers and is very well used by the ruling political elites for their own political interests."[88]

The low knowledge and misunderstanding of the mission and importance of the local government caused extremely wrong interpretations. During the last decentralization reform in 2013, even the Georgian Orthodox Church, which has a very high level of trust in the country, came against the decentralization reform. "The culmination of the public debates was a statement made by the Patriarch Ilia II on December 4, 2013, according to which 'the implementation of the Local Self-Government draft Code will entail the disintegration of Georgia'." [89] This statement had a great public resonance. In the end, the reform's opposition within the government managed to change the initial draft law, which almost transformed decentralization reform into the facade reform. We meet this wrong perception in Georgia while in many countries decentralization is considered as a preventive mechanism for ethnic conflicts. [90]

Fourth, the phobia of losing control. One of the most problematic obstacles for the decentralization is a fear to lose political control over the local government. This is partially rooted in the syndrome of the post-communist state. After the second generation reform government abolished a lot of legal regulations which allowed the exercise of the direct control over the local government, however,

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85 *Swianiewicz P.* Public Opinion about Local Government in Georgia, Tbilisi, 2011, 20.

86 *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 182.

87 See *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 292; *Kandelaki K., Losaberidze D., Orvelashvili N.,* Local Government in Georgia Developing New Rules in the Old Environment, Developing New Rules in the Old Environment, Local governments in Eastern Europe, in the Caucasus and in Central Asia, Local Government and Public Service Reform Initiative, *Popa V., Munteanu I.* (eds.), Budapest, 2001, 309-310; *Bolashvili P.,* Fiscal Autonomy Problems of Local Government in Georgia, *Davey K.* (ed.), Fiscal Autonomy and Efficiency: Reforms in the Former Soviet Union, Open Society Institute, Budapest, 2002, 61-64.

88 *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 293.

89 *Losaberidze D.,* Local Self-Government Reform in Georgia 2013-2014, Local Self-Government in Georgia 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015, 190 (in Georgian); *Rimple P.,* Report Georgia, Annual, Freedom House, 2014, <https://freedomhouse.org/report/nations-transit/2014/georgia>, [20.09.2018]; *Skorupska A., Zasztowt K.,* Georgia's Local Government Reform: How to Escape from the Soviet Past, Policy Paper, Polish Institute of International Affair, Vol. 4, № 87, 2014.

90 See part 3.1.

this led to the emergence of a new informal control mechanism. It also should be noted that from 2003 almost all local elections (elections of the Local Councils and the Mayors) were won by the ruling political party. [91]

After the second generation reforms, many scholars and international organization indicated the increase of informal political control mainly exercised through the line ministries and the Governors. They also pointed out that after the municipal amalgamation reform in 2006[92] the bigger and fewer local units made central control much easier. [93]

After the third generation reforms, the problem of informal political control still remains.[94] This fact is proved by the former Deputy Minister of Regional Development and Infrastructure of Georgia when he officially declared the need to "overcome of the practice when Governor or the Minister perceives himself/herself as a chief of municipalities".[95]

Fifth, the low trust in local government. Local government has a low trust in the country, and this position is shared both by the central government and the local community. There is a dominant perception that local government has a weak human capacity to be responsible for something important in the country.[96] The human capacity of the local government is a real problem. However, there is no any study results available in the country which would provide us with the comprehensive analysis of the situation. The recent survey referring the issue conducted by *NDI* in 2017 gave the following result: "the majority believes there is a lack of professionalism in local government ... While a few people have interacted with local government institutions, the majority of those who have reports that they were

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91 Exeption was 2017 local election when non-ruling party won the position of the Mayor (In Tianety Municipality) and majority in the local council (in Borjomi municipality).

92 In 2006 the government abolished 1004 municipalities and instead created 64. As a result of this amalgamation reform, Georgia is one of the first ranked countries according to the size of the self-governing units (under the average population) in Europe with Denmark, Lietuva, and the United Kingdom of Great Britain.

93 *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 297-298; *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 184; *Losaberidze D.,* Local Self-Government Reform in Georgia 2013-2014, Local Self-Government in Georgia 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015, 12-13 (in Georgian); *Freedom House*, Report Georgia, Annual, Freedom House, 2010, <https://freedomhouse.org/report/nations-transit/2010/georgia>, [20.09.2018]; Freedom House, Report Georgia, Annual, Freedom House, 2009, <https://freedomhouse.org/report/nations-transit/-2009/georgia>, [20.09.2018].

94 *Mitchel L.,* Nations in Transit, Georgia, Freedom House Report, 2015, 258-259, <https://freedomhouse.org/sites/default/files/NIT2015_Georgia.pdf>, [20.09.2018]; *Rimple P.,* Report Georgia, Annual, Freedom House, 2014, <https://freedomhouse.org/report/nations-transit/2014/georgia>, [20.09.2018].

95 *Shergelashvili T.,* Interviewed by *Morgoshia T.*, Its Time for Local Self-Government, International Center for Civil Culture, Bulletin № 8, Tbilisi, 2015, <http://www.ivote.ge/images/doc/merve.pdf>, [20.09.2018] (in Georgia).

96 *Losaberidze D.,* Local Self-Government Reform in Georgia 2013-2014, Local Self-Government in Georgia 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015, 92-94, 116; *Salamadze V.,* Citizen Participation in Self-Governance, Civil Society Institute, Tbilisi, 2009, 58-68 (in Georgian).

treated with respect and that officials were competent."[97] Thus the mistrust to the local government in some degree is a kind of "cliché" and the sheer breadth of the assessments is often far from objective reality. According to the survey low degree of community participation in the local government activities, mistrust to the local government and a mere importance of the local authorities still remains as unresolvable challenges.[98]

Sixth, unresolved dilemma – administrative-territorial reform. The administrative-territorial reform of the country was a part of all three reforms' generations. However, still, the issue is not losing its actuality. As Professor *Swianiewicz* in his study indicated, the current administrative borders of the municipalities are not adequately responding to Georgia's social and geographical realities. Thus, there is a need for finding an effective balance between the local government's efficiency, local context, and local community interests. The fact is that the formation of larger municipalities has not resulted in a more effective and efficient local government. [99]

Seventh, the territorial disparities. It is noteworthy to mention that in Georgia high fiscal centralization level is one of the main causing factors for local disparities. The central government's grants distribution system stipulates greater inequality and also leaves a wide margin for central manipulation. Capital – Tbilisi and the administrative centre of Adjara autonomous republic – Batumi is getting much more from central budget per resident than other municipalities. Despite the fact that the experts, international organizations are constantly indicating to the problem the government of Georgia is failing to find effective response to address it. [100]

Eighth, the low motivation to perform better. High dependency of local revenues to the central transfers reduces the local efficiency. Local government has no interest in local economic growth, as it doesn't affect local revenue. Local government still has only one local tax – property tax. As the World Bank in its report indicates, this environment limits the local government's efficiency and causes demotivation. [101]

Ninth, mere functions. Local government lacks the functions to have a significant impact on the local community's development.[102] According to the Charter, the local government should have the right

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97 *NDI,* National Democratic Institute, NDI Poll: Low Awareness and Approval for Constitutional and Legislative Changes; Average Assessment for Local Government, Tbilisi, 2015, <https://www.ndi.org/August-2015-Public-Opinion-PressRelease-Georgia>, [20.09.2018] (in Georgian).

98 Ibid.

99 *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 298, 309.

100 *The World Bank*, Georgia Public Expenditures Review, Strategic Issues and Reform Agenda, Vol. 1, Washington, 2014, 63-66*; Murgulia S., Toklikishvili G., Gvelesiani G.,* Fiscal Decentralization In Georgia, Project - Strengthening Local Authorities – The Way Towards Decentralization, Project Founded By EU, The Center for Strategic Research and Development of Georgia, Tbilisi, 2011, 20-21, 55, <http://www.alda-europe.eu/newSite/public/eap/6-georgia-Fiscal-Decentralization-in-Georgia-study-eng.pdf>, [20.09.2018].

101 *The World Bank,* Georgia Public Expenditures Review, Strategic Issues and Reform Agenda, Vol. 1, Washington, 2014, 63-64.

102 See *Ladner A., Keuffer K., Baldersheim H.,* Measuring Local Autonomy in 39 Countries (1990-2014), Regional and Federal Studies, Vol. 26, № 3, 2016, 321-357.

and ability "to regulate and manage a substantial share of public affairs."[103] When the local government have no power to provide or regulate local water supply in the cities or cannot repair school building in the village than it should not be surprising that local people don't know much about local government and don't distinguish it from the central government.

"A ship without the sail" – the failure to have the successful decentralization policy. More than 20 years have passed after the first generation of decentralization reforms, however, the country still has been failing to develop an effective long-term vision of decentralization policy. The analysis of all three generations of decentralization reforms indicates that the government never had the true commitment to achieve the real decentralization of the country. Moreover, the answer to the question: what is the country's decentralization policy? – It is not evident.

During the first generation of decentralization reforms in Georgia the government faced the dilemma to find a balance between two controversial interests: On the one hand the government's mission was legitimization of the power through the democratic system, and foster the process of European integration, on the other hand, there was the high interest to preserve the dominance of the ruling political elite. Thus, the decentralization reform was more seen as a mean to creating democratic façade than the tool of formation the effective governance system at the local level.[104]

After the second generation of decentralization reforms, the president of the National Association of Local Authorities of Georgia wrote the following conclusion: "An analysis of the existing situation shows that implementation of local government reform went out of control and results are contrary to the initial goals. At the starting point, the goal was to establish strong, self-sustainable, and effective local self-government units of a proper scale, but, at the end of the day, Georgia created large municipalities with restricted autonomy, resources, and limited efficiency."[105] Despite the officially declared high readiness and political will the actual result of the second generation reforms was a local government with marginal functions and under the informal political control. This conclusion was also made by different studies and reports. [106]

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103 Article 3.1., *Council of Europe*, Explanatory Report, European Charter of Local Self-Government, European Treaty Series, №122, Strasbourg, 1985, <http://conventions.coe.int/Treaty/EN/Reports/HTML/122.htm>, [15.09.2018].

104 *Kandelaki K., Losaberidze D., Orvelashvili N.,* Local Government in Georgia Developing New Rules in the Old Environment, Developing New Rules in the Old Environment, Local governments in Eastern Europe, in the Caucasus and in Central Asia, Local Government and Public Service Reform Initiative, *Popa V., Munteanu I.* (eds.), Budapest, 2001, 291.

105 *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 184.

106 See *Bolkvadze T., Kandelaki K., Chikovani T., Losaberidze D.* (eds.), Local Self-Government in Georgia 1991-2014, The International Centre for Civic Culture, Tbilisi, 2015; Freedom House, Report Georgia, Annual, Freedom House, 2010, <https://freedomhouse.org/report/nations-transit/2010/georgia>, [20.09. 2018]; Freedom House, Report Georgia, Annual, Freedom House, 2009, <https://freedomhouse.org/report/nations-transit/2009/georgia>, [20.09.2018]; *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 395. *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 184.

There are not much more positive conclusions about the results of the third generation of decentralization reforms too. The third generation reform had a long list of the ambitious goals. Initially decentralization Strategy of Georgia was motivated by more revolutionary changes than the simple modification, however, finally, we observed the moderate and mainly cosmetic changes of the existing system. The result of the reform is the formation of the limited local government. [107]

In addition, all three reforms were characterized by a strong top-down approach. The local community, NGOs, and local government involvement in the process were limited. Therefore, the reforms' ownership had only the central government, to be more precise only the ruling political elite. Thus the failure to achieve broad political consensus frequently led to the situations when the reform was completely restarted by each new government.[108]

Eleventh, the battle of two visions. As one of Georgian scholars, which has been studying decentralization processes in the country from 1991, admitted: we have been observing the battle of two visions in the country. "Supporters of the first vision argue that the establishment of democratic principles is critical for the country's development and that there is no alternative to active civil participation in governance and granting effective rights to citizens. Moreover, this is the only way to successfully finalize the integration with the western democratic world." "The supporters of the second vision hold that the Georgian society is not yet ready to take over the country's management which requires a long-term preparatory measure to be undertaken by the country's elite (under political elites the supporters of this vision obviously imply themselves). As for the western integration, this seems to be a time-consuming process and apparently less important than maintaining authority (for the purpose of the presence of good governance)."[109]

To summarize all above discussions we could add, that although the local self-government's autonomy is already guaranteed by the Constitution of Georgia, the central dependence of the institution is still very strong. This situation is acceptable both for the central and local governments. In the case of local failures, the local political elite can simply readdress political accountability to the central government. Considering above, it is not surprising that local community cannot distinguish between the central

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107 *Cecire H. M.,* Freedom House Report, Georgia, Annual Freedom House, 2016, 8-9, <https://freedomhouse.org/sites/default/files/NiT2016_Georgia.pdf>, [20.09.2018]; *Skorupska A., Zasztowt K.,* Georgia's Local Government Reform: How to Escape from the Soviet Past, Policy Paper, Polish Institute of International Affair, Vol. 4, № 87, 2014; *Transparensy International*, Georgia, Local Integrity Systems Assessment, Transparensy International Georgia, Tbilisi, 2015, <http://www.transparency.ge/sites/default/files/post_attachments/lis_report_2015_eng.pdf>, [20.09.2018]; *Losaberidze D.,* Local Self-Government Reform in Georgia 2013-2014, Local Self-Government in Georgia 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015, 133, 171-178 (in Georgian).

108 See *Melua D.,* Local Government Reform in Georgia, Territorial Consolidation Reforms in Europe, Local Government and Public Service Reform Initiative, *Swianiewicz P.* (ed.), Budapest, 2010, 169, 183. *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries? Local Government Studies, Vol. 36, № 2, 2010, 295. *Losaberidze D.,* Local Self-Government Reform in Georgia 2013-2014, Local Self-Government in Georgia 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015 (in Georgian).

109 Ibid, 167-168.

and the local governments and the responsibility for all sort of local problems fells either to the Prime-Minister or to the Government of Georgia or to the President of the country. This should be warning also for the central ruling political elite itself.

In addition during the political debates mainly the political arguments for decentralization prevail. The economic arguments, which consider the decentralization as an instrument for local development and local public services improvement have a little attention. It is not also fully realized the decentralization potential as the mechanism of conflict prevention. Therefore, besides the political arguments making more accent to the other advantages of decentralization may create additional consensus opportunities between the above mentioned rival positions.

6. Conclusion

The views about the pros and cons of decentralisation are often controversial and even contradictory. The process of decentralization meets a lot of challenges in the developing countries and today there is not exaggerated expectations towards its positive effects. The good practice from the developing countries indicates that decentralization should not be considered as a definite goal but as a tool for achieving certain desirable goals. With this standpoint, decentralization presents a substantial list of the promises, beginning from the development of the civil society and insurance of the vertical balance of power to improved local public services, equal territorial development and conflicts prevention.

Choosing the right policy design is the most complicated issue during the decentralization process. "Decentralization is … a complex process whose dimensions and prerequisites are not just political, legal and administrative, but also economic and cultural… Practicable approaches to decentralization are to some degree country-specific and they heavily depend on time and context."[110]

The presented article indicates that the historical past has the huge impact on the country's future development. Although about 30 years has already passed from the collapse of the Soviet Union, its shadow still is strongly sensible in the country. Hyper-centralized governance model stays as an unresolved challenge for Georgian State and Society.

Like all other public sector reforms, the decentralization reform is never ending process. In 2018 the Government of Georgia announced the start of the new decentralization reform. Thus, considering the past experience and learning from the mistakes can be a decisive factor for future reforms success.

Finally, I want to end the article with the following citation. Once, the World Bank's expert *Andrew Parker* compared successful decentralization reform policy to the cooking of a soufflé and he proposed "soufflé theory" of decentralization. "Like a soufflé that requires just the right combination of milk, eggs, and heat to rise, so a successful program of decentralization will need to include just the right combination of political, fiscal and institutional elements.". Decentralization is a learning process, and the results come through the trial and mistakes.[111]

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[110] *Illner M.,* Issues of the Decentralization Reforms in Former Communist Countries, Informationen zur Raumentwicklung, Vol. 7, 2000, 391.

[111] *Parker N. A.,* Decentralization the Way Forward for Rural Development, Policy Research Working Paper 1475, The World Bank Agriculture and Natural Resources Department Sector Policy and Water Resources Division, 1995, 44.

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Irakli Kakhidze*

The Principle of Subsidiarity and its Implementation Prospects in Georgian Political-Legal Environment

As the saying goes, the change of three words in the legislation turns all the libraries into waste-paper, however, the three new words suffice to fill the libraries again. The principle of subsidiarity belongs to the latter category[1]*. Nowadays the principle of subsidiarity has become a kind of "trendy" idea. It is the constituent conception of the political-legal traditions for a number of European countries*[2] *having gained the recognition and influence even in the USA*[3]*. Moreover, the principle of subsidiarity is reflected in the treaty of the European Union as well.*

As a result of the Constitutional Reform of 2017 the principle was enshrined in the Constitution of Georgia as well. Thus, the principle gained the additional topicality for Georgia. In the present paper there is reviewed the basic concept of the principle of subsidiarity, the conditions for its enforcement and the practice of the Constitutional regulation, in addition, there are evaluated the challenges posed to implementing the principle of subsidiarity and the further prospects of its enforcement in Georgia.

Key Words: *Principle of Subsidiarity, Decentralization, Local Self-Government, Autonomous Republic of Adjara, Division of Power, Separation of Power*

1. Introduction

The modern developing, fast-changing and globalized world introduces the new challenges. The dynamics of globalization – technological progress, international trade and investments, smooth flow of financial capital among countries, market expansion and economics based on the knowledge and innovations – have become a burden on the state power. The list of issues, the resolution of which is the internal problem of a country, is more and more decreasing. Even inside the country, there are several interested public and private parties participating in the decision-making process. The demands of citizens and social structure of the society have significantly changed as well.[4] "The nature of the problems faced by the government has changed. … Nature of the problems as well as the possible solutions are deeply contest-

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1 *Schutze R.,* Subsidiarity after Lisbon: Reinforcing the Safeguards of Federalism?, Cambridge Law Journal, Vol. 68, № 3, 2009, 525.

2 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, №. 55, 1994, 7-8

3 See *Vischer K. R.,* Subsidiarity as a Principle of Governance: Beyond Devolution, Indiana Law Review, Vol. 35, № 103, 2001, 103-142.

4 *Cheema S., Rondinelli D.,* Decentralizaing Governance: Emerging Concept and Practice, Washington, 2007, 4-6.

ed … as the problems have become more difficult, so have the powers available to the central (national) government declined".[5]

The new challenges posed to the state and the economic crisis, the growth of unemployment have outlined the limits of the centralized system of governance. "The large, the enormous, the distant, are no longer synonymous with efficiency."[6] The mentioned tendency is well expressed in the statement of the prominent American sociologist, *Daniel Bell*: "the nation-state is becoming too small for the big problems of life, and too big for the small problems of life."[7] The state is so engaged in the global and major problems that its capability to respond adequately to the different local, regional issues of great variety is restricted.

The crisis of centralized governance led the way in popularizing the idea of a small state that has accounted for the universal tendency of decentralization over the world.[8] In a wide sense, the decentralization is defined as the transfer of the state (central) power to the territorial bodies of state authorities, the partially autonomous state institutions, the regional and local authorities, and/or to the private corporations and non-governmental sector.[9]

"The subsidiarity is primary a de-centralizing principle", in accord with which the process of decision-making and solution to problems occurs closest to the location they have been triggered, thus taking advantage of the quick and accurate managing of the issues.[10] Despite the fact that the principle of subsidiarity has gained in considerable popularity for the last several decades, it is not the "invention" of the modern society. The philosophical origin of the principle of subsidiarity goes back to the antique era. However, it should be noted that the ongoing processes over the world breathed new life into the concept of subsidiarity, which in the Western world became one of the most topical principles and is still disputable even today.

In the vertical structure of the state the local self-government bodies run the closest to the population. Within the scopes of the present paper the focus is made exactly on the issues concerning the enforcement of the principle of subsidiarity during the course of relationships between the state power and local self-government.

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5 *Pollitt C.,* Advanced Introduction to Public Management and Administration, Cheltenham, Northampton, 2016, 46.

6 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 7.

7 *Bell D.,* Previewing Planet Earth in 2013, Washington Post, B3, 1988.

8 *The World Bank*, Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 5.

9 See *Rondinelli D., Nellis J., Cheema S.*, Decentralization in Developing Countries, a Review of Recent Experience, World Bank Staff Working Papers, № 581, Management and Development Series, № 8, 1983, 13; *The World Bank*, Decentralization in Client Countries An Evaluation of World Bank Support, Washington, 2008, 3.

10 *Evans M., Zimmermann A.,* Editors' Conclusion: Future Directions for Subsidiarity, Global Perspectives on Subsidiarity, *Evans M., Zimmermann A*. (eds.), Heidelberger, London, New York, 2014, 221.

In Georgia, the process of decentralization had been progressing with difficulty for about 3 decades of the independence of the country. For that period of time a number of decentralization reforms had been implemented. However, sometimes even the necessity of decentralization itself was open to question. Today the system of self-government is far from perfection and is still in the process of formation. Despite some of the positive changes, generally, it is poorly developed and takes the insignificant role in the governance system of the country.[11]

On October 13, 2017 the Parliament of Georgia adopted the Constitutional Law of Georgia on "Amending the Constitution of Georgia" (hereinafter*, Constitutional Amendments)*. By the amendments, in fact, the new Constitution was confirmed. The major part of amendments will come into effect immediately after taking the oath by the president to be elected in the next Presidential Elections of Georgia in 2018. The amendments included constitutional norms regulating local self-government issues too. There should be highlighted the 4th section of Article 7 of the current Constitution envisaged by the Constitutional Amendments,[12] according to which the new Constitutional principle of separating the state from local self-government powers – the principle of subsidiarity- is being established in Georgia.

The introduction of the principle of subsidiarity in the Constitution and the new initiative in regard to the strategy of decentralization to be developed in 2018 as announced by the Government of Georgia, give grounds for expectation of the additional measures to be taken with the aim of implementing the principle of subsidiarity. The present paper is the recall to the mentioned tendency. Our goal is to review the subsidiarity concept as well as the conditions for its application and then analyze the prospects of implementing the principle in Georgian political-legal environment.

The second part of the paper starts with the analysis of the principle of subsidiarity. The third and fourth parts refer to the challenges posed to the implementation of the principle and the issues of its application. The fifth part reviews the examples of the Constitutional regulations of the principle. The fifth part evaluates the possibilities for implementation of the principle of subsidiarity in the political-legal environment of Georgia and the final part of the paper presents our conclusions.

2. The concept of subsidiarity

The term – "subsidiarity" is premised on the term "subsidia", which, in its turn, is derived from the Latin verb – *subsidium*. This word in Latin means aid, assistance. The term itself had the military significance in the past. In ancient Rome this word denoted the replacement of military units, which set to battle only upon necessity.[13]

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11 See *The International Center of the Civil Culture*, The local self-government in Georgia, 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K*. (eds.), Tbilisi, 2015 (in Georgian); *Ladner A., Keuffer K., Baldersheim H.,* Measuring Local Autonomy in 39 Countries (1990-2014), Regional and Federal Studies, Vol. 26, № 3, 2016, 321-357.

12 Constitutional Law of Georgia on Amendments to the Constitution of Georgia, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

13 *Khubua G.,* The Federalism as the Normative Principle and the Political Order, 2000, 110 (in Georgian).

As it was mentioned, the genesis of the philosophical basis of the principle of subsidiarity goes back to the antique era. Particularly, the principle conceptually represented the part of the Greek philosophy. The aspiration of the principle of subsidiarity is reflected in "Politics" (the art of governing the free human being) – the work by *Aristotle*. *Aristotle* points out that the main goal of a state is to provide the unity, however, the exceeded unanimity is devastating. The state exists in variety. It consists of free people, families, yards, villages, communities, tribes. The mentioned units are diverse each performing its own function, however, for Aristotle the perfect formation, is only the state, while the other parts are only its constituent elements, the independent existence of which is impossible.[14]

Aristotle's viewpoints were further developed by *Thomas Aquinas* (1225 -1274). He denoted that in the state there existed the different groups (religious, trade, political, territorial, vocational, etc.) fulfilling the independent public and private functions. In contrast to *Aristotle*, *Thomas Aquinas* thought, that the existence of each group mentioned above is necessary, as they represent the essential means of self-realization for the human being. And the state can intervene in their affairs only in specific cases.[15]

In the 20th century a kind of revival of the concept of subsidiarity is connected with the encyclical published by the Pop of Rome *Pius XI* in 1931, which comprehensively formulated the concept of subsidiarity. According to the encyclical, "It is indeed true, as history clearly proves, that owing to the change in social conditions, much that was formerly done by small bodies can nowadays be accomplished only by large corporations. None timeless, just as it is wrong to withdraw from time individual and 'commit to the community at large what private enterprise and industry can accomplish, so, too, it is an injustice, a grave evil, and a disturbance of right order for a larger and higher organisation to arrogate to itself functions which can be performed efficiently by smaller and lower bodies. … Of its very nature the true aim of all social activity should be to help individual members of the social body, but never to destroy or absorb them. The State should leave to these smaller groups the settlement of business of minor importance; it will thus carry out with greater freedom, power, and success the tasks belonging to it, because it alone can effectively accomplish these, …as circumstances suggest or necessity demands."[16]

To summarize, subsidiarity is a political philosophy referring to the principles of managing the social affairs. And the central idea of subsidiarity principle is the free individual. The principle of subsidiarity pays attention to the significance of the various social groups (family, community, local societies, vocational union, etc.) in the social life, as far as the mentioned groups are deemed to be the essential conditions for the development of a free individual. The state assumes a kind of consolidating function in this diverse social structure. The intervention of the state in the social life is justified only in case the members of the society or their groups are not capable to meet their own demands. To sum up, the philo-

14 *Aristotle,* Politics, *Jowett B.* (trans.), Kitchener, 1999, 23-24.

15 *Aroney N.,* Subsidiarity in the Writings of Aristotle and Aquinas, Global Perspectives on Subsidiarity, *Evans M., Zimmermann A*. (eds.), Heidelberger, London, New York, 2014, 24-25.

16 *Pius XI,* Quadragesimo Anno: Reconstructing the Social Order and Perfecting it Conformably to the Precepts of the Gospel in Commemoration of the Fortieth Anniversary of the Encyclical Rerum Novarum, Australian Catholic Truth Society, 1931, № 19, 21.

sophical basis of subsidiarity, first of all, is the freedom and free individual that makes it the democratic principle.[17]

The enforcement of the concept of subsidiarity in the state is possible at the horizontal and vertical levels, accordingly, there are distinguished the territorial and functional versions of the subsidiarity concept. The horizontal (functional) subsidiarity highlights the importance of the individual, various social groups and unions. While the vertical (territorial) subsidiarity emphasizes on the territorial units of the state.

The territorial conception at the official level first appeared in the Basic Law of Germany of 1949 and became the essential part of German Federalism, before long it became the dominated concept in Europe. In the process of the division of power among the different territorial levels of government the principle of subsidiarity acts as a presumption in favour of the lower territorial government, whereas formally, the obligation of proving the opposite is imposed to the higher territorial government.[18] In the present paper mainly the territorial concept of subsidiarity is highlighted.

Interestingly, from then onward, the concept of subsidiarity has encompassed the controversial elements which are often called the negative and positive elements of subsidiarity. The negative (proscriptive) subsidiarity concept implies the protection of lower units from the interference of the higher authorities. Whereas the positive (prescriptive) subsidiarity admits the possibility of the intervention of higher authorities into the freedom of lower units. However, as mentioned above, the right of higher authorities to intervention is conditioned by the incapability of the lower units.[19] "Subsidiarity is not simply a limit to intervention by a higher authority …, it is also an obligation for this authority to act", when the lower unites need the aid.[20] The coexistence of the above mentioned two elements contributes to the perfect self–realization of the social groups, unions and individuals. However, this coexistence offers the possibility of making quite a wide interpretation too. In particular, the logical question arises: in what case and to what extent do the higher authorities have the right to intervene in the freedom of lower units?

The ample opportunities for the definition of the concept of subsidiarity significantly simplify the integration of the principle with political-legal space of the countries having various traditions and interests.[21] As it seems, its flexible nature deserves the general approval. Some of the researchers compare it

17 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 10-11.

18 *Follesdal A.,* Subsidiarity, The Journal of Political Philosophy, Vol. 6, № 2, 1998, 195-196; *Endo K.,* The Principle of Subsidiarity: From Johannes Althusius to Jacques Delors, Hokkaido Law Review, № XLIV/6, 1994, 568, 640-39.

19 Ibid.

20 *Delors J.,* The Principle of Subsidiarity: Contribution to the Debate, Subsidiarity: The Challenge of Change: Proceedings of the Jacques Delors Colloquium Subsidiarity – Guiding Principle for Future EC Policy Responsibility?, European Institute of Public Administration, Maastricht, 1991, 9, 17.

21 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 10-11.

with the old Swiss army knife, "flexible enough to apply to most policy issues, pointed enough to command caution, dull enough to never do serious harm, and always in its pocket."[22]

While analyzing the principle of subsidiarity the professor of Columbia University George Bermann distinguishes its five main values: the first is self-determination and accountability. The individuals get more opportunities to influence their own life when the rules are set at the territorial level, where they have more possibilities for their participation. The opportunity for participation implies the compatibility of the local laws and policy with the demands and interests of the local population. It is easier for the society to express the dissatisfaction when the government is closer to the population. The second, political liberty. The subsidiarity hinders the exceeded concentration of power and creates the better possibilities of gaining a balance between the diverse interests. The third, flexibility. The subsidiarity allows the society to take into account the uniqueness of the local – physical, economic, social, moral, cultural conditions and promptly respond to the changes. Accordingly, the subsidiarity allows to enjoy the democracy as well as the efficient governance at the same time. The fourth, preservation of identity. The local society can develop the local social and cultural identity and take the local peculiarities into consideration. The fifth, diversity. The subsidiarity is important to ensure the variety of politics. It allows conducting a number of experiments within the certain community. Thus the community turns into a kind of laboratory allowing to create and develop the best practice. Hence, the principle is the important policy tool for developing the efficient management practice as well.[23]

All in all, the subsidiarity, first of all, means more autonomy (self-government). The implementation of the principle allows to reach the reasonable balance among the interests of the individuals, social groups, unions and the state. In the process the state assumes the responsibility for the security, social unity, general regulation and coordination. However, the dual nature of the principle provides the opportunity to conduct the complex manoeuvers. In the process of vertical division of powers on the one hand, the principle is deemed to be the argument for transferring the powers to the lower level, however, on the other hand, it presumes the opportunity of centralization too, particularly, when the lower level is not capable or the incapability of exercising the power on lower level is evident.[24]

To conclude, it is worth noting that "subsidiarity is primarily a de-centralizing principle, which aims to empower the individual by ensuring that decisions are made, and problems are resolved, closest to where they arise. In turn, decision-making and action taken by those directly affected allows for problems to be resolved more quickly, and more accurately than if a higher-level decision maker who is distanced from the problem, were to become involved."[25]

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22 *Martin A.,* The Principle of Subsidiarity and Institutional Predispositions: Do the European Parliament, the German Bundestag, and the Bavarian Landtag Define Subsidiarity Differently?, CAP Working-Paper, München, 2010, 3.

23 *Bermann A. G.,* Taking Subsidiarity Seriously: Federalism in the European Community and the United States, Columbia Law Review, Vol. 94, № 2, 1994, 339-44.

24 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 11.

25 *Evans M., Zimmermann A.,* Editors' Conclusion: Future Directions for Subsidiarity, Global Perspectives on Subsidiarity, *Evans M., Zimmermann A*. (eds.), Heidelberger, London, New York, 2014, 221-223.

3. The Challenges of the Principle of Subsidiarity

The principle of subsidiarity cannot be reviewed isolated in the system of public governance. It is in constant competition with other important public interests and principles and has to be balanced therewith. The experts of the Congress of Local and Regional Governments (hereinafter referred as Congress) distinguish four principles, over which the principle of subsidiarity must reach a kind of "compromise", they are as follows: the principles of unity of actions, effectiveness, the unity of application and solidarity.[26]

The unity of action implies to the unification and concentration of the effort within the state. The modern challenges require the mobilization of energy at every level and the economic management of resources from the states.[27] However, the effective management and solution to problems is not always possible to be achieved by the centralization of power and unified action. Today the central government is overloaded with the global and bigger issues that it is not able to make the adequate response to various and diverse local problems. Under such conditions, in some case, the most proper solution is to rely on the principle of subsidiarity.

The principle of subsidiarity is often opposed by the principles of effectiveness and economy. The effectiveness can be perceived differently, accordingly, its exact definition is a complicated task. In the theory of management and finances there are distinguished two types of "effectiveness" (effectiveness and efficiency), the Georgian equivalents of which do not exist. That is why, conditionally, we will use the terms: effective results (effectiveness) and efficient expenses (efficiency). The effectiveness implies, to what extent the goal has been achieved in the relevant policy area (e.g. social security, healthcare, transport, etc.) The achievement of goals is regarded as the positive changes of the existing situation and environment. (e.g. reducing the rate of unemployment, decreasing of illnesses, diminishing of traffic congestions, etc.) The efficiency implies the number of wasted resources (finances, materials, human resources, etc.) and the number of produced "objects" resulted therefrom (e.g. how many km of road were constructed, how many reports were written, how many persons were arrested, how many persons were trained, etc.). In this case, the greater importance is attached to the proportion between the amount of the wasted resources (finances, time, human resources, etc.) and the amount of produced objects (the amount implies: size, weight, volume etc.). Whereas the economy means the resources saving.[28]

In the process of evaluating the distribution of functions the economic criteria are frequently applied: firstly, the criteria of proximity. The closeness of the public government with the problem offers

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26 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 24-29.

27 Ibid, 25.

28 *Endo K.,* The Principle of Subsidiarity: From Johannes Althusius to Jacques Delors, Hokkaido Law Review, № XLIV/6, 1994, 636-37; *Rossell C.,* Using Multiple Criteria to Evaluate Public Policies, The Case of School Desegregation, American Politics Quarterly, Vol. 21, № 2, 1993, 164; *Pollitt C., Bouckaert G.,* Public Management Reform: A Comparative Analysis: New Public Management, Governance and the Neo-Weberian State, 3rd ed., Oxford, 2011, 15, 135.

the flexibility to become better aware of the situation and solve the problems by adapting to the local conditions thereto; the second one is the economy of the scale that implies the reduction in expenditure along with the increase in the amount of production; and the third criteria is the effect of access. According to the mentioned criteria, while dividing the powers effectively, it should be considered the extent (the volume) of the direct benefit of the local population from the relevant public good produced by the local community (local government). For example: the consumer of the outdoor lighting and fire protection service is mainly the population of the specific territorial unit in contrast to the international highway which is equally used by the whole population of the country.[29]

The last two criteria of effectiveness logically lead to the centralization and the merger of territorial units, which are opposite categories with the principle of subsidiarity. However, the concept of subsidiarity does not contradict to the concept of effectiveness. The principle of subsidiarity introduces other criteria along with the traditional financial and economic criteria for evaluating the effectiveness. For example, the criteria such as the welfare of the population and the respect for the historical-cultural peculiarities.[30] For instance, the construction of one big House of Justice (state agency which provides some public services, for example, registration of the property, issuing identity cards and etc.) in the region may be the most efficient and economical, however, in this case the population living in the peripheries has to go a very long distance to be provided with the service, whereas the decision on opening the Houses of Justice in the mountainous settlements may not be financially justified but it will improve the welfare of the local population.

Based on this, in the social and political issues the economic-financial criteria may be only the relative concept. The common welfare is not always connected with the financial and economic categories. The subsidiarity principle takes notice of not only the quantitative but qualitative factors as well. At the same time, the economy of scale has its limits and sometimes contributes to the increase of bureaucratic procedures.[31] Accordingly, bigger does not always mean more effective.[32]

One more principle contending with the principle of subsidiarity is the principle of the unity of application. The central power is characterized by the tendency of unification, which is the condition for the existence and development of the unified state. The provision of unification, in a fairly general sense of this word social, economic, cultural, political, legal and other is the important condition for the equal social-economic development of the country. At the same time, ensuring the equal living standards for the whole population represents the constitutional obligation of the country.[33]

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29 *David K.,* Fiscal Tiers (Routledge Revivals): The Economics of Multi-Level Government, 1st ed., New York, 2016, 17-18.

30 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 26.

31 Ibid, 26-27.

32 See *Swianiewicz P., Łukomska J.,* Is Small Beautiful? The Quasi-experimental Analysis of the Impact of Territorial Fragmentation on Costs in Polish Local Governments, Urban Affairs Review, № 55(3), 2017, 1-24.

33 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 27-28.

At first glance, the principle of unification is directly contradictory to subsidiarity, however, the unification can be most effectively achieved on the basis of the principle of subsidiarity. The subsidiarity offers the opportunity for adaptation to the local conditions and demands, which is far more effective means of creating the equal living conditions over the territory of the country. "Subsidiarity can reduce the possible rigidity and ill adaptedness that unity of application can involve."[34] The subsidiarity encourages the individualism and allows free rein to initiative and innovations. Sometimes under the conditions of the local initiative even the original ways of solving the problems are explored, that increases the prospect of the generalization and further development.[35]

The principle of subsidiarity and solidarity are in conflict as well. During the course of distributing the wealth among the rich and poor, one of the complicated challenges for the modern state is the assurance of fair balance. From this point of view, the centralization of all the resources and their further distribution seems to be an appealing way out without any alternative.[36] However, the concentration of comprehensive knowledge of the problems pertaining to each settlement and territory at the central level is practically impossible. Accordingly, the logical question arises: how fair is the centre unless having the relevant information concerning the local conditions and demands?

The subsidiarity does not actually exclude the solidarity. The concept of subsidiarity implies the positive alongside negative obligations of the state power as well, which is expressed in the duty of providing the subordinated units with the aid. This element approximates the subsidiarity to the principle of solidarity and makes the outlines for coexistence therewith. The coexistence of the principles of subsidiarity and solidarity necessitates the need to preserve the reasonable balance between the municipalities possessing the different capabilities (e.g. urban or high mountainous or rural municipalities) and obliges the state to distribute the resources among the municipalities equally. At the same time, "subsidiarity introduces the idea that equalization or aid have no meaning unless they lead to the equal capacity for action and are accompanied by acceptance of responsibility."[37] Correspondingly, based on the autonomous management of resources and the relevant responsibility therefor the concept of subsidiarity itself implies the consent of the other party to accept the aid as well.[38]

4. The "Standard" for Enforcement of the Principle of Subsidiarity

The implementation of the principle of subsidiarity requests the establishment of the standard for its enforcement, which means the stipulation of the criteria and rules according to which the principle will be enforced. In this term, the criteria for the division (distribution) of power established by the dif-

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34 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 28.

35 Ibid, 27-28.

36 Ibid, 28-29.

37 Ibid, 28.

38 Ibid.

ferent international legal regimes in Europe are of interest for Georgia. In this respect the greatest importance is attached to the European Charter on Local Self-Government (hereinafter referred as Charter) which was ratified by the country in 2004.

The principle of subsidiarity is not directly enshrined in the Charter, however, its essential aspiration is premised on the subsidiarity conception.[39] In this respect, the 3rd section of Article 4 of the Charter is worth noting, pursuant to which "public responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation of responsibility to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy."[40]

In accord with the explanatory report of the Charter, it is impossible to determine the precise and comprehensive list of functions of "local importance." The great part of functions bears the local as well as the statewide significance. They vary according to the states as well as change in time and are differently distributed among the governments of various territorial levels. "To limit local authorities to matters which do not have wider implications would risk relegating them to a marginal role."[41] That is why, pursuant to the Charter the local self-government must assume the responsibility for the substantial share of public affairs.[42]

Four criteria of the division of powers are stipulated by the 3rd section of article 4 the Charter. The first two are more or less "objective" categories, such as: the "nature" and "volume" of the function. For example, the solution to the issues such as the administration of defense and foreign affairs of the country, the construction of pipeline and international highways do not represent the issues of the local importance due to their nature and volume and they cannot be managed by municipality, in contrast to, for instance, the functions of municipal waste management and arranging the resting places. The rest of two criteria "effectiveness" and "economy" are the normative (evaluative) categories, which we have discussed above.

The Charter heavily focuses on the positive obligations of the state, which is one of the elements of the subsidiarity conception. In particular, "Local self-government denotes the right and the ability of local authorities… to regulate and manage"[43] The creation of the real "ability" of regulation and management is the direct obligation of the state power. In this respect, the three groups of norms of the Charter can be conventionally distinguished. The first group requires from the state the provision of the or-

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39 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 13.

40 Council of Europe, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://www.coe.int/t/dgap/localdemocracy/WCD/CS_Conventions_en.asp#>, [15.04.2018].

41 Council of Europe, Explanatory Report, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://conventions.coe.int/Treaty/EN/Reports/HTML/122.htm>, [15.04.2018].

42 Article 3 (1), Council of Europe, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985,<http://www.coe.int/t/dgap/localdemocracy/WCD/CS_Conventions_en.asp#>, [15.04.2018].

43 Ibid.

ganizational and personnel autonomy of the local self-government (article 6 and article 7). The second group, denotes to the necessity of ensuring the financial autonomy (article 9, sections 1-5 and section 7), and the third group focuses its attention on the mechanisms of the influence of the local self-government over the central power (article 6, section 6 and article 9, section 6).[44]

The principle of subsidiarity is prescribed by the Treaty of Lisbon as well.[45] The attitude of the European Union related to the subsidiarity principle is different from the concept enshrined in the Charter. The goal of the Charter is to protect and popularize the concept of the local self- governance. Whereas the European Union aims at achieving of the prudent political balance between the interests of the Union and the member states.[46] Despite the diverse agenda, even in the Treaty of Lisbon it is possible to identify the interesting guidance criteria for the division of power in compliance with the principles of subsidiarity.

The 5.1st and 5.3rd sections of the Treaty of Lisbon envisages the following frame approach of the distribution of the powers among the Union and its members: "The use of Union competences is governed by the principles of subsidiarity and proportionality. Under the principle of subsidiarity, in areas which do not fall within its exclusive competence,[47] the Union shall act only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level".[48]

The Treaty of Lisbon offers several criteria for the division of powers: firstly, the Union is entitled to act if the lower unites cannot sufficiently exercise their authorities (negative test); Secondly, the Union is authorized in case it can prove that by reason of the scale or effects of the proposed action the set goals be better achieved at the Union level (positive test, so-called the test of additional value)[49] and thirdly, if the first and the second criteria are in place, the union is obliged to imply with the proportionality principle and exercise the power only to the extent that is necessary to achieve the better result (proportionality test).[50]

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44 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 15-16.

45 Treaty of Lisbon was signed by 27 countries of EU, in Portugal, Lisbon on December 13, 2007. The Treaty of Lisbon moves amendment to the Treaty of European Union and the Treaty Establishing the European Union, which was renamed and called Treaty on the Functioning of European Union.

46 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 14.

47 The term – exclusive competence implies to the European Union.

48 *Bonde J. P.* (ed.), Consolidated Reader-Friendly Edition of the Treaty on European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU) as amended by the Treaty of Lisbon (2007), Foundation of the EU Democracy, 3rd ed., Notat Grafisk, 2009, 16-17.

49 The phrase "by the reason of the scale or effects" means that achieving the set goals demands impact on large area (territory) or the result of the action could have a large scale effect. See *Endo K.,* The Principle of Subsidiarity: From Johannes Althusius to Jacques Delors, Hokkaido Law Review, № XLIV/6, 1994, 635.

50 *Kiiver P.,* The Early Warning System for the Principle of Subsidiarity: Constitutional Theory and Empirical Reality (Routledge Research in EU Law), 1st ed., New York, 2012, 23, 70-71.

Despite the difference there can be found the common signs related to the principle of subsidiarity both in the Charter and Treaty of Lisbon. In both of the cases in the process of the division of the powers the subsidiarity principle is the presumption in favour of the lower territorial governments, while the obligation to confirm the opposite is imposed to the higher authority. The guidance criteria and principles of the division of powers may be chosen in accordance with the generalizing the approaches reviewed above. In particular, upon the division of powers the following criteria and principles should be considered:

- The presumption of the granting the power to the lower territorial units;
- The criteria of nature and volume of power;
- The criteria of economy and effectiveness;
- The criteria of the scale and effect of the objective;
- The positive obligation of aid;
- The principle of proportionality.

At the same time, the enforcement of the subsidiarity principle is not completed only by determining the principles and criteria for the division of powers. In the process of division of powers the compliance with certain rules is not less important.

Upon the recommendation of the experts of the Congress in the process of division of the powers introduction of shared authorities should be avoided as possible, it means excluding the possibility of overlapping responsibilities of the various territorial units.[51] In accord with the Charter, the powers transferred to the local self-government shall be full and exclusive.[52] The mentioned position is straightforward and logical, the autonomy of the local self-government "can be preserved and collaboration is fruitful if there is a clear rule."[53] That is why, the authorities must be stipulated as precisely and comprehensively as possible.

Here it should be determined that the above mentioned approach does not hinder the existence of the principle of general competence (universal competence), according to which "Local authorities shall, within the limits of the law, have full discretion to exercise their initiative with regard to any matter which is not excluded from their competence nor assigned to any other authority."[54] Hence, upon the division of the powers, the maximally clear and comprehensive definition of the powers by the Constitu-

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51 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 30.

52 Article 4 (4), Council of Europe, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://www.coe.int/t/dgap/localdemocracy/WCD/CS_Conventions_en.asp#>, [15.04.2018].

53 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 30.

54 Article 4 (2), Council of Europe, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://www.coe.int/t/dgap/localdemocracy/WCD/CS_Conventions_en.asp#>, [15.04.2018].

tion or Law must be the major and guiding principle, whereas the principle of the general competences is deemed as the additional, "auxiliary" means.

The transfer of powers to the local self-government by the higher (state, autonomous republic, federation, etc.) authorities can be made in the form of the own as well as delegated authority. Correspondingly, the question arises: which of the authorities must be more emphasized? The own powers of the local self-government are the powers granted by the Constitution or Law to the local self-government, which is exercised independently or under its own responsibility. Whereas the delegated powers represent the authority imposed to the higher territorial government, which is exercised by the local self-government under the extensive supervision and in the name of the relevant government.[55]

The well-defined position related to the mentioned issue is enshrined in the Charter which emphasizes on the own powers, in particular, the exercise of power by local government independently and under its own responsibility. Otherwise the danger will be posed to the local self-government to turn from the autonomous unit into the local agency directly subordinated to the highest governmental body. Hence, pursuant to the Charter the local self-government must have the freedom of action even in case of execution of the delegating powers thereto.[56]

The principle of subsidiarity is the method of action of the public authority emphasizing the exercise of power at the lower territorial level. However, it is debatable, which territorial level/levels can be the lower territorial levels of the public governance. The lower territorial level may be a settlement (village, town) or/and a certain community of several settlements (district, department, county, etc.) or/and larger territorial level – region. Traditionally, the discretion of solving the mentioned issue is within the remits of the state power.

The systems where the self-government units are established at several territorial levels allow using the subsidiarity principle in more flexible manner. In the mentioned case the central government can effectively manipulate the diverse criteria reviewed above, that is attested by the territorial reforms having been implemented by the states for the last 30 years, which was followed by the creation of several-level systems of public governance. There is displayed high tendency for forming the regional level too.[57] In this respect, the countries of Eastern Europe are distinguished by the implemented reforms too. For example, two levels of local self-government have been established in Czech Republic, Slovenia, Serbia, Hungary, Rumania, Croatia and Greece, and in Poland – three levels.

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55 Study of the European Committee on Local and Regional Democracy (CDLR) with the collaboration of *Marcau G.,* Local Authorities Competences in Europe, 2007, 40-41, <https://rm.coe.int/1680746fbb >, [13.04.2018].

56 Article 4 (5), Council of Europe, European Charter of Local Self-Government, European Treaty Series, № 122, Strasbourg, 15/10/1985, <http://www.coe.int/t/dgap/localdemocracy/WCD/CS_Conventions_en.asp#>, [15.04.2018].

57 See Study of the European Committee on Local and Regional Democracy (CDLR) with the collaboration of *Marcau G.,* Regionalization and its Effects on Local Self-Government, Local and Regional Authorities in Europe, № 64, 1998.

5. The Principle of Subsidiarity in the Constitutions of Foreign Countries

The principle of subsidiarity is rarely enshrined in the legislative acts of the European States, especially in the Constitutions. However, the norms completely or partially encompassing the subsidiarity concept is often encountered in the Constitutions.

In the Basic law of Germany the subsidiarity concept is referred to only in terms of the relationship with the European Union. However, the subsidiarity conception is mentioned in various articles of the Basic Law. Among them Article 30 of the Basic Law of Germany is noteworthy, pursuant to which "except as otherwise provided or permitted by this Basic Law, the exercise of state powers and the discharge of state functions is a matter for the *Länder,*" It is worth noting that Article 30 of the Constitution is clearly defined by the Constitutional Court of Germany. Particularly, the Constitutional Court denotes that upon the division of powers the following sequence should be followed: municipality, land and federation.[58]

It is also interesting, how the Constitutional Court defines the concept of "local affairs". According to its definition, "local affairs are those needs and interests that have their roots in the local community and that have a specific link to the local community."[59]

The first section of Article 70 of the Basic Law is also premised on the subsidiarity concept, in compliance with which, "The Länder shall have the right to legislate insofar as this Basic Law does not confer legislative power on the Federation", however, the above mentioned general authority of the land is therein limited to the conception of exclusive and competitive (equal, parallel) authority by the Basic Law. In the sphere of competitive authorities the Federation is entitled to pass the legislative act in case it is impossible to exercise the power efficiently by the regulations based on the land legislation, and/or the interests of the land or the whole state are jeopardized (the definition of the Constitutional court). In case of the existence of the above-mentioned conditions, the Federation exercises the relevant power only to the extent that is necessary to create the equal living conditions over the territory of the country or/and to ensure the legal and economic unity.[60] It is worth noting that this approach applies to the above discussed criteria to a certain extent as well.

The principle of subsidiarity is not directly enshrined in the Constitution of Austria either. However, in the Constitution there is the article covering the idea of subsidiarity. Pursuant to Article 118 of the Constitution of Austria all the issues applying exclusively or/and generally to the local society belong to the own power of the municipality and they can be exercised within its territory.[61]

In the constitution of France the principle of subsidiarity is prescribed as follows: "Territorial communities[62] may take decisions in all matters arising under powers that can be best exercised at their

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58 *Bröhmer J.,* Subsidiarity and the German Constitution, Global Perspectives on Subsidiarity, *Evans M., Zimmermann A.* (eds.), Heidelberger, London, New York, 2014, 144-145.

59 Ibid.

60 Ibid, 133-137.

61 *Eberdhard H.,* Austria – Municipalities as the "Third Tier" of Austrian Federalism, Local Government in Euorope, The Fourth Level in the EU Multilayered System of Governance, *Panara C., Varney M.* (eds.), London, New York, 2013, 13.

62 In France the term Territorial Community means the self-governing unit.

level."[63] (Article 72). In accord with the Constitution of Greece, "for the administration of local affairs, there is a presumption of competence in favour of local government agencies." (The 1st section, Article 102).[64] And in compliance with the Constitution of Romania the public governance and the delivery of public services is conducted on the basis of the principles of decentralization, local autonomy and deconcentration.[65]

The Constitution of Italy holds in the rare cases, when the principle of subsidiarity is directly recognized by the Constitution, pursuant to which, "Administrative functions are attributed to the Municipalities, unless they are attributed to the provinces, metropolitan cities and regions or to the State, pursuant to the principles of subsidiarity, differentiation and proportionality, to ensure their uniform implementation…"[66] The subsidiarity is the Constitutional principle in Portugal as well. Portugal is a unitary state which is organized and functioning on the basis of subsidiarity, democratic and decentralization principles of the state governance under the Constitution of Portugal.[67]

In the Constitution of Poland the subsidiarity principle is enshrined in the preamble of the Constitution as well. The principle is contextually stipulated by Article 163 according to which the state functions are performed by the local government unless otherwise defined as the functions of other bodies by the Constitution and Law. The public objectives, the goal of which is to meet the demands of the local society, shall be realized by the local government as its direct obligation.[68]

6. The Challenges of Implementation of the Principle of Subsidiarity in Georgia

In the paper the evaluation of the prospects of implementing the principle of subsidiarity in Georgia is presented on the basis of the analysis of five major challenges. From our point of view, overcoming the mentioned challenges adequately has the decisive importance for the effective enforcement of the principle of subsidiarity. Particularly, they are: mobilizing the political will; providing the efficient separation and division (distribution) of powers; strengthening the financial autonomy of the local self-

63 *Couzigou T.,* France – Territorial Decentralisation in France: Towards Autonomy and Democracy, Local Government in Euorope, The Fourth Level in the EU Multilayered System of Governance, *Panara C., Varney M.* (eds.), Routledge, London, New York, 2013, 82..

64 Article 102 (1), Constitution of Greece, 1975, <http://www.hellenicparliament.gr/en/Vouli-ton-Ellinon/To-Politevma/Syntagma/>, [15.04.2018].

65 Article 120 (1), Constitution of Romania, 21/11/1991, <http://www.cdep.ro/pls/dic/site.page?id=371>, [15.04.2018].

66 *Villamena S.,* Organization and Responsibilities of the Local Authorities in Italy Between Unity and Autonomy, Local Government in Euorope, The Fourth Level in the EU Multilayered System of Governance *Panara C., Varney M.* (eds.), London, New York, 2013, 196-97.

67 Article 6, Constitution of the Portuguese Republic, 1976, <http://www.en.parlamento.pt/Legislation/CRP/Constitution7th.pdf>, [15.04.2018].

68 Articles 163, 166, Constitution of the Republic of Poland, 02/04/1997, <http://www.sejm.gov.pl/prawo/-konst/angielski/kon1.htm>, [15.04.2018].

government; carrying out the territorial reforms in compliance with the local conditions and demands and at last, creating the system for the development of appropriate human resources at the local level.

6.1. The Political Will

The principle of subsidiarity is the principle of decentralization, accordingly, its implementation is related to the decentralization reform. The enforcement of the principle requires the substantial changes of methods of public administration to be made by the public authorities. Therefore, the existence of the political will is attached the decisive importance for the implementation of the principle.

As the past period has shown the reform of decentralization is frequently perceived to have a single, narrow "field" remits and its scales are not adequately realized. After perceiving its real scale it is difficult to mobilize the political will for taking the thorough measures. That is why, despite several attempts of implementing the reform of decentralization, the process is progressed too slowly and the advancements are frequently followed by the regress. Consequently, the positive results of decentralization are less tangible in the country.[69]

The decentralization reform is the complex issue. It implies not only changing of the vertical structure of the state but the significant transformation of the whole system of public governance. The decentralization encompasses almost all the spheres and fields of state policy (economics, environmental protection, social security, culture, sports, health care, agriculture, finances, elections, etc.). Along with the legal and institutional changes the decentralization requires the transformation of the behaviour of subjects involved in the process of public administration. This is the prolonged and complicated process. In particular, the state's politicians should conform to weakening their political control over the local level, the authorities of the state power and the local self-government should become aware of the necessity of their mutual cooperation, in addition, the citizens should assume more responsibility to solve the local problems and exercise the effective civil control over the local self-government.

The decentralization is like the learning process, when the outcome is a result of the prolonged and determined work, however, the long duration of the process should not account for postponing its start point for decades. The decentralization requires from the government to apply the complex approaches and pursue the consistent policy. In the process the principle of subsidiarity "In the form of a "constitutional leitmotiv"… could at least be regarded as a permanent "anti-upward" clause... Subsidiarity could be more than just a questioning of the principle of unity of action; it could serve as a basis for debate."[70]

In this regard, the initiative concerning the long-term strategy of decentralization to be developed is definitely a great step forward declared by the Government of Georgia in 2018, however, if taking into consideration the unenviable experience of the previous years, the mentioned initiative should be necessarily followed by the specific and duly measures as well.

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69 See *The International Centre for Civic Culture*, Local Self-Government in Georgia, 1991-2014, *Losaberidze D., Bolkvadze T., Kandelaki K., Chikovani T.* (eds.), Tbilisi, 2015, (in Georgian).

70 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 25.

6.2. The Separation and Division of Powers

6.2.1. The Principle of Subsidiarity in the Constitution of Georgia

Before reviewing the issue related to the separation and division of powers among the public authorities it is necessary to define what the term itself – "power" implies. The power is the right to act which is legally conferred to the public authorities or persons and has a certain goal. The power, is expressed in combination with the functions, rights and duties, for example: the right of the governmental authorities to enact the legislative act, to purchase a certain goods, to create the legal entities, etc. is always linked to the specific function, e.g. the waste management, regulating the issues concerning domestic animals, providing water supply or pre-school education. The functions, in their turn, are the issues pertaining to which the rights and duties of public authorities are applied. Accordingly, the powers without any function have no sense, whereas the functions cannot be analyzed without considering the powers and duties.[71]

The term – power is conceptually perceived together with the relevant functions in the Constitution of Georgia. Hereinafter, in the text of the paper, the terms – power and function are used in compliance with the above mentioned definitions.

After the Constitutional Reform of 2017 the Constitution of Georgia joined the group of the rare types of constitutions where the principle of subsidiarity is directly enshrined. According to the Constitutional Amendment and envisaged by the 4th section of Article 7 of the Constitution of Georgia: "The citizens of Georgia shall regulate the affairs of local importance through local self-government in accordance with the legislation of Georgia. The separation of powers between the state authorities and self-governing units is based on the principle of subsidiarity. The State ensures the compliance of financial resources of self-governing units with its powers defined by Organic Law."[72]

Despite the fact that it was the first time the principle of subsidiarity had been enshrined in the Constitution of Georgia, the legislative norm premised on the concept of subsidiarity is prescribed in the current version of the Constitution of Georgia as well. In particular, pursuant to the 3rd section of article 101^2, "A self-governing unit shall have the right to take any decision on its own initiative, provided that the decision does not fall within the competence of any other government agency or is nor prohibited by law."[73] Before determining the responsible authority for the function, its automatic imposition to the local self-government completely corresponds to the idea of subsidiarity.

Pursuant to the 4th section of Article 7 enshrined in the Constitutional Amendment the following brief comment should be made: the term – "separation of powers" does not completely depict the concept of subsidiarity. The essence of the principle of subsidiarity is not the separation of powers (i.e. the prevention of the duplication of functions), but it implies the transferring, division (distribution) of the

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71 Study of the European Committee on Local and Regional Democracy (CDLR) with the collaboration of *Marcau G.,* Local Authorities Competences in Europe, 2007, 12, <https://rm.coe.int/1680746fbb>, [13.04.2018].

72 Constitutional Law of Georgia on Amendments to the Constitution of Georgia, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

73 Constitution of Georgia, Herald of Parliament of Georgia, № 786, 31-33, 24/08/1995.

powers and function to the lower territorial units. Thus, the precise term has not been selected in the Constitution. Accordingly, the relevant norm of the article of the Constitutional Amendments should be referred to in the sense of the division (distribution) of powers and functions.

According to the concept of subsidiarity the choice regarding the division of power is made in favour of the local government, which is the closest public entity to the population and this principle equally applies to all the territorial units of the state authorities. In the Constitutional Amendments the mentioned element of the concept of subsidiarity is disregarded. The Constitution indicates to the division of powers only between the state and local government, whereas the issue concerning the division of powers between the autonomous republic and local government is not deemed to be noteworthy. We hope, that the mentioned article of the Constitution will be defined more broadly in the process of enforcement and the principle of subsidiarity will become the guideline principle also for the division of powers between the autonomous republic and local government.

In addition, in the process of the division of powers the effective implementation of the principle of subsidiarity requires the existence of the adequate legal guarantees. The experts of the Congress explicitly indicate that the enforcement process of the principle of subsidiarity requires the regular supervision. In this respect, one of the mechanisms is considered to be the Constitutional control exercised by the constitutional court.[74]

Unfortunately, the legislators of Georgia abstained from strengthening the legal significance of the principle of subsidiarity with the effective Constitutional control mechanism. Pursuant to the Constitutional Amendments the self-governing units does not reserve the right to apply the Constitutional Court of Georgia for protection of the principle of subsidiarity. All in all, the issue related to the practical enforcement of the principle mainly depends on the political will of the state power which offers the vague prospect of launching the principle.

6.2.2. The Challenges of Separation and Division of Powers

As it has been mentioned the principle of subsidiarity implies the implementation of the public duties by the government closest to the citizens. Correspondingly, the first stage of implementation of the principle in Georgia should begin with the reconsideration of the issues related to the division of powers between the State and local self-government. The overall agreement which functions are vested on the categories of the local importance does not exist. The functions of local authorities in different countries considerably vary from each other. The general criteria and principles to be taken into consideration in the process of the enforcement of subsidiarity principle were reviewed above, but the issue concerning the transfer of the certain functions to the local authorities requires to conduct the separate research. In the process the peculiarities of geographic, historic and territorial arrangement should also be taken into

74 *Delcamp A., Balducci M., Busch J., Nemery J., Pernthaler P., Uyttendaele M.,* Definition and Limits of the Principle of Subsidiarity, Report Prepared for the Steering Committee on Local and Regional Authorities (CDLR), Local and Regional Authorities in Europe, № 55, 1994, 34.

account. Thus, within the scope of the presented paper it is possible to discuss only the major objectives and principles of the relevant reform to be implemented in Georgia.

Despite the slight increase of functions of the local self-government in 2013-2014 years, on the whole the limited number of functions are assigned thereto (see Appendix). The aforesaid is confirmed on the basis of the comparative analysis of the foreign countries as well. In particular, in 2014 the research evaluating the process of decentralization in 39 European countries during the last 24 years was published. According to the results of the research, despite the fact that the tendency of increasing the autonomy of the local self -government has been fixed in Georgia since the 90s up today, the country still belongs to the group of the least decentralized countries. Particularly, it is ranked as the 36th - one of the last among 39 countries. Such position is mainly conditioned by the extremely low quality of financial autonomy and the insignificant functions of the local self-government. The research reveals that the local self-government performs the restricted functions in the most important fields of local affairs, such as: education, health care, social security and public order. According to the extent of decentralization Georgia is outrun by almost all the countries of Eastern Europe: Moldova, Ukraine, Macedonia, Czech Republic, Slovenia, Serbia, Croatia, Baltic Republics and etc.[75]

On this basis, the discussion on the issue regarding the transforming of the new functions to the local self-government is possible to be started with the fields mentioned in the study (the education, healthcare, public order and social security). The list of authorities, which fell within the competence of the district governance authorities of Georgia pursuant to the Law of 1997, may also come useful (see Appendix).

As it was reviewed above, for the purpose of efficient realization of the principle of subsidiarity it is of equal importance to make the clear separation between functions. The analysis of the legislative acts reveals that there exist the serious problems in Georgia to this extent. Specifically, it is often impossible to understand whether the authority is endowed on the central government bodies, an autonomous republic or on the local self-government or whether it is the delegated or own power.[76] The similar problems complicate the identification of the public bodies responsible for exercising the certain authorities. Eventually, this bureaucratic labyrinth damages the interests of Georgian citizens.

In order to respond to the mentioned problems, in 2013 pursuant to the Local Government Code[77] the Georgian Government assumed the responsibility for making the relevant legislative amendments. In April 2016, the set of amendments to 174 of laws were introduced to the parliament to be considered. In Spring of 2016, at the Spring Session the Parliament of Georgia adopted the proposed amendments with the first hearing, however, the further discussion on the legislative package was terminated for the unknown reasons.

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75 See *Ladner A., Keuffer K., Baldersheim H.,* Measuring Local Autonomy in 39 Countries (1990-2014), Regional and Federal Studies, Vol. 26, № 33, 2016, 321-357.

76 See *Zardiashvili D*., The Powers of the Self-Governing Units, Tbilisi, 2009, 38-70 (in Georgia).

77 Article 165, Sec. 2, Organic Law of Georgia, Local Self-Government Code, Legislative Herald of Georgia, 1958-IIS, 19/02/2014.

6.2.3. The Issue Concerning the Separation and Division of Powers in Autonomous Republic of Adjara

The analysis about the vertical (territorial) separation and division of the powers of the public authorities would be unaccomplished without reviewing the problems of separation and division of the powers of the Autonomous Republic. Due to the occupation of the Georgian territories the issue concerning the administrative-territorial arrangement of the State is unresolved. Accordingly, within the present paper the analysis of the issue of separation and division of powers could be conducted only related to the Autonomous Republic of Adjara.

Before the Constitutional reforms of 2017, under the Constitutional Law "on the Status of Autonomous Republic of Adjara", the powers of the Autonomous Republic were stipulated by the Constitution of Georgia, Constitutional Law and the Constitution of Autonomous Republic of Adjara. At the same time, in case of not regulating the issues included in the exclusive powers of the Autonomous Republic of Adjara by the Autonomous Republic, it could have been regulated by the legislative act of the state.[78] The aforesaid rule attached the sign of competitive powers to the exclusive powers of the Autonomous Republic.

In addition, the Constitutional Law encompassed a number of norms making the functions included in the scopes of exclusive powers of the Autonomous Republic identical to the functions of the local self-government[79] (e.g. construction of the local roads and issuing local construction licenses etc.).

Pursuant to the new Constitutional Law on "The Autonomous Republic of Adjara" of October 13, 2017 the issues concerning the powers of the Autonomous Republic has been substantially revised. The new Constitutional Law envisaged the possibility of prescribing the powers of the Autonomous Republic of Adjara by the Law of Georgia and the Law of the Autonomous Republic of Adjara too.[80] In addition the Constitutional Law of Georgia enshrined new legislative norm responding to the idea of subsidiarity. In compliance with the Constitutional law, "Autonomous Republic of Adjara may exercise any authority in the fields of economy, agriculture, tourism, health care and social security, education, culture, sport and youth policy, environmental protection, which does not belong to the exclusive powers of the state authority or own exclusive powers of local self-government and the exercise of which is not excluded from the powers of the Autonomous Republic of Adjara based on the Legislation of Georgia"[81] Furthermore, the above mentioned problem of duplication of the duties of the local self-government has been solved.

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78 Article 6, Sec. 1 and Article 7, Sec. 2, Constitutional Law of Georgia on the Status of the Autonomous Republic of Adjara, Legislative Herald of Georgia, № 16, 04/07/2004.

79 See *Kakhidze I.,* Administrative Supervision over Local Self-Government Bodies, Comparative Analysis, Tbilisi, 2012, 308-309, (in Georgian).

80 Article 2, Sec. 1, Constitutional Law of Georgia on Autonomous Republic of Adjara, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

81 Ibid, Article 2, Sec. 3.

Despite some of the positive amendments, the Constitutional Reform has raised the new questions. Particularly, they are as follow:

The functions included in the exclusive powers of the Autonomous Republic of Adjara have been significantly reduced. Despite the fact that the Autonomous Republic of Adjara is vested with the significant rights and guarantees by the Constitutional Law of Georgia (e.g. the right to property, financial autonomy, right to enact the laws of the autonomous republic, organizational autonomy, etc.), the exclusive powers of the autonomous republic include only a few functions, such as: spatial planning; management of the roads of the autonomous significance; the management of educational, scientific, art and sports organizations; the operation of archive of the autonomous republic and the management of land, water and forest resources.[82]

The reason of the substantial contraction of the list of functions included in the area of the exclusive power is ambiguous. The field of the exclusive powers of the Autonomous Republic of Adjara may have encompassed at least those functions which are stipulated as the functions of the Autonomous Republic by the various laws of Georgia. For example, what legal or other type of reasoning may the inclusion of the function of operating the autonomous republic archive in the scopes of the exclusive powers, while the functions, such as: the management of landfills of solid waste, the implementation of fire–rescue measures over the territory of Autonomous Republic of Adjara, the maintenance of the primary schools, regulating hunting activities, the management of the hospitals and healthcare organization of the Autonomous Republic, etc. - are excluded?[83]

Some other issues pertaining to determining the powers of the Autonomous Republic have not been clarified either. According to the old Law, the exclusive powers of the Autonomous Republic could be defined only by the Constitution, Constitutional Law and the Constitution of the Autonomous Republic. Whereas the new Constitutional Law envisages (Article 2, section 1.)[84] the possibility of prescribing (transferring) of the powers by the Law of Georgia as well. At this point the following logical questions arise: what type of powers can be prescribed by the Law of Georgia? The Constitutional Law recognizes only two types of powers of the Autonomous Republic, such as: exclusive and delegated powers. In case the legislator admits the existence of the third type of the power, the issue requires more distinct and detailed regulation. In particular, the issues concerning the procedures transferring the new functions and imposing the new obligations of the Autonomous Republic should be laid down by the Law of Georgia as well as the necessity of consultations or the question related to the reimbursement of costs incurred require to be determined. These are the issues which should be responded at least by the new Constitution of Adjara which is in the process of drafting.

In addition, upon comparing the 2nd section of Article 75 of the Constitutional Amendment with the 4th section of Article 2 of the Constitutional Law on the Autonomous Republic of Adjara, the principle of division of powers between the local self-government and the Autonomous Republic of Adjara is

82 Ibid, Article 2, Sec. 2.

83 25 laws comprising the functions and duties of the Autonomous Republic are identified by us.

84 Article 2, Sec. 1, Constitutional Law of Georgia on Autonomous Republic of Adjara, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

ambiguous in the part of so-called "undistributed" competence. In particular, it is not clear which government enjoys the privilege of the performance of those functions which neither belong to the state authorities and the field of the exclusive power of the Autonomous Republic nor represent the exclusive power conferred on the self- governing units.[85]

It is noteworthy, that the Constitution as well as the Constitutional Amendments highlight the issue concerning the necessity of separation of powers between the state authorities and the local self-government. But the issue as regards the need for the separation of powers between the Autonomous Republic and the local government is still ignored.[86]

6.3. Financial Autonomy

The capability of the local self-government to exercise the transferred authorities successfully greatly depends on the quality of financial autonomy of the local self-government.

The financial autonomy consists of three components: the revenue autonomy, expenditure autonomy and the budget autonomy, which implies that the local government should have its own income and be eligible to manage it independently and on its own liability as well as enjoy the freedom to determine its own budget.[87]

According to the overall evaluation, the financial autonomy is considerably low in Georgia. Particularly, the local self- government has the limited degree of expenditure and revenue autonomy. The major sources of income of the self-governmental units are the state transfers and the only local tax is a property tax. The transfers allocated from the central budget often assume the specific purpose and the local self-government is constrained to freely manage it. At the same time, the high dependence on the central transfers reduces the possibility of independent planning and regulating of the revenues. According to the conditions of the above mentioned system, the local government does not take any interest in the development of the local economy as the increase of local income does not make any substantial changes to local self-governing units' revenues. Moreover, the increase of local incomes may account for the reduction of the amount of transfer guaranteed by the central government.[88] The solution to this problem is to transfer the independent sources of revenues (e.g. the local taxes, the pro rata share from the state taxes, payments, etc.) and entrust the control and regulation of the expenditure to the local self-government.

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85 Comp. Article 75, Sec. 2, Constitutional Law of Georgia on Amendments to the Constitution of Georgia, Legislative Herald of Georgia, № 1324-RS, 19/10/2017; with Article 2, Sec. 4, Constitutional Law of Georgia on Autonomous Republic of Adjara, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

86 See Article 101^2, Sec. 1, Constitution of Georgia, Herald of Parliament of Georgia, № 786, 31-33, 24/08/1995 and Article 75 Sec. 2, Constitutional Law of Georgia on Amendments to the Constitution of Georgia, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

87 *Beer-Toth K.,* Local Financial Autonomy in Theory and Practice, The Impact of Fiscal Decentralisation in Hungary, Fribourg, 2009, 70, <https://doc.rero.ch/record/12729/files/Beer-TothK.pdf>, [15.04.2-18].

88 See *The World Bank,* Geogia Public Expenditures Review, Strategic Issues and Reform Agenda, Vol. 1, Washington, 2014, 56-66; *Ladner A., Keuffer K., Baldersheim H.*, Measuring Local Autonomy in 39 Countries (1990-2014), Regional and Federal Studies, Vol. 26, № 33, 2016, 321-357.

Due to the range of the topic it is impossible to conduct more detailed analysis of the local financial autonomy within the scopes of this paper. Correspondingly, the financial autonomy of the local self-government will be discussed below only in terms of the constitutional guarantees.

According to the 1st section of Article 76 of the Constitution of Georgia the local government has its own property and finances. This citation from the Constitution is rather general only indicating to the possibility for the self-governing unit of possessing its own property and finances. The Constitution of Georgia would have provided the better guarantee for protecting the financial autonomy of the local government, if it had directly indicated that the self–governing unit enjoyed the financial autonomy. Let alone, the term – "financial autonomy" has already been used in the Constitutional Law of the Autonomous Republic of Adjara by the legislator.[89] Unfortunately, within the framework of the Constitutional Reform of 2017 the mentioned term was rejected to be used again.

The sufficient constitutional guarantee for financial autonomy of the local self-government is not provided by the 4th section of Article 7 of the Constitutional Amendments either, pursuant to which "the state ensures the compliance of the finances means of the self- governance units with the authorities thereof stipulated by the Organic Law."[90] The term -"the means of finances" (financial means) allows the state to execute the extremely broad interpretation and implies the probability to make no changes to the existing situation. It was desirable, in order to change the above mentioned situation, the legislator had used the phrase - ensuring "the own revenue sources" instead of referring to the term "the means of finances." It is worth noting, that exactly such approach is envisaged by the Constitution of Estonia, Hungary, Germany, Poland, Armenia, Portugal, France, Spain, Slovenia and Italy. In addition, the Constitutional value of the mentioned Article is even more reduced by the fact that according to the Constitutional Amendment, the self-governing unit does not reserve the right to apply the Constitutional Court of Georgia to protect the local autonomy pursuant to the mentioned article.

To sum up, it may be concluded that in Georgia the extent of implementation of the principle of subsidiarity will be directly depended to the financial decentralization reform, which should ensure the real financial autonomy of the local government.

6.4 The Territorial Reform

The implementation of the principle of subsidiarity always raises the question concerning the territorial level and its extent within which the most effective enforcement of the principle is possible. The issue leads us to the reconsideration of the current administrative-territorial division of the country.

Today in Georgia the existing borders of the municipalities coincide with those of districts established in the period of the Soviet Union. This arrangement was reestablished as a result of the local self-government reform of 2006, when more than 1000 small self-government units were abolished and the authorities of the district governance were replaced by the local self-government bodies. As a result of the

89 Article 2, Sec. 5, Constitutional Law of Georgia on Autonomous Republic of Adjara, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

90 Comp., Article 7, Sec. 4, Constitutional Law of Georgia on Amendments to the Constitution of Georgia, Legislative Herald of Georgia, № 1324-RS, 19/10/2017.

reform Georgia is ranked as one of the first positions according to the size of the self-governing units (under the average population) in Europe (following Denmark, the United Kingdom of Great Britain). There are the cases when the areas of a separate municipality exceed the territory of Autonomous Republic of Adjara or approximately equals thereto (e.g. the municipalities of Dusheti, Dedoplistsyaro, Mestia, Akhmeta).

The outcome of the reform of 2006 is not unequivocal; for example, according to the research conducted by the Polish scientist *Pavel Swianiewicz*, the mergers of self-governing units were not resulted by improving the quality of local self-government autonomy.[91]

Under the conditions of existing large municipalities a number of practical problems arise. For instance, in some cases the administrative centre of the municipality extends a long way from the peripheral villages, in addition, it is difficult to achieve the balance of interests between the administrative centre-a city and villages (within one large municipality). The aforesaid problems reduce the involvement of the population in resolving the local issues and the possibility to provide the efficient management at local level. All in all, the positive effect of the principle of subsidiarity – the opportunity of the management adapted to the local conditions and requirements is eventually missed out on.

In Georgia since 2013 after the reform the status of a self-governing city has been additionally granted to seven cities – the administrative centres of historic-geographic regions of Georgia. The Code envisaged the further continuation of the territorial reform,[92] however, in 2017 the Parliament of Georgia abolished the newly – created cities and declined to proceed with the territorial reform.[93]

Thus, more flexible and efficient enforcement of the principle of subsidiarity requires the objective reassessment of the existing territorial division. The existing system and boundaries of the authorities of local self-government should be revised in compliance with the challenges and objectives facing the state and local population needs.

In the mentioned process, on the one hand, it should be taken into consideration whether the local government maintains the close territorial proximity to the local population, on the other hand, the reform should discharge the central government from the communal functions. The process may illustrate the reasonability of the existing municipal borders as well as the need of establishment additional level (including regional level) local self-government too.

6.5. The Human Resources

The effective implementation of the principle of subsidiarity is related to the real ability of the local self-government to exercise its powers. And the mentioned ability requires the existence of relevant financial as well as the human resources.

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91 See *Swianiewicz P., Lielczarek A.,* Georgian Local Government Reform: State Leviathan Redraws Boundaries?, Local Government Studies, Vol. 36, № 2, 2010, 307-309.

92 Article 152, Sec. 1, Organic Law of Georgia, Local Self-Government Code, Legislative Herald of Georgia, 1958-IIS, 19/02/2014.

93 Within this article it is impossible to assess 2013 territorial reform in Georgia as well as decision of the Government of Georgia made in 2017 therefore there is only indication to the relevant facts.

Today in Georgia one of the main challenges of the decentralization reform is the lack of the qualified personnel at the local level. By the Code of 2013 the municipalities were imposed the obligation concerning the amount of money to be allocated for training and further professional development of the public officials employed in the municipalities. Pursuant to the Code, this amount of money should have been equal to no less than 1 percent of the total volume of public servants' remuneration envisaged by the budget of the municipality. In order to ensure the effective implementation of the mentioned obligation, "The system of lifelong education of local self-government's public servants, the powers of the agencies involved therein and the system and rule of implementing this system" was adopted by the Government of Georgia in accordance of the Article 132 of the Public Service Law of Georgia of 1997. Unfortunately, the practical realization of this system could not be managed.

In particular, the new Law of Georgia on Public Service having been entered in force in 2017 didn't envisage any specific regulations related to the vocational education of the public officials employed in the municipalities and the above mentioned resolution of the Government of Georgia was declared to be annulled. Regrettably, the requirements and challenges facing the municipalities and state authorities are reviewed in the same terms and no differentiation is made by the new Law of Georgia, whereas the deep acuteness of the shortage in the qualified staff at a local level and the need of specific approach is generally acknowledged.

In conclusion, one of the primary objectives of the state power shall be to form the system of development of the qualified human resources in the municipalities, otherwise all the reform of decentralization is doomed to failure.

7. Conclusion

As mentioned above, the role of a state in the system of public administration is being transformed. The modern states have discovered that they are not alone anymore and the world around them has substantially changed. The structure of the society has become more complicated and diverse revealing more difficult and divergent interests as well. The model of the centralized governance is becoming less appealing due to the anonymity and complexity of the decision- making process.[94] In such a situation, the principle of subsidiarity, which is premised on the idea of autonomy (self-government) and requires to take into account the interests of various groups, unions and territorial units, has become the attractive conception.

The major benefit of subsidiarity is the maintenance of diversity under the idea of the unified state. It is centred on the interests and freedom of each person. The principle of subsidiarity introduces new criteria in the process of assessing the effectiveness of the public administration. While analyzing the governance process it emphasizes on the qualitative criteria alongside to the financial and economic criteria. The subsidiarity provides the creation of equal conditions by applying the individual and diverse approaches. Its

94 *Vischer K. R.,* Subsidiarity as a Principle of Governance: Beyond Devolution, Indiana Law Review, Vol. 35, № 103, 2001, 126.

final objective is to promote the existence of the government caring for the interests of the specific groups, unions, territorial units and individuals, which is based on the idea of common well-being.

The implementation of the concept of subsidiarity pertains to the substantial transformation of the governing process that demands the considerable change of behaviour of all the subjects involved in the process. The attempts of enforcement of the principle of subsidiarity in Georgia has not achieved much success up today. The reforms conducted in different periods are controversial, the positive advance of the reform is sometimes followed by regress, and more frequently the situation is stagnating.

The present paper reviews five major challenges to the implementation of the subsidiarity principle in Georgia, overcoming of which is the essential condition for the effective enforcement of the principle. In particular, first of all, the principle of subsidiarity will be left only on pages of the Constitution of Georgia, unless there exists the real political will for its enforcement; secondly, the "benefit" of the principle will not be sensed unless the authorities are effectively distributed between the central and local levels and the subject responsible for exercising the power is not precisely defined; thirdly, the execution of the principle will not start unless the local government is transferred the adequate sources of revenues; the fourthly, the various local interests and demands will not be adequately satisfied unless the accurate local territorial boundaries for the enforcement of the principle is fixed and at last, unless the system of development of the appropriate human resources is created, any attempt to implement the principle of subsidiarity is doomed to failure.

Appendix

Local Government Functions in Georgia 1997-2018[95]

1997-2006	2006-2013	2013-2018
Economic Profile		
Solid Waste (household) Management;	Solid Waste (household) Management	Solid Waste (household) Management
Management of the Local Roads;	Management of the Local Roads;	Management of the Local Roads;
Outdoor Lighting;	Outdoor Lighting;	Outdoor Lighting;
Organization of the Public Transportation Service;	Organization of the Public Transportation Service;	Organization of the Public Transportation Service;
Amenities of the Area of the Municipality Planting of the Territory;	Amenities of the Area of the Municipality Planting of the Territory.	Amenities of the Area of the Municipality Planting of the Territory;
Water Supply and Sewage;		Water Supply and Sewage;

95 The Graph is prepared based on the analysis of the Organic Law on Local Self-Government and Governance of Georgia, Legislative Herald of Georgia, N44, 11/11/1997; The Organic Law on Local Self-Government of Georgia, Legislative Herald of Georgia, N2, 09/01/2006; The Organic Law of Georgia, Local Self-Government Code, Legislative Herald of Georgia, 1958-IIS.

The Development of the Melioration Systems of Local Importance;		The Development of the Melioration Systems of Local Importance.
Housing;		
Gas Supply;		
Electricity Supply.		
Town Planning and Regulatory Profile		
Spatial Planning;	Spatial Planning;	Spatial Planning;
Organization of the Traffic;	Organization of the Traffic;	Organization of the Traffic;
Issuance of Construction Permits;	Issuance of Construction Permits;	Issuance of Construction Permits;
Regulation of the Outdoor Trade, Exhibitions, Markets and Fairs	Regulation of the Outdoor Trade, Exhibitions, Markets and Fairs	Regulation of the Outdoor Trade, Exhibitions, Markets and Fairs
Arrangement and Maintenance of Cemeteries;	Arrangement and Maintenance of Cemeteries;	Arrangement and Maintenance of Cemeteries;
Regulation of the Outdoor Advertising Placement	Regulation of the Outdoor Advertising Placement	Regulation of the Outdoor Advertising Placement
Assigning Names to the Geographical Objects;	Assigning Names to the Geographical Objects.	Assigning Names to the Geographical Objects;
Make Decisions on the Usage of the Natural Resources[96].		Make Regulations on Keeping Pets, and Homeless Animals.
Education and Social Profile		
Pre-school (kinder gardens) and Out-of-School Education;	Pre-school (kinder gardens) and Out-of-School Education;	Pre-school (kinder gardens) and Out-of-School Education;
Libraries, Cinemas, Museums, Theatres, Sports -Recreational Facilities;	Libraries, Cinemas, Museums, Theatres, Sports -Recreational Facilities;	Libraries, Cinemas, Museums, Theatres, Sports -Recreational Facilities;
Protection and Development of local Identity and Cultural Heritage;	Development of appropriate and adapted Municipal Infrastructure for Disabled, Children and Elderly;	Development of appropriate and adapted Municipal Infrastructure for Disabled, Children and Elderly;
Maintenance and Preserving of Local Cultural Monuments;		Protection and Development of local Identity and Cultural Heritage;
Maintenance Primary and Secondary Schools, Special Schools;		Maintenance and Preserving of Local Cultural Monuments;
Hospitals and Primary Healthcare;		Provision of shelters to the homeless People;

[96] Italic shrift indicates to the functions of the District Local Governance during 1997-2005.

Elderly Shelter Homes and Orphanages;		
Organizing Sanitary, Veterinary and anti-Epidemic Activities;		
Public Order and Security Profile		
Fire and Rescue Services;	*Fire and Rescue Services;*	Regulation of the Issues, Related to Organizing Public Meetings and Demonstrations.
Maintenance of the Public Order and Civil Defense;	Regulation of the Issues, Related to Organizing Public Meetings and Demonstrations.	
Environment Protection and Ecological Security.		

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Kakhi Samkharadze*

Consideration of Competence Disputes in the Constitutional Court, as the Principal Constitutional Mechanism for the Realization of Power Division Principle

"Think of the word 'constitution — *it doesn't* mean *a 'bill of rights', it* means *structure*" — *Antonin Gregory Scalia*

The idea of the Constitutional Court is essentially linked to the constitutional control of the state authorities power. In the Constitutional judicial history, one of the most important precedents (Marbury vs. Madison) happened in the United States Constitutional Justice and it was particularly about the crisis of power division between state authorities. Therefore, at the modern development stage of the constitutionalism, it is important to evaluate the role and significance of the Constitutional Court's competence regarding the competent disputes. It is also necessary to evaluate the European experience in this direction and those important and interesting consequences for the constitutional control and constitutional justice within such competence. Consequently, within the framework of this key instrument of constitutional control, we should talk about the primacy of the law, within that the idea of constitutionalism should be developed. This issue has a doctrinal importance and at the same time has a special significance for the development of Georgian constitutionalism.

Key words: *Constitutional Court, principle of power separation, competent disputes, constitutional justice.*

1. Introduction

"It is universally recognized that the division of governmental power is one of the fundamental principles of the successful functioning of the state governmental organization and the Constitutional order. This provision, which has been repeatedly confirmed by the doctrine or practice, in the 16th Article of the "Declaration of the Rights of the Man and of the Citizen of 1789 (French: *Déclaration des droits de l'homme et du citoyen de 1789*)," was reflected: "The state, where is no division of the governmental power, has no constitution.[1]

History of Georgian Constitutionalism includes the number of different models of the state governance. Still under the Constitution of 1921, in the governance model, the division of governmental power was established in an interesting way. The main feature of this constitution is pointed out to be that, the basic law did not envisage the governance of the head of state and because of such peculiarities, it is called the "naive" constitution.[2] Law of November 6, 1992, so called "the small constitution" non-

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1 *Kverenchkhiladze G.*, Constitutional Status of the Government of Georgia (Comment on Article 78 of the Constitution), Contemporary Constitutional Law, *Kverenchkhiladze G., Gegenava D.* (eds.), Book I, Tbilisi, 2012, 8-9 (in Georgian).

2 *Papuashvili G.,* 1921 Constitution of the Democratic Republic of Georgia (from the perspective of 90 years), 2nd ed., Batumi, 2013, 24 (in Georgian).

ordinary regulated by the organization of the governmental bodies, for e.x. Under Article 17 of this Law, the person elected as the Chairman of the Parliament also had the status of the Head of State.[3]

According to the new Constitution, adopted on 24 August 1995, was created a new model of governance that formed a type of presidential governance system. This Constitution provided the basis for the idea of constitutional justice in Georgia, in particular, for the Constitutional Court.[4] By the constitutional reform of February 6, 2004, was formed the semi-presidential model of the mixed governance, to be more specific, the semi-presidential system of the presidential-parliamentary subtype.[5,6] Particularly, interesting is the constitutional law enacted on 15 October, 2010 and adopted on 17 November 2013 as a result of the constitutional reform of 2009-2010. According to which the responsibilities of the executive governmental authorities are separated from of the head of state and it is clearly defined, that the executive government is the Government of Georgia. Under this amendment of the basic law, classification of the state governance model was determined as the Prime Minister-Presidential subtype of the Semi-Presidential model. Mainly as a rule, in the such forms of governance arise constitutional conflicts and collisions.[7] It could be noted that, the Prime-Minister-Presidential model is more sensitive to constitutional conflicts, than-a Presidential-Parliamentary model.[8] In the frames of the principle of power separation, the parliamentary governance model, that will be established in Georgia within the framework of the 2017-2018 constitutional reform, is especially sensitive to the constitutional conflicts.[9]

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3 *Kverenchkhiladze G.*, Constitutional Status of the Government of Georgia (Comment on Article 78 of the Constitution), Contemporary Constitutional Law, *Kverenchkhiladze G., Gegenava D.* (eds.), Book I, Tbilisi, 2012, 19 (in Georgian).

4 The history of the constitutional justice is very important and is directly related to the development of constitutionalism and the idea of securing division of power. In the United States, in 1803, in the case of Marbury v. Madison, 5 U.S. 137 (1803), Judge *John Marshall* by his decision established one of the most important constitutional precedent, which is the subject of interest even today. The 1920s, *Kelsen*'s European Reception became the basis for the idea of the Constitutional Court. The Constitutional Court of Georgia was established on the base of the Constitution adopted on 24 August 1995.

5 The second wave of democratization in Europe has led to the types of regimes that do not belong to either parliamentary or presidential systems. The term 'semi-presidentialism' was first used by the French journalist and editor of the newspaper 'Le Monde' – *Hubert Beuve-Méry* in 1959, and in the case of academic spheres, the term in this case was used by *Maurice Duverger* "About of the Political Institutions and Constitutional Law" of 11th edition, *Elgie R.,* The Politics of Semi-Presidentialism, 1999, <http://www.researchgate.net/publication/265101267_The_Politics_of_Semi-Presidentialism>, [20.11.2018]. A mixed model of governance originated in the French constitution by combining European and American consensus systems and a hybrid of these two systems. *McQuire K. A.,* President – Prime Minister Relations, Party System, and Democratic Stability in Semiprezidental Regimes, Comparing the French and Russian Models, Texas International Law Journal, Vol. 47(2), 2012, 429.

6 *Alasania G.,* The Scope of the Executive Government of the President of Georgia with the Constitution of Georgia, Seminar Paper, Tbilisi, 2008, 23 (in Georgian).

7 *Protsyk O.,* Intra-Executive Competition between President and Prime Minister: Patterns of Institutional Conflict and Cooperation under Semi-prezidentalism, Politik Studies, Vol. 54, 2006, 222.

8 *Sedelius T., Mashtaler O.,* Two Decades of Semi-presidentialism: Issues of Intra-executive Conflict in Central and Eastern Europe 1991-2011, East European Politics, № 29:2, 2013, 115.

9 On 24th August, 1995 the Constitution compiles three major constitutional reforms: 1) of 6 February 2004; 2) of October 15, 2010 (adopted on 17 November 2013), and 3) the constitutional reform of 13 October

I can say, that despite of those changes, the realization of the power separation principle cannot be perfectly implemented without the substantial and practical involvement of the Constitutional Court. I believe that the confirmation for this is the fact that in finding for a political censuses and the number of reforms, the consensus about the optimal model of the power division has not yet reached and it is therefore important that this process be conducted through a much more impartial constitutional jurisdiction.

It is important to judge the idea of the primacy of law, on the base of the legal state principle in the context of the political-competent dispute. Consequently, all the competent or governmental collisions should be resolved within the constitutional jurisdiction, in order to ensure that these conflicts are systematically resolved, through the real constitutional mechanism of the principle of powers' separation. Since all competencies must serve the purpose and objectives, that are defined for each branch of the government, in accordance with their main state functions.

The principle of "judicial review" implies the idea of constitutional justice, which was introduced in 1803, in the case of Marbury vs. Madison.

According to the above mentioned, it can be clearly stated that as well in the frame of the acting, also within the future Constitution, the issue of constitutional conflicts among the state authorities is particularly relevant, because the basic law does not rigidly separate the competences and constitutional functions between state authorities.

In this situation, It can be said that the most important constitutional mechanism to eradicate such constitutional collisions is the constitutional court, as the main body to review the competent dispute between the highest authorities.

Therefore, it is important to be considered the contents of constitutional competences and practice in Georgia and Europe.

The purpose of the work is, on the base of the analysis of the Competent Dispute Conceptual Issues of regulatory provisions, to determine the necessity and inevitability of establishing a wide range of disputes in the Constitutional Court, also to evaluate the systematic resolution concepts of such constitutional conflicts and to present opportunities for implementation of them within the borders of justice idea.

For the research were used prescriptive, analytical, comparative, historical, legal, practical methods of analysis, as well as the meta-legal and interdisciplinary methods. As far as the discussion is around the political sector of the constitutional justice, also was used a historical-socio-political analysis.

2. Constitutional Justice as a Guarantee of Division of the Power

The well-known lawyer *Steinberg* correctly pointed out that, "It is an important circumstance when the constitutional reforms are implemented for the first time in the history of the state, constitutional justice is created, especially, when the former legal practice of that state did not deserve any trust."[10] The Constitutional Court may have a significant impact on resolving competent disputes over

2017 and 28 March 2018, which will enter into force, after 2018 presidential election. These reforms have transformed the model of governance and replaced the semi-presidential model with a dual executive governance system, in the form of semi-presidential and semi-parliamentary models, and it means the future transition to a classic parliamentary system.

10 *Bezhuashvili G.,* The Role of Modern International Law in Implementation of Georgia's Foreign Policy, Georgia and International Law, *Korkelia K., Sesiashvili I.* (eds.), Tbilisi, 2001, 27 (in Georgian).

foreign and domestic political activities. This issue is principally related to the sense of common sovereignty, which is assigned to all the governmental branches, including the Constitutional Court.[11] And therefore the court with its jurisdiction ensures the distribution of power by the principle of unity of government. "A big policy was, it is and will remain a problem of the Federal Constitutional Court of Germany. From the day of its' establishment, the Constitutional Court of Germany has to deal with this issue, since honest people have to make fair decisions on the merge of the politics and justice." [12]

About the Constitutional Court of Georgia, at first we have to noted that, according to Article 82 (paragraph 1) of the Constitution of Georgia[13], judicial power is executed according to the constitutional control, justice and other forms determined by law, but in accordance with article 83, paragraph 1, The Constitutional Court of Georgia is a judicial body of constitutional control" The same constitutional provision is read by Article 59 (2) of the Constitution, which constitutes constitutional control and at the same time constitutional justice.[14] Thus "Specialized judicial body" acts in Georgia, which carries out constitutional control and at the same time constitutional justice. I believe that this term may have a broad definition, than just being determined as a constitutional control, because the majority of scientists implies the examination of the constitutionality of the laws and normative acts (*M. Nudiel*, *T. Nasirova*, *G. Kakhiani*). There are also different opinions that do not only refer to the constitutional control as the concept of the legal acts, but also to examine the actions (*L. Lazarev*), but *A. Blancenagel* points out that, the constitutional control is the activity directed towards division of governmental power and resolving constitutional conflicts.[15] The most important function of the constitutional control organs is to consider competent disputes that are directly related to the principle of power separation.[16] The purpose of the constitutional justice is substantially the same as the constitutional control has, but somewhat different are the form of means for achieving the goal. It can be said that in the view of the guarantee of the Constitution's protection, it is far more effective than constitutional justice, because in this case the advantage is given to its purpose and not the formal circumstances.[17]

The Constitutional Court may be the only constitutional subject that can solve conflicts among the competent state organs. "*Carl Schmidt* believes that, because in the constitutional disputes there is more

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11 *Bezhuashvili G.,* Constitutional Legal Basis of the Foreign Policy of Georgia, Journal "Man and Constitution", № 3, Tbilisi, 2001, 57 (in Georgian).

12 *Getsadze G.,* Constitutional Justice and Politics?! (On the example of the Federal Republic of Germany), "Georgian Law Review", 1st 2nd Quarter, Tbilisi, 1999, 74 (in Georgian); comp. *Wesel U.*, Die Zweite Kreise, Zeit № 40, September, 1995.

13 The amendment to the Constitution of Georgia of October 13, 2017 and March 23, 2018, which is valid until 2018, when the newly elected president is elected in the presidential election. Constitution of Georgia, Departments of the Parliament of Georgia, 31-33, 24/08/1995.

14 Amendments to the Constitution of Georgia on 23 April 2017 and 2018 on the new edition after the newly elected president's election in 2018 presidential election. Constitution of Georgia, Departments of the Parliament of Georgia, 31-33, 24/08/1995.

15 *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 24 (in Georgian).

16 Ibid, 20.

17 We mean, for example, the categories of issues where the constitutional jurisdiction is not necessary to dispute a specific legal act, but from all forms, including constitutional traditions, habits, or/and any other action which may Constitutional subject.

politics, than the law, the supreme patron of the constitution cannot be the Supreme Court, but rather than the President of the Reich"[18], but for a long ago this view has been rejected, but the president still maintains the function of the constitutional guarantor. At the same time, the task of the President is to solve the problem, which constitutes constitutional conflicts between the state authorities and it should be implemented through the application to the Constitutional Court.[19] "In the post-soviet countries, the constitutional courts have the mandate to take part in political relations between the branches of government".[20] According to *Schwartz*, there should be a neutral institution in the system of power division, which will solve constitutional conflicts related to the power division.[21]

As far as the Constitutional Court examines disputes between the political-constitutional authorities,[22] and the political disputes are judged in accordance with the law, it is possible to say, that the law is the only "tool" for the Constitutional Court. However, when the constitutional authorities argue about their competences-the legal dispute is inevitably transferred into the political dimension.[23] According to *Jörn Ipsen*: "Justice is the aim, outcome, frame, and scale of the policy"."[24] By *Theodore Munts*: "the constitutional dispute is a dispute between law theorists and politicians".[25]

According to Article 89 (paragraph 2) of the Constitution of Georgia, it is established that, "the decision of the Constitutional Court is final. The normative act totally or a part of it is null and void, after the decision of the Constitutional Court is published." Essentially identical text is copied, the new Constitution, in particular in the new edition of the Constitution of Article 60 paragraph 5, however, the new edition of some favorites have been included in the contents of the regulations, according to which the normative act or its part loses force upon the moment of publication of the constitutional court decision, if the decision does not establish an act or part of the power loss of the other later date. So, in the end I can say that in the Constitutional Law the Constitutional Court's decision is the sole and final authority, and has the power to be mandatory for everyone. Regarding this issue, could be said, the primacy of the law in constitutionalism, which, in turn, is a constant guarantee of the power division and the unconditional recognition of other ideas and values of the constitution.

Of note is the fact that the status of the Constitutional Court would be suspicious, because of its ability to influence a policy. In this topic may be considered the case of the constitutional changes operated by the legal political subjects, and moreover, when these constitutional authorities have the possibility to act on The Constitutional Court.

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18 *Getsadze G.,* Constitutional Justice and Politics?! (On the example of the Federal Republic of Germany), "Georgian Law Review", 1st 2nd Quarter, Tbilisi, 1999, 75 (in Georgian).

19 *Nakashidze M.,* Peculiarities of Presidential Relations with Government Departments in Semi-Presidential Systems of Management, Tbilisi, 2010, 210 (in Georgian).

20 Ibid, 217

21 Ibid, 218

22 Political-constitutional organs are meant by the authorities of the authorities directly related to the implementation of the state policy based on their constitutional status.

23 *Getsadze G.,* Constitutional Justice and Politics?! (On the example of the Federal Republic of Germany), "Georgian Law Review", 1st 2nd Quarter, Tbilisi, 1999, 81 (in Georgian).

24 Ibid, 81, comp. *Ipsen J.*, Statrecht, München, 1996, 245.

25 *Getsadze G.,* Constitutional Justice and Politics?! (On the example of the Federal Republic of Germany), "Georgian Law Review", 1st 2nd Quarter, Tbilisi, 1999, 82 (in Georgian).

The constitutional justice openly confronted with the 'cardinal issues' of the policy gave the reverse results. For e.g., in the 50s of the twentieth century, the Supreme Court of South Africa recognized the discriminatory law as unconstitutional. In response, its power was restricted by constitutional amendments. Moreover, in 1993, the Chairman of the Russian Constitutional Court was dismissed from the position, after he interfered with the parliament and the president's dispute.[26] Despite of a such problematic experience in the Constitutionalism history, in Georgia there are sufficient safeguards in place to protect the court at the institutional level. This has been proved by the Constitutional Court practice, according to which the court may amulet the law, which determines its competences by other governmental bodies. Also, the adoption of the new amendment of Constitutional law against its will, is protected by a high quorum, but there is space for improvement and possibility of higher standard introduction.[27] Also, the judicial independence at the institutional level is ensured, as the independence of all judges is protected individually and there are substantial guarantees regarding carry out their powers.

Another issue that confirms the importance of judicial decision-making in constitutional conflicts is that the Constitution becomes politicized by entering "state objectives" into it. At the expense of this, political issues can be resolved not only by the interaction of the government forces but in exchange for it, to give the constitutional dimension, by which creates the possibility to find in the legal framework more balanced solutions for the political processes. But it is a very dangerous game because it is not easy to put legal forms into concrete situations."[28] Therefore, it is important that the Constitutional Court participates in the forming process of the state objectives correctly on the basis of general constitutional principles. That ultimately leads to less politicization of the text of the Constitution, which in itself is unconditionally important for the development of a legal state.

3. The Essence and Basis of the Competent Dispute

At the same time the purpose and essence of the Competent Dispute is the Article 5 (paragraph 4) of the Constitution (in accordance with the Constitutional Reform of 2017-2018, the paragraph 3 of Article 4 of the Constitution of Georgia envisages the principle of regulating the power separation),[29] ensuring the power separation principle and this mechanism is one of the basic constitutional and legal

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[26] *Shajo A.*, The Restriction of the Authorities (Introduction to Constitutionalism), *Maisuradze M.* (trans.), *Ninidze T.* (ed.), Tbilisi, 2003, 283 (in Georgian).

[27] In the frames of the 2013-2015 Constitutional Commission, there were the considerations regarding the Constitutional Court involvement in the discussion about new constitutional amendments. It is true that, so-called Certification Agency cannot be the perfect substitutive entity, but at some point, can create important guarantees to protect the law from unnecessary policies. See the project of Authors Group of Constitutional Law, <http://constcommission.ge/1-6>, [20.11.2018] (in Georgian).

[28] *Shajo A.*, The Restriction of the Authorities (Introduction to Constitutionalism), *Maisuradze M.* (trans.), *Ninidze T.* (ed.), Tbilisi, 2003, 45 (in Georgian).

[29] The constitutional laws of October 13, 2017 and March 28, 2018, which will come into force after the incumbent of the elected president in 2018. Above mentioned reforms have transformed the model of governance-presidential model has been replaced with a mixed governance model, as the combination of the semi-presidential and semi-parliamentary models, and with farther logical transition to a classic parliamentary system.

guarantees to ensure the power's horizontal division between the highest state authorities.[30] In addition to resolving the conflict between the highest state authorities, with the exception of the Constitutional Court, the dispute can become a collision of powers that arises between central and local authorities.[31]

Despite the multilateralism of the competence disputes', the classical competence dispute is the one between the highest authorities of the Government. The grounds for the competent disputes are defined by the Constitution, particularly in accordance with Article 89 (paragraph 1, subparagraph "b") of the Constitution of Georgia (from the Constitutional Reform of 2017-2018-the same is defined by the Article 60, paragraph 4, subparagraph "d" of the Georgian Constitution). The definition of the competence dispute between the state authorities could be in conflict with the definition of governmental branches' the functions and competencies by the Constitution of Georgia.[32]

The essence of the competence dispute, as one of the main constitutional-legal principle and the core idea of constitutionalism, is the ensuring of the supremacy of the principle for the power division. Constitutional conflicts have often arisen in countries where acted or acts the mixed governance model, more specifically, the semi-presidential model's subtype of Prime-Minister — Presidential governance model, which is currently active in Georgia. The same political regimes also operate in Poland and Hungary and in the states of Central and Eastern Europe, where government collisions happened in the circumstances of the newly formed governance systems. Although some competent conflicts may arise in the presidential republics, for example disagreement between the President of the United States and the Congress on the military powers, but the regulation of this dispute was easily accomplished in benefit of the President (Chief of Staff), and the decision was based on the legal nature of the state governance model.[33] In particularly of *Lewis Fischer's* opinion, the President of the United States can launch the war without agreement of the Congress.[34]

"With or without the Constitution, the government-structural conflicts were widespread in the former socialist bloc countries, and each of these conflicts due to of their constitutional nature became the subject of discussion for the Constitutional Court."[35]

The decisions list adopted by The Polish Constitutional Tribunal includes 1. Early cases of a delegation of governmental functions that deal with administrative duties; 2. Changes introduced in

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30 *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 147 (in Georgian).

31 In Georgia, due to the current legislation, the dispute between the central and local authorities is further expected, because the regulation of this issue is not directly determined by the constitution and depends on the full restoration of the jurisdiction on the entire territory of Georgia.

32 Competance disputes in doctrinal sources are more widely interpreted, and it includes the separation of competences in the vertical and horizontal context of the powers' division, which is considered within the competence of the Constitutional Court, *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 146 (in Georgian).

33 Actually only in 1975 Year During the Mayaguez incident, the conflict arose about the military powers between the President of United States and the Congress, and it was the only exception to the 132 military paradigms.

34 *Council on Foreign Relations*, Balance of U.S. War Powers, 2013, <http://www.cfr.org/united-states/balance-war-powers-us-president-congress/p13092>, [20.11.2018].

35 *Schwartz H.,* Establishing Constitutional Justice in Post-communist Europe, *Aleksidze K.* (trans.), Tbilisi, 2003, 112 (in Georgian).

the small constitution of 1992, concerning the relationship between the *Sejm* and the Senate; 3. The release of the Chairperson of the Radio-TV Broadcasting Board in 1994, which was related to the powers of the President over the governmental bodies; 4. The case of 1994, which concerned the issue of the dissolution of the *Sejm* and the budget, caused a conflict between the President and the *Sejm*. The first cases were about the relationship between the government and the ministry cabinet, in which the government went beyond the scope of the law and the matter was settled by its act, but the Constitutional Tribunal of Poland abolished this act.[36] Since then, the Constitutional Tribunal has made decisions that strictly adhered to the rule of law and legalized the highest standards in this regard.[37]

In Hungary and Poland, the constitutional courts, unlike the Supreme Court of the United States, have been consistently confined to economic issues, and this was caused by the economic situation in those countries. [38]

A case of Hungary is in an area of our interest, when the conflict arose conflict between the Prime Minister *József Antall Jr.* and the President *Árpád Göncz.* "The Prime Minister *József Antall Jr.* hoped to attend the meeting, instead of President *Árpád Göncz*, with *Czechoslovak* and Polish delegations, in *Visegrád*, to discuss the relationship with Western Europe, despite that the attendees had to be the head of the governments. The issue was resolved without pain."[39]

Thereafter, constitutional conflicts emerged and those were not easily resolved. The first controversy led to the efforts of the Defense Minister to control the armed forces, which seriously confronted the President *Árpád Göncz* and his political supporters, but the constitutional court resolved the dispute in favor of the government.[40] It is noteworthy that the Constitutional Court had judged this dispute in the part of the interpretation of the Constitution and therefore the decision was just a recommendation.[41]

Also, it is worth to say in few words, about the decision of the Hungarian Constitutional Court on competence disputes-in the case to choose between Primer Minister and the President, as the which authority body, who could assign the head of national TV-Radio broadcaster, the decision was made in favor of the Government of Hungary.[42]

It is also possible that to separate paragraph on the issues about the appointment of officials from the introduction of disputed functions. Because of that the above mentioned belongs to the cases, with high probability of development disputes regarding the Constitution, and already we have observed the practice of such disputes in Poland and Hungary, and also, in Georgia, there was the same kind of dispute case with the significant political content.[43] So, I consider that one of the main tasks of

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36 *Schwartz H.,* Establishing Constitutional Justice in Post-communist Europe, *Aleksidze K.* (trans.), Tbilisi, 2003, 112 (in Georgian). 113.

37 Ibid, 114.

38 Ibid, 117.

39 Ibid, 149.

40 Ibid, 149.

41 Ibid, 415.

42 Ibid, 120.

43 The diplomatic content of Amagvari's political content was broad in Georgian political reality, including the example of which was particularly relevant to the signing of the Association Agreement between Georgia and the European Union signed on June 27, 2014. This was partially expressed in the academic circle in this context, the following concepts were expressed: "Discussion on this issue [the issue of signing the Associa-

constitutional justice is to define clearly the Constitutional Court competence to discuss and resolve the disputes among the competent subjects and thereby facilitate the development of the principle of constitutionalism and separation of powers in the country. Consequently, the Constitutional Court must provide all necessary mechanisms to resolve disputes of this category.

4. The Scope of competence disputes

A competent dispute has to be understood broadly because the formal grounds for reviewing competent disputes are inadmissible and contrary to the idea of constitutional justice. A court dispute could be conducted directly through the interpretation of and within the constitutional provisions. Although the dispute between the competent authorities may also arise in relation to matters not directly defined by the Constitution, but with the constitutional content. I believe, that in this case the Constitutional Court must examine substantially and solve the problematic issues, including the more concrete explanation on the country's governance model nature, on the basis of broad understanding of the constitutional norms. The Constitutional Court must be the principal body, which determines the manner of power division in the different types of governance models, within its competences and in accordance with the governance model's classificatory.

It is right that a definition of a state governance model has to be a function of the commissions, but in this case it is necessary that the Constitutional Court has its own position on this issue, therefore which will result in systematic solving of a problem, to avoid of the development of new one with an incomplete solution. At the same time, the polemic about a definition of the governance regimes must not carry only the theoretic meaning and be considered only in the process of formation of the Constitution.

4.1. The Subjects of Competent Dispute

In the constitutional jurisdiction the parties are those constitutional bodies and persons, who have been granted with the status by the Constitutional Court of Georgia in accordance with the Or-

tion Agreement] would be considered to be complete, the dispute had to be decided on the competence of the Constitutional Court and not when the Prime Minister announced the issue closely. The constitutional dispute should be initiated by the President on the competence of the competence. If such a president is judged as a manifestation of legal and political culture in the legal state, such a move in Georgia will be considered 'political split' or 'rising presidential ambitions". *Liberali*, What is the meaning of the Liberal, who will sign the Association Agreement with the European Union?, 2014, <http://liberali.ge/blogs/view/5903/ra-mnishvneloba-aqvs-vin-moatsers-khels-evrokavshirtan-asotsirebis-shetankhmebas>, [20.11.2018] (in Georgian). There were also clearer opinions regarding this issue, the President of Georgia has the primary competence of signing the Association Agreement. This is the logic of the constitution. Nevertheless, discussion on this topic has been renewed once again. *Menabde V.,* Who should Sign the Association Agreement?, "Liberali", 2014, <http://liberali.ge/blogs/view/5889/vin-unda-moatseros-kheli-asotsirebis-khelshekrulebas> (in Georgian). In addition to this issue, broader public opinion polls have been interviewed so much about the current political issue. *Transparency International — Georgia*, The Association Agreement with European Union should be signed by the President of Georgia, 2014, <https://www.transparency.ge/ge/blog/evrokavshirtan-asotsirebis-shetankhmebas-kheli-sakartvelos-prezidentma-unda-moatseros>, [20.11.2018] (in Georgian).

ganic Law and the Constitution, in particular, defined by the articles 33-40 of the Law on Constitutional Court.[44] As for the competent disputes, this issue is regulated by Article 34 of the same law, in the 1 paragraph it sets out the determination of the applicant and the subjectiveness of the claim, and paragraph 2 regulates the legal status of the respondent.

The subjects in the competence disputes are the main participants of the constitutional jurisdiction, who dispute the competences and, therefore, they represent the governmental bodies and the constitutional officials. In the Constitutional Court, at the dispute, the subject can be only the authority or the official listed in Article 89 of the Constitution of Georgia. The subjects, referred to in Article 89 (1) of the Constitution, are: the President of Georgia, the Government of Georgia, at least 1/5 of the members of the Parliament of Georgia, the Supreme Representative bodies of the Autonomous Republic of Abkhazia and the Autonomous Republic of Adjara, representative body of self-governing unit-an assembly, the High Council of Justice or the Public Defender.[45]

By the Constitution and the Organic Law on the Constitutional Court, the head of state is also equipped with a universal power and a function to appeal to the Constitutional Court and request the discussion of the case, even though it is under his jurisdiction, or under the scope of other state governmental bodies. The above mentioned follows from the Presidential function as the guarantor of the Constitution, which is not literally read in the text of the Constitution, but the President gives the oath and therefore undertakes the responsibility to protect the Constitution, and it is from the list of the powers that are assigned to its constitutional jurisdiction. The President is entitled to submit the matter to the Court for almost all competencies of the Constitutional Court. The Organic Law of Georgia indicates all other constitutional bodies, enlisted in Article 89 of the Constitution, with competence to appeal to the Constitutional Court in the case violently involvement in their competencies by the another of state authority. Also, the 1/5 of members of the Parliament have got the universal applicant competence to appeal to the Constitutional Court, for the determination of competences between the authorities. This group can appeal to the Constitutional Court, if they define the violation in the frame of the constitutional competences of their own or of other governmental authorities.[46]

By the law the issues regarding the side of defender in the court is not clearly defined. Although the claimant in this category has to be represented by a governmental body that has issued a normative act in accordance with Article 34 (2) of the Organic Law,[47] but still there is no an exact definition of who may be the respondent when the dispute does not refer to the normative act, but the disputable is a constitutional-legal relationship, a constitutional-individual act or constitutional-legal action, which is not explicitly excluded by law and while, in accordance with the Constitution it can be viewed as a possible disputable subject. Consequently, the applicant has to specify who should be the defendant in relation to his claim, and the Constitutional Court has the competence, envisaged by law, on the same

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44 *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 197 (in Georgian).

45 Constitution of Georgia, Departments of the Parliament of Georgia, 31-33, 24/08/1995.

46 Organic Law of Georgia on the Constitutional Court of Georgia, Departments of the Parliament of Georgia, 001, 27/02/1996.

47 By the opinion of the applicant, the defender is the state agency, whose statutory act has violated its constitutional competences, Constitution of Georgia, Departments of the Parliament of Georgia, 31-33, 24/08/1995.

time, when the claim is registered, to send the copies of case to the President of Georgia, the Government, the Parliament, the Supreme Representative Authorities of Adjara and Abkhazia. Within 15 days, if these authorities claim that their competence could be restricted by the satisfaction of the claim, the Court is entitled to invite the concrete legal authorities to the dispute as a party.

Also, in this category of cases, by the law and the Constitution, is vaguely defined the full and comprehensive circle of suers and defenders. As I have already indicated the Organic Law of Georgia, in the case of determination of the applicant's circle, refers in general to the Article 89 of the Constitution, which does not specify the issue. So, it can be said that the Article 89 indicates as a representative bodies-a local self-government body, also the High Council of Justice and Public Defender.

First of all, I have to mention that, in the disputes of this category, the enlisted bodies' subjective nature is beyond of the scope. By the paragraph "E", in Article 89 of the Constitution does not at all consider the constitutional authorities, including the State Audit Office of Georgia, the National Bank of Georgia, the National Security Council and other constitutional subjects, whose functions and competencies are directly defined by the Constitution, and that they may be forced to address in defense of their competences to the Constitutional Court.[48]

The most evident problem in the constitutional court's current practice is related to the claimant's powers, as far as the defender is represented by the improper subject at the court, and the process cannot be fully accomplished without the appropriate parties and the right applicant. That is why, it is more appropriate that constitutional authorities not to have the limited rights to initiate a lawsuit in the Constitutional Court.[49]

4.2. The Object of Competent Dispute

The constitution of Georgia defines the right of the Constitutional Court's competencies to determine the dispute within the constitutional jurisdiction. According to the Constitution, the rules for the dispute process at the Constitutional Court is determined by the Organic Law and by the Organic Law of Georgia on the Constitutional Court, it is possible to judge the subject of the dispute, which may become the object of the Constitutional Court's consideration.

The constitutional claim concerns the dispute over the competence between the state authorities. Such dispute, based on Articles 23 and 34 (paragraph 2) of the Organic Law of Georgia on the Constitutional Court of Georgia, has to be examined by the Constitutional Court, if the breach of competence relates to a normative act.[50]

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48 Within the framework of the 2013-2015 Constitutional Commission, the proposals were also considered to include such powers as an institutional formation of independent constitutional organs.

49 By the record of № 3/6/668 dated October 12, 2015, the Constitutional Court has received a complaint of a group of members of the Parliament of Georgia, asking for the substantial consideration to find unconstitutional the amendment and addition of the 'Organic Law on the National Bank of Georgia' (№ 4188-I to 03/09/2015) The law adopted by the Parliament of Georgia by the justification Georgia had the National Bank, since the law adopted by the Parliament of Georgia limits the Georgian National Bank's, as the Constitutional Institute's competences. An Introductory Record of Plenum of the Constitutional Court of Georgia, № 3/6/668 of 12 October 2015.

50 Organic Law of Georgia on the Constitutional Court of Georgia, Departments of the Parliament of Georgia, 001, 27/02/1996.

The normative act clearly represents the subject of a possible dispute, but in addition to the statutory act, there are no other objects of the dispute envisaged by any legislation. However, by the analysis of the constitutional record, I can say that the dispute may arise in any matter, even if it does not concern the normative act.

The President has the opportunity to create a normative act, with the particular issues discussed on the government meetings and later adopted as the normative act and/or by the presidential request of creation a normative order on the governmental session, which in future could be appealed at the Constitutional Court. This possibility can be considered as the mechanism for realization, but of course, this approach is unnatural.

In addition, in the case of refusal of the submitted act for counter-assignment, the President of Georgia can appeal to the Constitutional Court and this type of dispute will have a normative nature. Also, the President of Georgia can appeal for the normative content of the Article 23 and the Article 34 (2) of the Organic Law of Georgia "On the Constitutional Court of Georgia", which may limit his power within reference to the Constitutional Court only regarding the constitutionality of the normative acts.[51]

In fact, above mentioned mechanisms, which may establish the constitutional 'truth' through the court, are based only a hypothetical reasoning. I consider that it may be more essential and give a better outcome in determination of the constitutional legal proceedings problems in practice, if the dispute goes not only in adherence with statutory text to the Constitution, but via the wider and more comprehensive legislative process.

In this way, the dialect of constitutionalism will be proceed with the formulated forms. There is an opinion, that the constitutional court should only discuss the disputes on normative acts with the legal grounds and not-the actions or legal relations. In particular, the doctrinal opinion states that "differentiation of subjects subject to constitutional justice is relatively simple, not by a circle of public relations or their importance, but with a 'normative scale'[52]. I believe, that it is not be appropriate to make such conclusions, even if the Constitutional Court examines the constitutionality of actions within other competences, including when the matter concerns the understanding of the impeachment or/and termination of the Parliamentary Deputies' delegation within the Constitution. In both cases, the Court actually discusses the circumstances of the case and therefore makes a decision.

There are the type of legal relations that neither can be considered within the competence of the General Court and nor be judged by the Constitutional Court within the current constitutional arrangement, as today it is impossible appeal if you do not have a normative-legal act. In this case, the issues of constitutional action or inactivity and constitutional individual legal acts are beyond judicial control.

In this case it is necessary to have an inspection body. In Georgia this type of "specialized body" [53] is the Constitutional Court and if it examines all the judgments related to constitutional control, will give better results.

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[51] In this case, all such subjects, which may be the claimant of this type of dispute, are eligible to make such a request.

[52] *Khubua G.*, Constitutional Court Justice and Policy, Journal "Review of the Constitutional Law", № 9, 2016, 8 (in Georgian).

[53] Generally there are specialized and non-specialized constitutional courts. The specialized body is the one, whose field of principal activity is constitutional control, *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 32-33 (in Georgian).

In practice of the Supreme Court of Georgia (*K. Davitashvili's* case) was the case, when the MP of the Parliament challenged the order N 286 of the President of Georgia, issued on 15th March 2003, which was a call for unscheduled meeting of the Parliament. The court did not examine the case, because, according to its decision, the act was not determined as a legislative, but as-an political act issued on the basis of the Constitution, and assessment of its appropriateness was beyond its competence. The Supreme Court stated that by taking the case into the consideration and ruling out the decision, would violate the principle of power division.[54]

Thus the Supreme Court did not accept for the consideration the case related to the individual constitutional-legal act. In spite of this impugned judicial assessment, I have to rely on the same opinion that the dispute arising from constitutional law is better to be considered by the Constitutional Court, due its specific nature, immediate and high level of competence.

5. The Rule of Examination of Competence Dispute and Enforcement of the Decision

The Constitutional Court shall guides by the strictly defined procedural rules in the case of the complaint. Constitutional proceedings are familiar with the following stages: 1) appeal to the Constitutional Court; 2) Preliminary examination and registration of the constitutional claim/submission; 3) Decision on the adoption of a constitutional claim/submission for substantial review; 4) Preparation of a constitutional claim/submission for substantial review; 5) Trial discussion.[55] The Constitutional Court reviews the dispute by reviewing the complaint and submission, in respect of which decisions or conclusions are made.[56]

The Competent Dispute Review in the Constitutional Court is carried out in compliance with the lawsuit. In accordance with paragraph 2 of Article 21 of the Organic Law of Georgia the Constitutional Court resolves the matter on competent disputes, usually with a collegial composition and not on the plenum. In accordance with the Organic Law of Georgia on the Constitutional Court of Georgia, in particular Article 23, paragraph 2, satisfaction of the constitutional claim on the issue of competent disputes leads to invalidation of the disputed normative act from its enactment. There may also be a multilateral constitutional dispute in the Constitutional Court when there are several applicants involved in the case review or/and respond to specific competences.

Besides that, it can be said that the person involved as the respondent is not necessary to be submitting/receiving subject of the contested normative act. In this context, the constitutional conflict can be understood as a result of legal and factual relations and not only a dispute on the basis of a normative act.

The Constitutional Court Board is authorized to consider a constitutional claim or constitutional submission and make a decision if at least three members are present at the session, and the Constitu-

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54 Decision of Supreme Court of Georgia of 22 May 2003, № 3d-as-44k-s-03, Decisions of the Supreme Court of Georgia on Administrative and other Categories of Cases, *Jorbenadze S.* (ed.), № 7, Tbilisi, 2003, 1769-1773.

55 *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 215 (in Georgian).

56 Ibid, 237.

tional Court makes a positive decision on a majority of the votes cast by a majority of the members attending the Panel.

The timeframe for consideration of the case is 9 months. The timeframe for reviewing a constitutional claim or constitutional submission to the court starts at the moment of their registration. The term of consideration of a special case, not more than two months, may be extended by the chairman of the Constitutional Court.

However, it should also be noted that these categories of disputes largely determine the constitutional order and they have a substantial impact on the constitutional system, and to my mind, that such disputes should be predominantly discussed by the Constitutional Court.

The decision of the Constitutional Court of Georgia is a self-acting act and is mandatory for the execution.[57] It is a legitimate definition of the constitution, when the consideration of the Constitution widely or narrowly is the subject of the Constitutional Court, even for the simple reason that he is the only and highest institution, whose decision-making mechanism is still in its hands.[58] However, the Georgian legislation provides certain mechanisms and important legislative safeguards in order to protect the decision of the Constitutional Court.

Organic Law of Georgia on Constitutional Court, in particular, in accordance with Article 25 §4[1], the Constitutional Court may withdraw the normative act without a substantive review If it considers that the decision that had already made on the matter leads to similar legal consequences of norms that are known as unconstitutional. In the practice of the Constitutional Court there are such cases when the Court has made such interlocutory decisions.[59]

In relation to these cases, the Constitutional Court has judged the legislative act that has been ruled out by the interlocutory decision. However, I believe that such a legislative guarantee should be directly reflected in the Constitution in order to protect the priority of the legal decision and the primary nature towards political decision making. Under the three-fold divisions of the government, the judiciary is, of course, involved in the division conflicts.

In Poland, the relationship between *Sejm* and the Constitutional Tribunal was particularly complex, as de Jure Tribunal's decisions on the unconstitutional nature of the law was not final.[60] The Polish *Sejm* did not carry out the execution of the tribunal decisions for a certain period.

However, the Tribunal, by its practice, determined, that the law, in which will not be enforced by the Parliament, would be automatically deemed to be valid after six months.[61] Also, an interesting practice was established by the Constitutional Tribunal when it considered that *Sejm* has no right to overcome the decision of the Constitutional Tribunal regarding the Act adopted without the signature

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57 *Nakashidze M.,* Peculiarities of Presidential Relations with Government Departments in Semi-Presidential Systems of Management, Tbilisi, 2010, 226 (in Georgian).

58 The Constitutional Court can overcome its own practice, but in this case it is necessary to make such a decision by the plenum.

59 Moldovan citizen Mariana Kiku against the Parliament of Georgia, Judgment of the Constitutional Court of Georgia of 14 December 2012, № 1/5/525. A citizen of Austria Matthias Huter against the Parliament of Georgia, Judgment of the Constitutional Court of Georgia of 24 June 2014, № 1/2/563.

60 *Schwartz H.,* Establishing Constitutional Justice in Post-communist Europe, *Aleksidze K.* (trans.), Tbilisi, 2003, 119 (in Georgian).

61 Ibid, 120.

of the *Sejm*.[62] In this case, it is also noteworthy that if we consider not only the normative act as a possible dispute in the court, but also the act or omission of any other constitutional-legal act or competent authority, the issue may be problematic in part of its enforcement. On the one hand, it is true that the decision of the Constitutional Court is self-enforced and, as a rule, does not lead to additional legal action, on the other hand, in case of such competent dispute, the cancellation of a constitutional act can be somewhat ineffective without substantial review. Since the dispute concerns a specific action, it may be difficult to assess if this action leads to the same legal consequences. Thus, this process will resemble 'real constitutional control',[63] which will result in the more constitutional dispute at the Constitutional Court, the court can not bypass substantial reviews and making decisions on all these types of cases.

Consequently, such regulation loses the positive effect that is a function of the abovementioned norm, that public interests were protected, saving state and judiciary resources, saving the economy, and most importantly, the guarantees of the enforcement of the Constitutional Court decision. The enforcement of the decision of the Constitutional Court will be changed and the parties to the constitutional dispute will be subject to different legal conditions. Despite the possible problems, this competence should be widely understood in order to implement the constitutional principle of the division of power in all forms and means.

In Poland, *Lech Walesa* tried to rewind a decision of the Constitutional Tribunal in the case of TV and Radio Broadcasting in 1994,[64] saying that the decision of the Tribunal had no retroactive force, but in 1995 the same Constitutional Tribunal explained that his decision was normally involved in the retroactive effect.[65]

6. Practice of the Constitutional Court of Georgia (Competent Disputes)

In legal literature, it is considered that the court decision is a lawful act in the common law countries, but in some cases it is a legal source of precedent, in contrast to roman German systems, which are considered to be just the act of law.

On the one hand, it can be said that the Constitutional Court is a source of law by executive effect of its decision and legal nature of action, on the other hand, the General Court will use it only for

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62 *Schwartz H.,* Establishing Constitutional Justice in Post-communist Europe, *Aleksidze K.* (trans.), Tbilisi, 2003, 120 (in Georgian)

63 It is important for the composition of the Constitutional Court to implement the 'real' constitutional control. Until now the doctrinal staff: judicial self-restraint, political question doctrine, *abgestufte Verhältnismäßigkeitskontrolle*, *Beck'sche Formel*, *Schumann's Formel,* etc.) and the most difficult process are considered, constitutional control. The object (compliance with the Constitution, and not the hierarchical balance between the legislative and general normative acts in the control of the law enforcement process and specify the quality of the constitutional judges in the proceedings ('real' constitutional control), *Erkvania T.,* Normative Constitutional Claim as an Imperfect Form of Concrete Constitutional Control in Georgia, 2014, <https://emc.org.ge/ka/products/normatiuli-sakonstitutsio-sarcheli-rogorts-konkretuli-sakonstitutsio-kontrolis-arasrulqofili-forma-sakartveloshi>, [20.11.2018] (in Georgian).

64 The president of the TV and Radio Broadcasting Director was considered an exemplary rule.

65 *Schwartz H.,* Establishing Constitutional Justice in Post-communist Europe, *Aleksidze K.* (trans.), Tbilisi, 2003, 117 (in Georgian).

justification, as the Constitutional Court only fulfills the function of a negative legislator.[66] It is possible to say that *René David's* opinion that "the judge should not become a law in countries of Roman-German law",[67] can not be applied to the Constitutional Court. It can be said indirectly that the legislator[68] is guided by the Constitutional Court when it makes a decision and thinks about whether or not a specific legislative or other normative act may later become subject to the Constitutional Court.

Georgia's Constitutional Court has no diverse experience in discussing competent disputes. However, we may partially agree with the opinion expressed in the literature that the purpose of competent disputes to protect the principle of separation of power, is carried out by the Constitutional Court in relation to other competences.[69] In this regard, several decisions of the Constitutional Court of Georgia may be considered.[70] The decision of 25 May 2004 by which the Constitutional Court recognized the state status of the Autonomous Republic of Adjara as unconstitutional, in which case the dispute was passed between the MPs and the head of the Government of the Autonomous Republic of Adjara. The Constitutional Court has unanimously established that in accordance with Article 3 of the Constitution of Georgia, announcing the state of emergency belongs to a special board of higher state governments. Consequently, the Constitutional Court annulled the January 7, 2004 order of the head of the Autonomous Republic of Adjara and the normative grounds that allowed him to provide such acts within the Autonomous Republic of Adjara. But in this case the basis for referring to the Constitutional Court by a group of MPs was not sub-paragraph "b" of Article 89 of the Constitution of Georgia, but subparagraph "a" of the same paragraph, discussion of competent disputes was the violation of the principle of vertical divisions of the government and not the principle of horizontal divisions.

Although the Constitutional Court of Georgia does not have practice in the separation of relations between the President and the Government, however, there is some experience in general regarding the competent disputes within the Article 89 (1) (b) of the Constitution of Georgia, in particular the dispute between the members of the Parliament of Georgia and the Ministry of Education of Georgia. In the dispute a group of Georgian MPs appealed to the constitutional court to order the № 469 Order of September 30, 1997 of the Minister of Education of Georgia to determine the financing rule for preschool, primary and general school education.

A group of MPs pointed out that this was contrary to Article 94 of the Constitution of Georgia which contained that the any kind of tax or fee could only be imposed by the law, and in this case the Ministry of Education violated the Constitution and was involved in the competence of the Parliament of Georgia.[71] Based on the fact that the matter was regulated by the Minister's order, the Constitutional Court did not make a decision because the procedure for adoption of this normative act was violated and could not be regarded as a normative act, and therefore could not be judged.

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66 *Marinashvili M., Gelashvili N.,* Place of the Decision of the Constitutional Court in the System of Justice, Journal "Justice", № 3, 2007, 167-170 (in Georgian).

67 *David R.,* Modern Legal Systems of Modernity, *Ninidze T., Sumbatasgvili E.* (trans.), *Ninidze T.* (ed.), Tbilisi, 1993, 125 (in Georgian).

68 Legislation does not mean only legislative authorities, but everybody receiving or issuing a normative act.

69 *Kakhiani G.,* Institute of Constitutional Control and its Problems in Georgia: Analysis of Law and Practice, Tbilisi, 2008, 22 (in Georgian).

70 Decision of the Constitutional Court of Georgia of 25 May 2004, № 15/290, 266.

71 Decision of the Constitutional Court of Georgia of 29 January 1998, № 1/1/72-73.

It is true that in this decision the court should express more boldness, because the Constitutional Court takes into account not only the formal nature of the Act but its contents, on the other hand, the Constitutional Court has avoided making decisions on this matter.

Therefore, it is important to consider the issue, that all categories of disputes should be considered essentially in terms of competent dispute regardless of whether or not a normative act is presented as a matter of dispute. In principle it is important that all constitutional legal acts and constitutional legal real-acts (action) may become judicable within the competent dispute, otherwise the real power of separation can not be realized through constitutional justice. In addition, the expression of institutional conflicts were the decisions of the Constitutional Court № 3/122, 128 of June 13, 2000 and the Decree № 6134-139-140 of March 30, 2001. In both disputes the applicant was a group of members of the Parliament of Georgia and the Central Election Commission was the respondent. In addition, there are several judgments related to the competent dispute at the Constitutional Court, namely, April 10, 1998, № 2/53/1, which finds that the members of the Parliament of Georgia disputed the competent issues with the Ministry of Finance.[72]

Interlocutory decision of the Constitutional Court of Georgia dated November 9, 1999, № 1/7/87 should also be mentioned. This issue was a dispute between members of the Parliament of Georgia and the President of Georgia that he violated his competence. The grounds for filing a claim were also included in subparagraph "b" of paragraph 1 of article 89. This is a classical competent dispute, but this time the Constitution Court shirked its responsibilities On the grounds, that the issue of the dispute in the conflict was the President's ordinances, which were adopted before the new constitution was adopted, consequently, the Constitutional Court clarified that it was not the normative act in that case, since such a decision had not been taken by the Minister of Justice. In this case, based on the formalities of the matter, the Constitutional Court avoided the relevant reasoning. [73]

Practice of the Constitutional Court has a few number of interlocutory decision in respect of competent disputes. In particular, the Constitutional Court's statistics on total constitutionality of five constitutional suits have been submitted to consider the constitutionality of normative acts with Article 89 (1) (b) of the Constitution.[74]

Therefore, it can be said that the separation of power in Georgia is not implemented by constitutional justice, not just because the court is not applied for decisions on these issues, but because the court was obviously avoiding discussions in this direction.

"The inability of the state to end the disagreements of its various organs ultimately threatens legal security and, therefore, freedom."[75] The Supreme Court of the United States has never tried to avoid conflicts among state governments. The doctrine of separation of power was recognized in 1787 not to encourage their effectiveness, but to prevent them from inclination. The goal was not to avoid disagreements, but to protect people from autocracy, through the inevitable disagreement of the divi-

[72] Decision of Constitutional Court of Georgia of 10 April 1999, № 2/53/1.
[73] Decision of Constitutional Court of Georgia of 9 November 1999, № 1/7/87.
[74] Constitutional Court of Georgia, <http://constcourt.ge/album/stat/9.gif>, [20.11.2018].
[75] *Shajo A.*, The Restriction of the Authorities (Introduction to Constitutionalism), *Maisuradze M.* (trans.), *Ninidze T.* (ed.), Tbilisi, 2003, 92 (in Georgian).

sion of power into three sections.[76] In the USA there is a 'political question' doctrine, according to which the Supreme Court of the United States may refuse to consider the case that 'the issue is political'. In practice, the Supreme Court basically refuses to discuss foreign policy issues. The American doctrine of 'political question' is less common in Germany and continental Europe. The German Constitutional Court developed its own doctrine of political question.[77] The Federal Constitutional Court of Germany does not distinguish those issues that are not subject to judicial review due to political content. At the same time, the German Constitutional Court does not avoid discussing politically important issues that may have a big impact on the political system. It can be said that the Constitutional Court of Germany became an important factor in political life. Decisions of the Constitutional Court define the frameworks of the government not only for individual cases, but also for politics and not rarely affect the content of the politics.[78]

It can be said that Georgia, as a country of continental European law, has to share a great deal of European experience and so called the issues of 'political question' should be discussed in the Constitutional Court more actively, in case of adequate preconditions, of course.

7. Conclusion

Competent dispute is the inevitable way out of division of power and it's perfect realization, which is more established in semi-presidential systems of mixed governance models, In which the functions of state power bodies are not strictly divided and it is less common in states which government systems are rigidly divided.

It can be said that the dispute between the high bodies is constitutional natural phenomenon and should not be treated as a crisis in the functioning of the government, on the contrary, all the bodies are determined to try to eliminate such incompatibilities of government functions within its competence, especially in this regard should the resource of the Constitutional Court be applied.

The Constitutional Court should review the competent dispute inherently and make decision in any possible hypothetical case, depending on the qualification of such a dispute and taking into consideration that this court is the main legal alternative of resolution of such dispute.

In addition, the Court must consider issues broadly in all cases and consider the general nature of the model of state governance, while making decision.

It is especially important to note that the practical part of the state government's constitutional organization is in the frame of the law and under the framework of such a legal primacy, the idea of constitutionalism and the principle of separation of powers is to be realized. The relevant constitutional institution, the Constitutional Court, must have the special and leading role in this process, with the competence that will ensure the consistent development of the principle of separation of the power and it's complete realization.

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[76] Ibid, 92-93, comp. Myers v. United States, 272 US 293 (1926).

[77] *Khubua G.*, Constitutional Court Justice and Policy, Journal "Review of the Constitutional Law", № 9, 2016, 5 (in Georgian).

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41. <http://constcommission.ge/1921>.

Guliko Peradze*

Geneva Conference (1904) in the Legal Context

The present article is dedicated to the First Conference of Georgian revolutionaries held in Geneva in 1904, which represents an important stage of the two decades of struggle of Georgia and its people for independence. The assembly of emigrated Georgian politicians was not paid attention by legal specialists for decades. It is possible to say that the decisions taken by political parties in this conference significantly contributed to the future tactics of national forces in the beginning of the last century. Consequently, the main task of the article is to analyse the protocols of this less known and very interesting event in legal terms and present it to the wider society. Also, it should be underlined that the study of the conference materials once again demonstrates a high level of political and legal preparation of the leadership of Georgian society at the beginning of the last century. This was well illustrated when discussing the issues such as the principles of federal arrangement of state, rights of federation subjects, quality of human rights protection in highly developed countries, knowledge of the methods to gain and protect these rights, etc.

Key words: *Geneva Conference (1904), independence, the Treaty of Georgiyevsk, Alliance Agreement, monarchical governance, autonomous unit, political party, the principles of federal arrangement of state, the rights of autonomous unit, republican form of governance, territorial autonomy, restoration of independence.*

1. Introduction

At any stage of public-political development, public experience shows that the history of the state is created by the people lived in this political unit and being created even today. For almost two centuries, the self-sacrificing struggle and labour of Georgian patriots were necessary to bring independence to Georgia again and also the right to determine its own future at the end of the 20th century.

The First Conference of Georgian revolutionaries, held in Geneva, 1904, represents an important stage of the two decades of struggle for Georgia's independence. Legal specialists did not pay attention to the assembly of emigrant Georgian politicians for decades. It is possible to say that, in the beginning of the last century, the decisions taken by political parties in this very representative and well-organised event significantly contributed to the future tactics of national forces. Consequently, the main task of the research is to analyse the protocols of this less known and very interesting event in legal terms and also present it to the wider society.

The article consists of four chapters. The first chapter is the introduction and the fourth is conclusion. The second chapter of the work examines the legal status of Georgia under the Treaty of 1783 and legal consequences of its violation by the Russian Empire. The first part of the third chapter represents the reaction of Georgian society to loss of statehood of Georgia and dividing the principalities into Russian provinces (Kutaisi and Tbilisi provinces). The second part of the third chapter is based on

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the conference protocol, which demonstrated the vision of political parties participating in the conference and about the measures taken by Georgia to obtain the status of an autonomous unit within Russia. And finally, the third part of the third chapter is dedicated to the delegates' views on the conference, such as principles of federal arrangement of state and the rights of autonomous units in its composition. The results of the survey are presented in the fourth chapter of this article.

2. Legal Status of Georgia under the Treaty of 1783 and after Its Entry into Force

Despite the fact that Georgia had many strong enemies for millennia, it had always managed to maintain its statehood. The country still faced up to a difficult choice in the second half of the eighteenth century. Some strong Muslim states such as the Persian and Ottoman empires were fighting against each other for conquering Georgia. Russia was looking forward to a favourable moment to subordinate Georgia under maximally convenient conditions.

It was correctly mentioned by the Academician *N. Berdzenishvili* that Russia was dissatisfied with the strengthening of *King Erekle-II's* position in the region. Georgia had successes in its relationship with Muslim states and political unions to regulate the relationship, while Russia was trying hard to create artificial obstacles for Georgians from pursuing their goals.[1] It was not in Russia's interest to strengthen the independence of the Georgian state and its relations with Persia and Turkey.[2] On the contrary, Russia was interested in weakening the Georgian state as much as possible and keep it highly dependent on Russia's assistance.[3]

In fact, developments around Georgia in the last quarter of the eighteenth century were the result of the effective steps which Russia took in this direction. As it is known, *Erekle-II* received a written offer from the Russian government in 1782 to start negotiations and the Kingdom of Kartli and Kakheti was under Russian patronage. At the same time, in case of consent, they were also asking *King Erekle-II* to present an official request for protection.[4] As we have already mentioned above, the proposal was preceded by deliberate and long-term activities of the Russian authorities and *Erekle-II* was forced to connect the fate of his own kingdom to the Russian Empire because of active enemies within the country (peerages, *Paata and Alexander Batonishvili*) and without. Also, according to Russia, *King Erekle-II* should be the initiator of the Alliance Agreement.

An official request for accession to Russian patronage was sent by *Erekle-II* on 21 December 1782[5] and the Emperor of Russia satisfied the request. A very significant agreement was signed on 24 July 1783 in the fortress of Georgiyevsk. The name of the contract is known as the Treaty of Georgiyevsk and its legal nature was determined with 13 main and 4 separate articles.

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1 *Berdzenishvili N.,* Essays of Georgian History, Vol. IV, Tbilisi, 1973, 169 (in Georgian).

2 In this regard, negotiations made by *King Erekle-II* to Turkey's Sultan are notable. By that time, as Russia's ambassador in Turkey informed his superiors, Georgians were negotiating with Turkish authorities to get millions in credit. According to the Ambassador, in case of successful negotiations, the Georgian side was ready to refuse Russian alliance, *Surguladze I. I.,* History of Georgian State and Law, Tbilisi, 1968, 114 (in Georgian).

3 *Metreveli V.,* History of Georgian Law, Tbilisi, 2004, 191 (in Georgian).

4 Ibid, 192.

5 *Berdzenishvili N.,* Essays of Georgian History, Vol. IV, Tbilisi, 1973, 689 (in Georgian).

The alliance of agreement started with the preamble in which the emphasis was on the connection between the Russian Empire and the co-religionist Georgian state over centuries. Moreover, it included their good neighbourly relations and aims, which led to the conclusion of the agreement. The following are the contents of specific articles of the agreement:

According to the first article, Georgia refused to work independently with other countries and recognised Russia's supremacy. In the second article, the Emperor of Russia pledged to protect Georgia and help to return lost territories. By the virtue of the third article, the Emperor of Russia's permission was necessary for accession to the throne of Georgia.

The fourth article of the treaty was about foreign relations and Georgia was forbidden from establishing relations with other states without the agreement of the resident of Russia. Under the fifth article, Georgia and Russia would change their representatives to the king's throne. The sixth article of the treaty is very important, according to which the Russian emperor should not interfere with Georgia's internal affairs, *King Erekle-II* and his descendants would remain representing the royal throne and an enemy of Georgia would be the enemy of Russia. In the seventh article, *Erekle-II* took the responsibility of helping Russia with the army of Georgia if needed. Under the eighth and ninth articles, the *Catholicos of Kartli* would become a member of the Russian Synod and Georgian nobles were given equal privileges as Russian nobles. The tenth article was about the issue of free movement of Georgian nobility in Russia, the right to resettle there, prisoners' redemption and resettlement in Georgia. The eleventh article provided benefits for Georgian and Russian merchants in both countries. The twelfth article referred to the term of the contract, according to which the agreement would go on forever and amendments were permitted only by the agreement of the parties. According to the thirteenth article, the agreement was in force after six months from signing the treaty.[6]

As it was already mentioned, four separate articles were included together with the main articles of the Treaty of Georgiyevsk. Under the first article, the Emperor of Russia advised *Erekle-II* to have good relations with the King of Imereti for security purposes of the country and he offered himself as a conciliator. By the force of the second article, the Emperor of Russia's obligation was to have two full Russian battalions with four cannons in Georgia. Under the third article, it was defined that the head of the Caucasus Line had the obligation to act in agreement with *Erekle-II* during war. The final fourth article indicated that Russia had the obligation to protect Georgia with force during war.[7]

After reading the content of the articles, we are once again convinced of *King Erekle-II's* optimism that the agreement with one of the strongest countries in the world, along with a number of other good things, would bring peace to a long-suffering country, its inhabitants[8] and the royal throne would be retained for the successors of the king. All of this was directly underlined in the contract that the Emperor of Russia should not interfere in the internal affairs of the country and the royal throne must be inherited by the descendants of *Erekle-II*.[9]

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6 *Guruli V., Vardosanidze S.,* The Treaty of Georgiyevsk, Tbilisi, 1983, 20-21 (in Georgian).
7 Ibid, 21.
8 Ibid, 20-21, see: main article 2nd and separate articles 2nd and 4th.
9 Ibid, 20-21, see: main articles 3rd and 6th.

It is noteworthy that until today there are different views and opinions about the alliance agreement made between Russia and Georgia in 1783 and about its legal nature. For example, some scholars think that the legal document was not based on the principle of equality of the parties and Russia established a protectorate of Georgia with the help of the agreement.[10] Another school of thought discussed the treaty, and is still reviewing it, as "the Act of Protectorate and Vassal".[11] An interesting opinion was expressed by Professor *W. Tsereteli* about the legal status of the Georgian state, which was based on the Treaty of Georgiyevsk. He believed that by virtue of the union agreement, Georgia would have remained a semi-independent state which would have full freedom of internal governance.[12] As for Academician *Ivane Javakhishvili*, he evaluated the Treaty of 1783 as a "friendly agreement on relationship and protection," according to which the Kingdom of Kartli and Kakheti would become "sovereign but dependent".[13]

The issue on which all parties agree with is that treaties like the Treaty of Georgiyevsk were not alien for the international law of feudal era. As a rule, by using this method, weak states were often under the protection of strong states[14] and, at the same time, they remained loyal to their own interests. In our case, Russia had strongly reinforced its positions in the region by Georgia's subordination. The Russian Empire certainly could achieve the same with military power but, as Professor *Ivane Surguladze* correctly mentioned, the real aim was successfully disguised by Tsarism, using religious unity and the noble mission to help the people of the same religion. That was the main factor in the success of Russian diplomacy, "to resolve the problem without violence and accordingly without sacrifice".[15] Finally, as academician *N. Berdzenishvili* noted, Russia has managed "to cross the Caucasian Mountains without war and achieve very favourable conditions to its south".[16]

Another issue is the fulfilment of the hopes of the Georgian side, viz., getting rid of the aggression of Muslim states, regaining the lost territories and restore the united Georgian state.[17] Unfortunately, as time has shown, real intentions of the Russian Empire were far from fulfilling its obligations. The expectations of Georgia did not come true and its status at international level became more complicated. The aid that the Russian Empire promised to *King Erekle-II* was not fulfilled during his lifetime.[18]

On the contrary, despite many requests from Georgia, the Russian army left the kingdom exactly when *King Erekle-II's* relationship with neighbouring Muslim political units was tense in 1787 because of the alliance agreement with Russia. With this action, Russia harshly violated the most important arti-

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10 *Berdzenishvili N.,* Essays of Georgian History, Vol. IV, Tbilisi, 1973, 691-693 (in Georgian).

11 Ibid, 196. See also: *Surguladze I. I.,* History of Georgian State and Law, Tbilisi, 1968, 116-118 (in Russian).

12 *Sidamonidze U.,* Historiography of the Victory of Bourgeois-Democratic Movement and Socialist Revolution in Georgia, Tbilisi, 1970, 219 (in Georgian).

13 *Berdzenishvili N.,* Essays of Georgian History, Vol. IV, Tbilisi, 1973, 692 (in Georgian). Also: *Javakhishvili I.,* Dependence between Russia and Georgia in the XVIII Century, Tbilisi, 1919, 25-32 (in Georgian).

14 *Berdzenishvili N.*, Essays of Georgian History, Vol. IV, Tbilisi, 1973, 693 (in Georgian).

15 *Surguladze I. I.*, History of Georgian State and Law, Tbilisi, 1968, 114 (in Russian).

16 *Berdzenishvili N.,* Essays of Georgian History, Vol. IV, Tbilisi, 1973, 693 (in Georgian).

17 *Metreveli V.,* History of Georgian Law, Tbilisi, 2004, 196 (in Georgian).

18 Despite the fact that the Georgian side had been always informing the Russian commander in advance about possible threats.

cle from the agreement, viz., to protect its own ally with arms during war. It can be said that the next betrayal by Russia was in 1795, during the invasion of *Agha Mohammed Khan*, which was fateful for the country. Despite repeated requests, the Russian army trooped into Tbilisi only after a long delay when the capital of the country was burnt and looted by the Persians.

After the death of *Erekle-II*, one of the most important conditions in the 1783 agreement was also clearly violated, viz., governance by the ancient *Bagrationi* royal dynasty in Europe was finally over.[19] Based on the manifesto published on 18 June 1801, Georgia was (considered Kartli and Kakheti) "declared as a Russian province" and the state management functions had gone into the hands of Russian officials sent from Saint Petersburg.[20] Such changes naturally caused dissatisfaction among Georgian people, which in the first period of Russian governance became the reason for armed confrontation.[21]

It should be noted that representatives of the royal family, nobility and the relatively low level of social layers, such as citizens, craftsmen, peasants and others, participated in the confrontation. This once again proves the correctness of the opinion expressed in scholarly literature that these speeches are primarily important for considering its political, national libertarian nature.[22]

It is also correct to evaluate that such developments gave a push to activate political and legal opinions in Georgia in the beginning of the 19th century. This is worthy of attention for us because frequently the views of Georgian nobility and public figures were not only about the independence of their country but also about its future political arrangements. As stated, it is especially interesting to know the ideas of the participants of the massive and well-organised conspiracy of 1832. Their future vision can be divided into three main directions, viz., restoration of feudal monarchy as before the Treaty of Georgiyevsk; introduction of constitutional monarchy; and establishing a republican model in Georgia, which was the most courageous and progressive view.

There is no doubt that one of the most visible public figures, a great Georgian educator and devoted patriot of his country, *Solomon Dodashvili* is among the supporters of the last viewpoint.

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19 Taking this into consideration, it is hard to say that decision made by the Russian authorities was fair or neighbourly after the abolishment of the Kingdom of Kartli and Kakheti. Instead of Royal throne, *David Batonishvili* had a monthly remuneration of 500 roubles, *Queen Darejani* – 300 roubles; and other princes 100 roubles. The princes, who were offended by the decision of the Emperor of Russia were moved to Imereti, the Russian Emperor deprived their lands and declared them as a state property, *Surguladze I. I.*, History of Georgian State and Law, Tbilisi, 1968, 114 (in Russian).

20 Later, the same fate was shared by the rest of the country: Kingdom of Imereti was merged into Russian Empire in 1810, Guria – in 1826, Samegrelo – in 1857, Svaneti – in 1858, and Abkhazia – in 1864, *Chkhetia Sh*., Russian Governance System in Georgia (1840-1846 years), Moambe of Georgian State Museum, *Aphakhidze A.* (ed.), XII-B, Tbilisi, 1944, 111 (in Georgian).

21 We mean rebellions: Kakheti — in 1802; Mtiuleti — in 1804; another rebellion in Kakheti in 1812, which spread out soon in Kartli and according to an official report 1,146 soldiers died in suppressing the rebellion; rebellion in Imereti — 1810, 1819-1820, etc., *Surguladze I. I.,* History of Georgian State and Law, Tbilisi, 1968, 221 (in Russian).

22 *Chkhetia Sh.,* Russian Governance System in Georgia (1840-1846 years), Moambe of Georgian State Museum, *Aphakhidze A.* (ed.), XII-B, Tbilisi, 1944, 113 (in Georgian).

3. The Idea of Fighting for Autonomy in Georgia in 19th and 20th Centuries

3.1. The Legacy of the Idea of Fighting for Autonomy – the Way from *Solomon Dodashvili* to the Geneva Conference

In spite of the fact that the conspiracy of 1832 was unsuccessful and its participants were brutally beaten by Tsarism;[23] it was the first time when the famous Georgian thinker and public figure *Solomon Dodashvili* (1805-1836) made a statement: "taking into consideration the existing reality, the prominent patriots of the country should abandon the unattainable dream of restoring the monarchy and apply their efforts to achieve national autonomy within the Russian Empire."

With his statement, *Solomon Dodashvili* offered us his own view about Republican Georgia, considering the reality created in the first half of the 19th century. As a researcher of the life and thoughts of this greater thinker, Professor *J. Putkaraia* notes that, "according to the model of *Dodashvili*, Georgia would remain a part of Russia. However, the national-state rights characteristic to an autonomous entity must be granted to it. As a step forward, it should be assessed that, in *S. Dodashvili's* autonomous republic, there was no place for monarchical governance and the country should refuse the institution of monarchy forever. However, the author found it possible that a representative of the royal family of *Bagrationi* held a high-ranking position in the Republic of Georgia and took part in the civil administration of the country, in its executive authorities, "the legislative and judicial authority should be gained by people.[24]"

Very briefly, this was the first speech containing the request for a republican form of governance in the history of Georgian political thought, which became the guide not only for *Solomon Dodashvili's* contemporaries but also for generations of the National Movement in the second half of the 19thcentury and in the first quarter of the 20thcentury.[25]

We consider that one specific expression of the above-mentioned is the First Conference of Georgian revolutionaries held in Geneva in the beginning of the 20th century, in particular during 1-7 April 1904. At first, 26 delegates were to attend the conference but finally 21 members attended it[26] where the future arrangement of the Georgian state was one of the key issues discussed. These dele-

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[23] In total, 145 people were arrested. After the trial, they were exiled to distant Russian provinces for various periods. *Solomon Dodashvili*, who was among them, was sentenced to permanent resettlement in Viatka. He was appointed as a penman. However, due to hard labour and after 18 months imprisonment in the barracks of Avlabari, his weakened body could not survive the north's harsh conditions and died in 1836, at the age of 31, suffering tuberculosis. Unfortunately, his family members shared his hard fate. His juvenile daughter — *Ana Kobiashvili* died in Viatka in 1838. *Constantine*, the son of *Solomon Dodashvili*, died on his way back to homeland after his father's death. In 1838, his wife *Elene Kobiashvili* died, too. Only *Ivane* survived from *Dodashvili's* family. After a century and half of his death, grateful descendants reburied the devoted patriot's remains in the Pantheon of Mtatsminda in 1994.

[24] *Putkaraia J.,* Political and Legal Views of Solomon Dodashvili, Tbilisi, 1997, 85 (in Georgian).

[25] Ibid.

[26] *Shvelidze D.*, Originating Political Parties in Georgia – Federalists, Tbilisi, 1993, 127 (in Georgian).

gates "for reasons easily understandable"[27] are referred to only by pseudonyms instead of their real names in the conference protocols, published in 1905 as a book in Paris, by the famous Georgian public figure *George Dekanozishvili*;[28] however, it is not difficult to determine their party affiliation. They expressed the positions of the most popular political parties in Georgia at that time, namely, a group of social federalists who were united around the editorial board of Georgian language newspaper "Georgia", which was published in Paris in 1904-1905; Georgian anarchists who were companions of *Varlam Cherkezishvili*; representatives of the Menshevik wing united around *Noe Zhordania*; members of Russian Social Democratic party; and Georgian socialist revolutionaries (revolutionists).[29]

The organisers of the conference intended to find out the following: "1. What the Georgian revolutionary factions were thinking about national issues; and 2. is it possible to unite them on the issue of national soil, in particular under the flag of Georgia's autonomy."[30] Consequently, the main task for them was to provide Georgian politicians both in Georgia and outside the country with the opportunity to judge the country's future in a free environment, far away from "Okhranka" agents and Russian censors. It was an attempt to enable them to show their own vision on important issues such as the independence of Georgia, advantages and disadvantages of the autonomous and federal arrangement of the state, "the peasant question", "workers question", tactics of the revolution, the issue of dependence with different parties, etc.

As expected, one of the main issues was the matter of releasing Georgia from the Russian Empire. Moreover, Georgians were not alone in this aspiration. The delegate elected as the chairman of the conference with the pseudonym 'Kartleli' said, "every nation of the Russian Empire is fighting against Russia's supremacy in order to gain freedom. The Russians are fighting, Poles and Armenians are also fighting and we, Georgian people, are fighting too."[31] At the same time, the chairman expressed his hope that, despite the party affiliations of the delegates who arrived to participate in the conference, they will be able to agree with each other's positions about specific issues "after a brotherly and friendly argument".

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27 Law enforcement authorities were searching for the majority of delegates in Russian Empire. Concerning pseudonyms, the list looks like as follows: Chairman – Kartleli (*Giorgi Dekanozisvhili*), Secretaries: Tergeli (*Mikhako Tsereteli*) and *Tsangala*; delegates: *Deviani* (*Noe Jordania*), *Mtieli, Efremidze, Manaveli* (*Varlam Cherkezishvili*), *Vermitsanidze* (*Alexander Gabunia*), *Orgayan* (*Commando Gogelia*), *Gorgeladze*, *K. Anvili*, *Sabueli* (*Archil Jorjadze*), *Morbeladze*, *Liakhveli*, *Ckhrarjuladze*, *Rashadze*, *Faliani*, *Saba*, *Neidze*, *Tezreli*, etc; See: Protocols from the first conference of Georgian revolutionaries, Paris, 1905, 257 (in Georgian); Also: *Shvelidze D.,* Originating Political Parties in Georgia – Federalists, Tbilisi, 1993, 127-129.

28 Ibid, 126.

29 Defender of Peasant's interests, heirs of Georgian *Khalkhosnebi*, socialist-revolutionaries' involvement in the conference is directly indicated in the manual "Protocols from the First Conference of Georgian Revolutionaries", Paris, 1905, 38 (in Georgian); It should be noted that the members of this party were dramatically separate as social-democrats: "whose ideal is the state embraced by the central authority", as anarchists "who are refusing all kind of government", which considered to be prematurely early for Georgia. Consequently, they preferred "State with government" but "the government ought to be decentralised", see: Protocols from the first Conference of Georgian Revolutionaries, Paris, 1905, 43 (in Georgian).

30 *Shvelidze D.,* Originating Political Parties in Georgia – Federalists, Tbilisi, 1993, 127 (in Georgian).

31 Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 11 (in Georgian).

Unfortunately, his expectations were not justified and the first one to refuse to make common decisions with anarchists and social federalists was *Noe Zhordania* (*Deviani*), leader of social democrats. The vision of the conference organisers was unacceptable to him and his fellow party members and they left the event on the next day. The leader of the group explained the reason for leaving the conference: "… if we knew that we would have to make common resolutions, we would not have come because we cannot make common resolutions with the group of "Georgia" and anarchists. You want common resolutions. So, we are going."[32]

Varlam Cherkezishvili, who participated in the conference with the pseudonym *Manaveli*, was surprised by the narrow party vision of the Social Democrats and his attitude to *N. Zhordania* and his supporters was expressed as follows: "Why do you think that in this conference the enemies meet each other! I thought that we came here as Georgian friends, to make our Georgian cases. …I came here not as a socialist but as a Georgian."[33]

Such approach to the case from *Varlam Cherkezishvili*, who was loyal to socialist issues, was conditioned by the situation in Georgia, which was alarming from his point of view. "I think if Russia's current policy lasted for another 20 years and if Russia also uses all opportunities it has, Georgian people will completely lose the soil on which its future should be built. Do not forget that we are a small nation, culturally unprepared for the economic and political struggle by which Russia is going to fight and it will not step back before achieving its goal."[34]

It can be said that, after Social Democrats left the meeting, the conference continued to work with this spirit and after long discussions about different topics, they made right decisions, the first of which was to find a way out from the difficult situation of the country.

3.2. The Vision of Representatives of Various Political Parties about the Measures to Gain Autonomy

Although all agreed to the necessity of taking effective measures to extricate the country from a difficult situation, there was a great discussion to develop a common position. It should be said that the statement "we must drive out Russians," which first appeared during the Revolt of Kakheti, 1832, was shared by all people. The vast majority of attendees agreed that it would be impossible to achieve this goal independently, without contacting other people who were enslaved by the Russian Empire.

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32 Ibid, 36.

33 Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 29, 37 (in Georgian). It should be noted that the conference adopted individual resolution about social-democrats, in which express sadness for the existence of factions between Georgians, "which refused to participate in the first free conference and consider Georgian people's urgent issues with the revolutionary group". See also: Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 75-76 (in Georgian).

34 Ibid. 20-21. "Disobedient'' patriots and social democrats as well as outside enemies brought no less harm to national liberation, which made the situation more complicated. They were representing as Bolsheviks, as Mensheviks, blindly following sedition of the Russian social democratic party: eliminate distinction between classes, workers movement consolidation and creation of united proletarian state. They were refusing importance of national issues. They preferred centralism than federal arrangement of the state. See also: Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 48-50, 54 (in Georgian).

Social revolutionaries stated in their reports: "We find it unnecessary and dangerous for Georgians to stand alone against the government of Russia." In this case, the Russian government "would give the Georgian movement a national character and then it would be easier for them to destroy our nation. Because of this we need to act together with Russian parties against the common enemy's government."[35]

One of the delegates, *Vermitsanidze*, supported the necessity to fight for autonomy with other nations that were forced to merge into Russia.[36] According to his vision, Georgians had enough allies in such a fight. He said: "Every nation within the Russian border is in favour of national autonomy,… and we should try to overthrow absolutism with the power of revolution together with others; then all the nations must gain autonomy and the unity of these autonomies must be federal."[37]

In addition, it is noteworthy that the leaders of the political parties that were represented at the conference were trying to regain freedom and independence through diplomatic means. From their point of view, the best way to do so was the Treaty of Georgiyevsk, signed between Georgia and Russia in 1783. The vast majority of the parties in the country did not share the opinion that the treaty lost its power. On the contrary, they connected the idea of restoring Georgia's political and territorial autonomy to the treaty – "our flag represents Georgia's agreement with Russia". The flag states: "Georgia is territorial autonomy."[38]

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35 Ibid, 43.

36 It should be noted that an interesting discussion was held between conference participants about methods of goal attainment. They agreed about the possibility to carry out terrorist acts against odious "public servants, factory or land owners in case of necessity to gain autonomy of the country. At the same time, they condemned the allocation policy of specific persons for such acts. For example: As the delegate *Tergeli* noted in his speech: "I think it is impossible to establish an executive committee for the execution of terrorist acts. Terror is an individual act and the revolutionary is able to sympathise with a terrorist whose personal matter was to carry out that opinion", Protocols from the first conference of Georgian revolutionaries, Paris, 1905, 208 (in Georgian). Delegate *Vermitsanidze* had the same opinion: "Terror – it is a personal matter that cannot be condemned by any revolutionary. And the governing of terror organization is not in the revolutionary sphere", Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 209 (in Georgian); *Archil Jorjadze* was also against the appointment of special persons or the creation of special organs to carry out terrorist acts. He said: "A central organisation is not required to commit terrorist acts. But if bounded people endeavour to take arms to gain freedom, we are obliged to tell them that it is their holy duty", Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 212 (in Georgian); *Varlam Cherkezishvili* had an interesting position about this issue. He was sharing the views of the delegates. He assumed that "appointment of individuals for committing murder is disastrous. Moreover, it kills enthusiasm". With the deep faith of Georgian politicians, "People should not be encouraged to commit murder, but rather persuade peoples' conscience and spread awareness that the overthrow of the government is possible only by force", Transcripts from the First Conference of Georgian Revolutionaries, Paris, 1905, 214-216 (in Georgian); According to delegate *Tergeli*, the basis of the attitude of Georgian patriots towards legal institutes (such as crime and punishment) must be sought in government and its legislation, according to the laws: "who must be punishers are punished and punishers are those who must be punished", Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 143 (in Georgian).

37 Ibid, 178.

38 *Chkhikvishvili G.,* National Democratic Party of Georgia in the Fight for Nation-State Independence, Tbilisi, 1992, 6-7 (in Georgian); See also: *Gvazava G.,* Our flag, Newspaper "Georgia", № 51, 1917, 3-4 (in Georgian).

The discussion of *G. Gvazava* is very interesting regarding this issue. He justified Georgia's right historically and legally to restore independence. *G. Gvazava* clarified that, in the 18th century, Georgia was politically united and with this status the country became a protectorate of Russia. The latter assumed the responsibility to return the lost territories to Georgia. Accordingly, Georgia's freedom and integrity of territory was determined by the treaty of 1783.[39]

G. Gvazava refers to the issue of restoration of Georgia's independence and its significance. He notes that the restoration of the statehood of Georgia was not an issue for Georgians alone, but it was an international issue.[40] In this regard, it is interesting to point out an opinion from one of the English newspapers, which indicates that "the basis for submitting complaints by Georgians was the 1783 treaty and also the fact that the last king of Georgia refused to rule royal government in 1801. In both cases, Russia agreed to respect Georgian local autonomy, Georgian language and Georgian church. However, these conditions were no longer protected".[41] Furthermore, the article explains that the Georgian anarchist *Varlam Cherkezishvili* was trying to inform Europe about the fact that Georgia was not a conquered country without rights. It was forced to obey Russian rule, however Georgia had rights and was still a party to the contract. The rights were usurped by the stronger partner and then Georgia asked for help to restore those rights.[42]

Varlam Cherkezishvili tried to strengthen the position of the speakers with historical arguments. He addressed the participants of the conference: "Dear friends, do not forget that Russia did not conquer us, but we joined it with an agreement. We have the right to talk to the Russian government, as free states talk to each other. If the imperialists do not consider the fair demands of Georgian people, let us declare war on Russia, based on the norms of international law. Right now, we can set up an independent governance committee of Georgians… Can you see, what kind of rights do we have? Why should we reject our rights?"

When *W. Cherkezishvili* found out that the participants were surprised because of his statements, he tried to explain his words: "You are surprised that I am speaking about governance whereas I am an anarchist. But tell me, why should we refuse our rights without fighting? If we defend our rights, Europeans will never accuse us. They will say that we are the ones who were fighting against the country who invaded Georgia by force. People should not refuse their rights. We need to get new rights and not lose old ones. We can claim autonomy from Russia in accordance with existing rights."[43]

It should be noted that the example here is not the only one from *W. Cherkezishvili's* biography when he left the principles of anarchism in favour of the interest of his homeland. A similar case was repeated later when Georgian political circles discussed the issue of participation in the Russian Duma elections. As one of the leaders of social federalists and the first Minister of Education of independent

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39 *Sidamonidze U.,* Historiography of the Victory of Bourgeois-Democratic Movement and Socialist Revolution in Georgia, Tbilisi, 1970, 214-215 (in Georgian).

40 Ibid, 215.

41 *M. N.,* Recollections of W. Tcherkesoff, Freedom, 1925, December, 48.

42 Ibid, 49.

43 *Sidamonidze U.,* Historiography of the Victory of Bourgeois-Democratic Movement and Socialist Revolution in Georgia, Tbilisi, 1970, 179 (in Georgian).

Georgia *George Laskhishvili* (1866-1936) recalled in his memoirs, "For all of us it was surprising that *W. Cherkezishvili* was against the refusal of participation in the Duma election. No one expected from him this kind of position and it was even amazing". The reason for the surprise of the public was the fact that *Varlam Cherkezishvili's* opinion about the parliament was well remembered by everyone. A Georgian anarchist explains that "the shameless institution like parliament was not created by bourgeoisie". It was "the big trade market where people are selling, where they are hypocrites and deceiving the country". Despite all this, as Mr. *George* noted, *W. Cherkezishvili* publicly urged social federalists to refuse the boycott of the elections. "You do not look at the parliament as I do, you believe in its political power, if I were you, the idea of boycott would seem insignificant. If you take into account the situation of our country, you should do your best. You should appear on the parliamentary tribunal and speak loudly about Georgia's historical right. Let Europe and the whole country understand that the Georgian nation has a historical right to live in a free and independent country. Do not you know that your opponents – social democrats –are going from Georgia as the representatives of our country? And they will not say even one word about the historical right of our nation. If I were you, the idea of boycott would not be attractive for me even for a second" – a senior friend told his young compatriots.[44]

Unfortunately, an experienced politician's prophecy was fulfilled later. On 3 December 1912, at the session of the Russian Duma, when *Varlam Gelovani*, a deputy from Kutaisi province, demanded autonomy for Georgia, he was attacked by Georgian social democrat deputies. *Karlo Chkheidze, Akaki Chkhenkeli* and *Evgeni Gegechkori* traduced their compatriot that autonomy was needed for him and his companions as they wanted "chauvinism to flourish" in Georgia.[45] It is not surprising that after such a harsh assessment by Georgians, the Russian Duma did not discuss the issue of Georgia's autonomy.

Unlike social democrats, the position of compatriots became the reason for compromise in the political beliefs of another Georgian anarchist *Komando Gogelia* (1878-1912). He told the participants of the conference, "I personally, do not have any favourite form of state governance. I am against any of them… So, how you can explain my being here? I will not fight for the constitution in Russia, in this I can see only the bondage of the monarchy and nothing else… We may be supportive of the federation of free societies and as long as all of these will happen, we must take part in every battle against the old governance. We are brothers to destroy the old form of governance…"[46]

Thus, as we become acquainted with the Geneva Conference materials, at the beginning of the twentieth century, a mere 14-15 years later, the anarchists known for the most anti-state views were more supportive of political forces fighting for Georgia's autonomy than the Menshevik wing of the social democrats, led by independent Georgia.

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44 *Laskhishvili G.,* Memoirs (1885-1915), Tbilisi, 1934, 254 (in Georgian).

45 State Conference Session, 13 December 1912, Newspaper "Imereti", № 75, 1912, 2-3 (in Georgian).

46 Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 188 (in Georgian).

3.3. The Views of the Geneva Conference Participants about Autonomy Units and the Federal State

"The Georgian people, both historically and naturally, morally and otherwise represent one special nation whose overall development requires a political framework which will simplify to fulfil its aspirations" – Georgian students wrote in the letter sent to the Geneva Conference. Also, they indicated that from their point of view, only in case of obtaining autonomy it would be possible to develop Georgia in a good way.[47] With the examples of the delegates' views, we will try to explain why there was such unanimity between the participants of the conference and their support for the issue of autonomy and federal arrangement of the state.

As a leader of the group within the newspaper "Georgia", *A. Jorjadze* said, he and his companions did not endeavour to establish national autonomy in Georgia after the overthrow of the government. A form of state which will contribute to the country's further cultural restructuring would be acceptable. "For this we join the other parties of Russia and other nation parties in Russia which are fighting against political centralism like us and all of whom are willing to grant all nations the status of autonomous republic which will be connected to each other federally instead of establishing one integral democratic republic. Today we are revolutionary autonomists and federalists" – said the leader of the Georgian national movement.[48]

As for the issue of the concept of autonomy for *A. Jorjadze*, we say it in his words that "it was a defined state institution, which made and passed the laws through parliament" and the existence of such an institution "was necessary for the protection and development of our national culture."[49] Even though *A. Jorjadze* believed that the parliament could not provide "the realisation of the ideals of socialism", it could still bring great prosperity for the public. "Sovereign of people", recognition as human, freedom of speech, gathering, faith and press – all this is a big treasure which was created by developed humanity with the help of free political forms. We do not deny it, on the contrary we want all these things to establish in our country… national self-governance, 'home rule' will protect our national identity and create cultural conditions for its development…"[50]

During the conference, *A. Jorjadze's* views were shared and further expanded by the delegate *Vermitsanidze*. It is true that he did not elaborate about the country's future models of autonomous and federal arrangements. However, he introduced to the delegates all the basic principles that will be the basis for such political formations. According to him: "1. A full democratic regime should be established with extensive local self-government; 2. All non-Georgian nationals who live in Georgia should be allowed to satisfy their cultural, civil and other needs without delay; 3. Faith should be regarded as a private affair, a matter of man's conscience; 4. It is necessary to eliminate the conditions by which the revival and connection of free associations are hindered; and 5. It is necessary to remove conditions which restrict private and collective initiatives."[51]

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47 Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 45 (in Georgian).
48 Ibid,63-64.
49 Ibid, 55.
50 Ibid, 57.
51 Ibid, 59.

The optimism that their plans were fulfilled was realistic for Georgians because the idea of national autonomy was popular not only in Georgia but also among other people who were conquered by Russia. We can read the same in the conference protocols as follows: "Poles do not want only autonomy, they want full independence!"… So, Poland is a great power to fight against the absolutism; Finland lost its autonomy yesterday and of course, will support this autonomy; In Ukraine (small Russia) the idea of autonomy is very common. Neither Armenians nor the other Caucasian nations will refuse this idea. As for Russia, the most powerful party in this country and its representative organ 'Osvobozhdhane' is hesitant on this question; Social-revolutionaries are obvious federalists; who was left in the camp of our opponents? – Russia's social democracy, Russian nationalists and the Russian government. What can I say about social democrats and the latter is an even dangerous force. But nothing is invincible."[52] Georgian patriots who were hopeful of the fact that national liberation movements were revived in Russia's invaded nations, came to such conclusions at the beginning of the 20th century.

As for the issue of coexistence of various nations and their autonomous units in the federal state, participants of the conference considered that this kind of unity was possible only in case of equality of federation subjects. It is noteworthy that for them declaring the idea of equality only at the legislative level did not mean that it would be realised in real life. To confirm this, they borrowed specific articles from the Austrian constitution, according to which: "Every race in the state was equal to the law. In particular, all of them had the right to protect their nationality and language. Equality of languages in the state schools, state institutions and public life was recognised by the state. In places where there were representatives of different races, public educational centres should function so that the representative of other countries must not be obliged to learn foreign languages. All races must receive education in their own languages, etc."[53]

Despite such good laws, the national question was not less intensive in Austria than in Russia. The reason was the fact that the requirements of the law were not fulfilled. There, as well as in Russia, "one nation was dominant and benevolent". Other nations should be satisfied with its "leftovers", which was incompatible with the principles of autonomy and federalism in the view of Georgian politicians. "National self-esteem, pride – we read in the conference protocols – it is a fact and it should not be forgotten when they are talking about national question; they should know that no one will be satisfied with the leftovers of other."[54]

Another great patriot of the last century, *Mikhako Tsereteli* (1878-1965), shared the common spirit of the participants of the Geneva Conference and believed that the federal arrangement of the country was "the essential form to create renewed humanity"[55] and focused on the necessity of equality and willingness to cooperate. Georgian politicians thought that it was not necessary to talk about federalism when you are told that your brotherhood does not help them, they are your enemies or the friends of your enemies or "when you are speaking about this issue "fellow-man" is looking at the for-

[52] Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 74 (in Georgian).
[53] Ibid, 71.
[54] Ibid.
[55] *Tsereteli M.,* Seize State Force and Social Revolution, Tbilisi, 1906, 97 (in Georgian).

est while reading the gospel".[56] It was deeply believed by Georgian politicians that federation and autonomy can be discussed only when there are full consent and mutual respect for the joint issues between the federation subjects.

It can be said that the same principles were based on a resolution adopted by the conference after a long discussion. According to it: "The conference recognises that the evolution of humankind is directed towards the unity and solidarity of the free nations; The autonomous nations federation is the best form for their consent and this is the best soil for social, mental and moral developments of these nations; This federation is also a reliable source of economic equality; and Despotism of Russia makes it impossible the implementation of these aspirations that our direct duty is to overthrow this despotism with a revolutionary struggle together with Russians and those people who are living in Russia and support this idea. Georgian Revolutionaries Conference rejects separatism, which is not considered to be the guarantee of solidarity and the social development between the nations and states. The best and the most necessary political goal for independent Georgia should be Autonomous Georgia, federally connected to other nations".[57] Hereby, we can assert that this resolution, which was adopted at the 4 April session of Geneva Conference, was supported by 29 delegates. One delegate did not participate in the ballot.

4. Conclusion

It can be said that, through the 1904 Geneva Conference Protocols and the materials which were less-known to the society, we tried to represent the positive and negative parts of fighting for Georgia's independence by Georgian people in 19th and 20thcenturies. As in other countries, this process was not easy and faultless in Georgia. However, in the 1930'sthe loyalty to a properly defined orientation can be considered as one of the main features of this movement.

We have studied and demonstrated this very representative assembly held by Georgian patriots in Europe in this respect. As expected, the vast majority of participants (except Mensheviks) once again confirmed the dedication of *Solomon Dodashvili* and loyalty to the autonomy supported by the best patriots of the country and determined the correct tactic for achieving the goal.

It should be underlined that the study of the conference materials once again demonstrated a high level of political and legal preparation of the leadership of Georgian society at the beginning of the last century. This was well illustrated when discussing the issues such as principles of federal arrangement of state, rights of federation subjects, quality of human rights protection in highly developed countries, knowledge of the methods to gain and protect these rights. All the above mentioned had a positive effect on the events taking place inside and outside the country and the correctness of the conclusions based on it. Here, we mean the clauses of the conference's resolutions, viz., rejection of separatism, strengthening connections with Russians and other people living in Russia and establishment of an autonomous Georgia as a part of the federation of liberated nations through common effort.

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[56] *Tsereteli M. (Alarodieli),* Guide Friends, Newspaper "Sakartvelos Moambe", № 4, 1909, 7 (in Georgia). *M. Tsereteli,* not only Russia, but also the most popular project in the early twentieth century, the Subjects of the Caucasus Federation, was taking into consideration.

[57] Protocols from the First Conference of Georgian Revolutionaries, Paris, 1905, 183 (in Georgian).

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16. *Tsereteli M.,* Seize State Force and Social Revolution, Tbilisi, 1906, 97 (in Georgian).
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Zoia Khasia*

Standards and Practices of Serving the Sentence by Persons with Disabilities

This article discusses the specificities of serving a sentence by persons with disabilities (hereinafter – PWDs) and the new approaches aimed at addressing this issue, which would enable the Georgian penitentiary system and the legal framework regulating the system to introduce the latest, international standards oriented approaches and to provide PWDs with the conditions of serving a sentence in line with their needs and on equal basis with other prisoners.

The creation of reasonable accommodation and accessible environment for persons with disabilities is new to the society, in general, since it was mainly introduced in 2006 when the Convention on the Rights of Persons with Disabilities[1] was adopted. Georgia ratified the Convention in 2014, therefore the national legislation, the practice and legal framework regulating the penitentiary system require many novelties, changes and regulations in this regard.

This material is based on the analysis of the existing practice and legislation, which at present fails to create the environment of serving a sentence based on the protection of honour and dignity of persons with disabilities.

Key words: *Persons with Disabilities, Penitentiary System, Reasonable Accommodation, Adapted Environment, Penitentiary Establishment, Barrier, Treatment, Status Determination, Punishment, Conditions.*

1. Introduction

The legislation of Georgia envisages the aspects, which should create an accessible environment for persons with disabilities in the country and support them in overcoming the obstacles they face in everyday societal life. However, these norms are mostly declaratory and often remain as 'dead norms'. Despite the legislative regulation, limited accessibility, unadapt environment, low level of public awareness and other external factors put PWDs at a disadvantage. These obstacles are particularly acute and painful, even discriminatory, when the PWDs find themselves in penitentiary establishments, often without vital care and services.

The role of the society in providing equitable living conditions for persons with disabilities is significant. How does the society perceive a disability? Is it a status, which is often a 'verdict' to live only behind the walls, isolated from the outside world or is it a stigma, which substantially affects the daily life of persons with disabilities? "The hindering factors come from the society, since people do not know how to treat persons with disabilities and such behavior suppresses persons with disabilities and pushes them to stay home and away from the community".[2]

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1 Convention on the Rights of Persons with Disabilities, UN General Assembly, 24/01/2007.

2 Personal Interview with a person with disability, Trainer, Representative of an NGO working on disability issues, Tbilisi, September, 2017.

The negative consequences of disability – a barrier that gets in the way of people at any stage of their life and puts them in unequal conditions with other people – can be overcome and minimized as a result of proper regulations, support and provision of services. The impact of unequal conditions is particularly strong when the person with disabilities is placed at the penitentiary establishment, in a foreign environment, without any support, in the information vacuum and in a situation where the PWDs cannot access the services and activities that other prisoners enjoy on daily basis. The absence of such care and services may be vital, depending on the condition of the person with disability. It is noteworthy that the recognition of problems of PWDs as a priority does not have a long history and is related to the adoption of the Convention on the Rights of Persons with Disabilities (hereinafter – the Convention). Therefore, the absence of clear mechanisms of regulation, the absence of mechanisms for the implementation of the Convention or the existing legislation and the low level of public awareness negatively affects any stage of life of persons with disabilities. Accordingly, in places where people serve their sentence it is even more painful and difficult, due to inadequate access to information, undertrained staff, improper medical service, lack of rehabilitation programs, etc.

However, the abovementioned cannot be considered as a defect of the Georgian system only. This is a problem that many developed or developing countries attempt to solve. The State should exercise special care to enable these people to serve the sentence, imposed by the court, in adequate conditions, and the state and non-governmental organizations conducting monitoring and research should focus on the conditions of persons with disabilities in such places.

2. Implementation of the Requirements of the Convention on the Rights of Persons with Disabilities and other International Standards in Georgia

The United Nations Convention on the Rights of Persons with Disabilities does not directly address persons with disabilities in conflict with the law and their treatment in places of deprivation of liberty, however, its role is significant in all areas of societal life. The Convention is the first document, which gave the international community a universal and structured definition of a person with disabilities.[3] It is based on the principles, such as: respect for inherent dignity, respect for individual autonomy, the freedom to make one's own choice, and non-discrimination. The definition is quite general, however, according to the preamble of the Convention, 'disability' is an evolving concept and the approach of the international community to the concept of disability should be dynamic and evolving over time.

In Georgia, a number of positive steps have been taken towards the implementation of the Convention. On October 27, 2014, the Office of the Public Defender of Georgia was named as a structural unit of monitoring, protection and implementation of the Convention. Several legislative amendments and sub-laws have been adopted. Practical steps, related to the implementation of the Convention,

[3] "Persons with disabilities include those who have long-term physical, mental, intellectual or sensory impairments which in interaction with various barriers may hinder their full and effective participation in society on an equal basis with others", Article 1, Convention on the Rights of Persons with Disabilities, UN General Assembly, 24/01/2007.

such as judicial decisions, which have been related to persons with disabilities since 2014, are especially noteworthy.[4]

Amongst several standards of treatment with prisoners, the United Nations Standard Minimum Rules for the Treatment of Prisoners[5] (hereinafter — SMR) takes a significant place in respect to persons with disabilities. The revised version of the Rules (hereinafter — the "Mandela Rules") significantly changed the part of the document in relation to the treatment of PWDs. Rapporteur on the Rights of Persons Deprived of Liberty of the IACHR[6] assessed these changes as follows: "These Rules represent a vital advance in the protection of vulnerable groups, in particular, persons with disabilities deprived of liberty. In this regard, among other provisions, the Rules require prison authorities to make reasonable accommodations to ensure that prisoners with disabilities have full and effective access to detention conditions and resources on an equitable basis".[7] The revised version of the Rules focuses on the classification of prisoners, which implies the individual needs assessment as a way to detect any risks, needs and threats. Classification systems should be flexible in order to support individualization of treatment. The Rules also covers the issues of establishing relevant environment for serving the sentence, identification of any signs of psychological or other types of stress or ill-treatment and reacting to them, and other factors.

The "Mandela Rules" calls for the prison administration to adapt to the needs of individuals with physical, mental or other disabilities to ensure their equal access to services and programs and states that "measures to protect and promote the rights of prisoners with special needs are required and shall not be regarded as discriminatory".[8]

3. National Legislation in the Context of Persons with Disabilities Serving the Sentence

3.1. Review of the Constitution of Georgia

The Constitution of Georgia does not include multiple mentions of persons with disabilities, and generally does not include a definite reference to persons with disabilities deprived of their liberty, but it should not be considered as if the issue remains outside the constitutional regulation. Although Article 11 of the Constitution[9] does not consider disability as one of the risk factors for discrimination, the Constitution of Georgia obliges the State to ensure that the rights of persons with disabilities as well as

4 Decisions of the Constitutional Court of Georgia, <http://constcourt.ge/en/legal-acts/judgments>, [09.09.-2018].

5 Rules 2, 5, United Nations Standard Minimum Rules for the Treatment of Prisoners (the "Nelson Mandela Rules"), UN General Assembly, 08/01/2016, <https://www.penalreform.org/wp-content/uploads/2016/-11/PRI_Nelson_Mandela_Rules_Short_Guide_Geo_final.pdf >, [20.09.2018].

6 IACHR (Inter-American Commission on Human Rights).

7 *Cavallaro J.,* Leading Human Rights Experts Call for Speedy Implementation of the Nelson Mandela Rules on Nelson Mandela International Day, Council of Europe, 2016, <https://www.coe.int/en/web/commissioner/-/leading-human-rights-experts-call-for-speedy-implementation-of-the-nelson-mandela-rules-on-nelson-mandela-international-day>, [06.07.2018].

8 Rules 2, 5, 6, United Nations Standard Minimum Rules for the Treatment of Prisoners (the "Nelson Mandela Rules"), UN General Assembly, 08/01/2016, <https://www.penalreform.org/wp-content/uploads/-2016/11/PRI_Nelson_Mandela_Rules_Short_Guide_Geo_final.pdf >, [20.09.2018].

9 Constitution of Georgia, 24/08/1995.

other vulnerable groups are protected in all areas of public life. The statement made by the Constitutional Court of Georgia that "the aim of Article 14 (Article 11 in the new version of the Constitution) of the Constitution is to ensure equality before the law, not to allow substantially equal to be considered as unequal or vice versa. ... The aim of the norm is much larger than the prohibition of discrimination based on the limited list provided",[10] can be attributed as an argument. Later, in the next decision, the Court explained the reasons as to why the list provided by Article 14 of the Constitution should not be considered exhaustive, saying that such an approach from the Court "would in itself confirm that any other grounds are not discriminatory, since they are not specifically covered by the Constitution. Naturally, such an approach would not be right, because any of other grounds not being mentioned in the Constitution does not exclude the groundlessness of differentiation".[11]

In this case, it is not the legislation itself that is questionable or how well it regulates the issues of treatment towards the persons with disabilities and the provision of adequate environment or how accurately the law is interpreted, but the important issue is if it covers all areas of public life, to what extent it is implemented in practice and how equally accessible these rights are to persons with disabilities. The state is obliged to protect the rights of persons with disabilities in everyday life, assist them and create appropriate conditions for those who are not actively participating in the public life due to their physical or mental disabilities. This obligation should be applied to any area of public life, including in places for serving the sentence.

3.2. Brief Analysis of the National Legislation Regulating the Penitentiary System

The Imprisonment Code of Georgia[12] discusses the standards of treatment of persons with disabilities, although it does not reflect all spheres of life of PWDs in the penitentiary establishment. In particular, the law mainly establishes that the accused/convicted prisoners with disabilities should have better living conditions and nutrition in comparison to others. However, what is meant by 'better' conditions, is not explained within the law or its sub-laws.

In spite of certain regulation attempts, in practice there is no definition of who should be considered as PWD in the penitentiary system, and what specific needs should be prescribed by law, whereas such definitions are applied by many countries, e.g. "a person who has a physical, sensory or mental impairment which has an effect on their ability to carry out normal day to day activities".[13] The definition by Prison Reform Trust[14] made in the Information Book for Prisoners with Disabilities,

[10] Citizen of Georgia, Shota Beridze and others v. the Parliament of Georgia, decision of 31 March 2008, № 2/1/392, the Constitutional Court of Georgia, 6.

[11] Political Unions of Citizens – New Rightists and Conservative Party of Georgia v. the Parliament of Georgia, decision of 17 September 2010, № 1/1/493, the Constitutional Court of Georgia, 14.

[12] Code of Imprisonment of Georgia, 24/03/2010.

[13] Sub-chapter 3.2., HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.doc>, [12.03.2019].

[14] Prison Reform Trust – PRT is an independent UK charity working to create a just, humane and effective penal system.

which, in contrast to the practice of post-Soviet countries, clearly demonstrates the ways of solving problems in regards to treatment of persons with disabilities, is also easy to understand.

In the countries where there is a problem of status determination, "the problem of determining the disability status of an accused/convicted prisoner with disability in the penitentiary system remains to be unresolved, and it makes it impossible to evaluate needs and to provide special services to the persons who had acquired disability while being in the Prison".[15] Often it is due to the lack of status that disabled prisoners do not have appropriate environment and services. However, the initial assessment of the disability can be achieved even without the status determination, in order to ensure that the conditions of serving the sentence do not only depend on the status, but are regulated based on actual needs. Apart from status determination, the list of problems also includes the absence of PWD oriented budgeting and funding in the penitentiary system, inappropriate infrastructure and living conditions, the absence of properly trained personnel, etc.

The regulation of the rights of PWDs in places of deprivation of liberty was included in the Government Action Plan for 2014-2016, which talks about the relevant conditions that provides adequate environment for serving the sentence for persons with disabilities, such as: treatment, identification of needs and improvement, access to healthcare, awareness about the rights and, in accordance with the Convention, the protection of the rights (elaboration of the social model of the approach towards remand prisoners/convicts with disabilities), creation of a special, adapted living conditions, assessment of the needs in order to improve the infrastructure in line with the specific requirements of PWDs and the creation of a physical environment considering the reasonable accommodation. This action plan obliges the penitentiary system to include the existing problems in the list of priorities and provide resources for solving it.

4. Analysis of the Practice of Serving the Sentence by Persons with Disabilities

4.1. Admission to Penitentiary Establishments

The admission to a penitentiary establishment is the first contact with the penitentiary system. This is the first stress the person is suffering by the loss of his/her freedom, which in fact, determines the success or failure of the adaptation with the penitentiary system. In his handbook *Andrew Coyle* explains the factors that may have negative influence on individuals, e.g., the admission area can be very intimidating for new arrivals to prison. To reduce this influence, he draws attention to the need for special training of the receiving staff on recognising how to exercise the difficult balance between firm control, which makes clear to the person that the prison is a well organised place, and an understanding of the stress which the prisoner is likely to be feeling as he or she moves into this strange new world. Not all staff are suited for this type of work. Those who work in the admission area "should be

[15] Public Defender of Georgia, National Preventive Mechanism: State of Rights of Persons with Disabilities in Prisons, in Institutions for Involuntary and Forced Psychiatric Treatment – Analysis of the Fulfilment of the Recommendations, 2014, 8, 17, <http://www.ombudsman.ge/uploads/other/2/2253.pdf>, [20.09.2018] (in Georgian).

specially selected and should be given specific training to enable them to carry out their work with sensitivity and with confidence".[16]

If we talk about the admission process and its importance, it differs from one jurisdiction to another, for instance: "Reception is the first opportunity to identify the special needs of prisoners. This process needs to be handled sensitively especially by communicating clearly and not making immediate assumptions about prisoners reactions".[17] The legislation of Georgia does not include the obligation to carry out the needs assessment of the persons with disabilities upon their admission to the penitentiary establishment. It includes the mandatory medical examination. Regarding the violations of the admission regulations and the failure on the first stages of imprisonment, also, the importance of the accurate needs assessment of the prisoners, we can discuss the decisions of the European Court of Human Rights, which states that "to detain a severely disabled person in conditions where she is dangerously cold, risks developing sores because her bed is too hard or unreachable, and is unable to go to the toilet or keep clean without the greatest of difficulty, constitutes degrading treatment contrary to Article 3".[18]

4.2. Allocation and Separation of Prisoners in Penitentiary Establishments

The admission of the prisoner with disabilities into the establishment and his/her needs assessment during this process represents an important matter, as the needs assessment determines the allocation of the person with disabilities in the facility most suited to their needs, where s/he is provided with equal access to all services and activities, which are available to other prisoners. The needs assessment and the allocation of the person with disabilities based on this assessment should be ensured on the legislative level. For example, "the prison administrations should take into consideration the mobility level of the prisoner, the social skills, ability to adapt to the environment, and should ensure the allocation of the prisoner, despite of the level of limited mobility, into facilities with the adequate household conditions".[19] Allocation of prisoners with disabilities in such facilities must be the main priority for prison administrations, in order to not expose the persons to a higher risk of human rights violations or other deplorable consequences. In practice, there are situations when "incarceration without requisite measures being taken within a reasonable time had resulted in a situation amounting to inhuman and degrading treatment".[20]

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16 *Coyle A., Fair H.,* A Human Rights Approach to Prison Management, Handbook for Prison Staff, International Center for Prison Studies, 3rd ed., London, 2018, 49.

17 Sub-chapter 3.1.1. and 3.1.2., HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.doc>, [12.03.2019].

18 Price v. the United Kingdom [2001] ECHR, 33394/96, Council of Europe: European Court of Human Rights, Fact Sheet – Persons with Disabilities and the European Convention on Human Rights, 2019, 3, <https://www.echr.coe.int/Documents/FS_Disabled_ENG.pdf>, [21.03.2019].

19 Sub-chapter 3.2.2., HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.doc>, [12.03.2019].

20 Z. H. v. Hungary, [2011] ECHR, 28973/11, Council of Europe: European Court of Human Rights, Fact sheet – Persons with disabilities and the European Convention on Human Rights, 2019, 4, <https://www.echr.coe.int/Documents/FS_Disabled_ENG.pdf>, [18.03.2019].

4.3. Living Conditions at Penitentiary Establishments

Admission and allocation of prisoners ensures the effectiveness of their adaptation process to the prison system. The living conditions in prison can enhance the stress caused by loss of freedom, which is particularly acute in the case of the persons with disabilities, mainly due to the fact that persons with disabilities in Georgia live in the family environment and they do not have any knowledge or experience of living independently, without the support of those people, who assist them in their daily lives. Therefore, proper individual sentence planning, through which the mentioned stress and related problems will be minimised, should be the main concern of the penitentiary system. These issues are covered in the UN handbook on prisoners with special needs, which states that prison authorities need to develop policies and strategies which address the needs of this vulnerable group in prisons. The handbook also provides that these policies "should be informed by the United Nations Convention on the Rights of Persons with Disabilities and national legislation [….]".[21]

An inadequate environment in prison influences the prisoners with disabilities not only inside the establishment, but after their release, since ensuring the adequate, safe environment, accessibility of various tools and programs in prisons has the crucial importance for ensuring the needs of the prisoners with disabilities in the facility and in the cell, as well for the effective reintegration into society upon their release.[22] The problems listed in the report of the Public Defender of Georgia on access to services in the penitentiary system of Georgia shows the lack of such policy in the Georgian penitentiary system: the access to phones by the prisoners in wheelchairs, when the phones are installed on such a height that prisoners with disabilities cannot individually dial the number; also, the height of the boxes for requests and complaints; unadapt corridors between the prisoner's cell and the walking area; inaccessible healthcare service, lack of sign language translation and Braille, etc.[23] The European Court of Human Rights considers it a violation of Article 3 of the European Convention on Human Rights if similar violations exist in practice. The court has stated, that lack of independent access to parts of the facility, including the canteen and sanitation blocks, and the lack of any organised assistance with his/her mobility "must have caused […] unnecessary and avoidable mental and physical suffering amounting to inhuman and degrading treatment".[24]

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21 *Atabay T.,* Handbook on Prisoners with Special Needs, Criminal Justice Handbook Series, United Nations Office on Drugs and Crime (UNODC), New York, 2009, 43.

22 *Vallas R.,* Disabled Behind Bars, The Mass Incarceration of People With Disabilities in America's Jails and Prisons, 2016, 10, <https://cdn.americanprogress.org/wp.../2016/07/.../2CriminalJusticeDisability-report.p>, [09.09.2018].

23 Public Defender of Georgia, National Preventive Mechanism: State of Rights of Persons with Disabilities in Prisons, in Institutions for Involuntary and Forced Psychiatric Treatment – Analysis of the Fulfilment of the Recommendations, 2014, 8, <http://www.ombudsman.ge/uploads/other/2/2253.pdf>, [20.09.2018].

24 Semikhvostov v. Russia, [2014] ECHR, 2689/12, Council of Europe: European Court of Human Rights, Fact sheet – Persons with disabilities and the European Convention on Human Rights, 2019, 5, <https://www.echr.coe.int/Documents/FS_Disabled_ENG.pdf>, [19.03.2019].

4.4. Prison Regime, Treatment and Response to Emergency Situations

Prisoners with disabilities might be at risk of being subjected to ill-treatment, by other prisoners and prison staff, because of their condition. The main reason is the lack of awareness and qualification among prison personnel, nonexistence of appropriate regulations and mechanisms, and other factors, which expose them to a higher risk. However, there are minimum requirements that the prison administration needs to ensure. Prisoners with disabilities should not only be held in a safe environment, but "they also need to feel safe, so that their mental well-being is protected, like all other prisoners".[25]

Fair attention should be paid to the policy of prison administrations regarding the specific treatment of prisoners with disabilities in cases of emergency. The penitentiary system needs to have the treatment and evacuation plan for prisoners with disabilities. In this regard, the post-Soviet countries, including Georgia, Kyrgyzstan, etc. can be considered as negative examples, as the legislation says nothing about the obligation to have specific evacuation or safety plans for prisoners with disabilities. "It will be necessary to make specific plans for the evacuation of disabled prisoners during an emergency ... These will need to be tailored to the particular circumstances of the individual prisoners and made known to the appropriate staff".[26]

4.5. The Use of Solitary Confinement and Disciplinary Measures

Frequently, the prison administration allocates the prisoners with disabilities separately, in the "solitary confinement cells". Especially, it applies to the prisoners with mental health issues, and those with restricted mobility or any other disability, which might cause some troubles to the prison administration and staff in case they will be allocated with other prisoners. Often the administration interprets such behaviour as the necessary security measure, however, such decision poses a high risk for the PWDs. The lack of special procedures poses the high risk for the prisoners with disabilities and puts their life and health conditions under the danger of complication. The National Preventive Mechanism of the Public Defender of Georgia in its report describes this faulty practice of Georgian penitentiary system. The practice of "prolonged or indefinite solitary confinement inflicts pain and suffering of a psychological nature, which is strictly prohibited by the Convention Against Torture".[27] The same interpretation can be found in various international documents, including the general comments of UN Human Rights Committee.[28]

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[25] *Atabay T.,* Handbook on Prisoners with special needs, Criminal Justice Handbook Series, United Nations Office on Drugs and Crime (UNODC), New York, 2009, 52.

[26] Sub-chapter 11, HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.doc>, [12.03.2019].

[27] *Manduric A.*, UN Human Rights Experts (Again) Push for Access to U.S. Prisons, Call for Solitary Reform, Solitary Watch, 2015, <http://solitarywatch.com/2015/07/24/un-human-rights-experts-again-push-for-access-to-u-s-prisons-call-for-solitary-confinement-reform/>, [18.03.2019].

[28] Istanbul Statement on the Use and Effects of Solitary Confinement International Psychological Trauma Symposium, 09/12/2007, <http://solitaryconfinement.org/uploads/Istanbul_expert_statement_on_sc.pdf>, [21.03.2019]. UN Human Rights Committee (HRC), CCPR General Comment No. 20: Article 7 (Prohibition of Torture, or Other Cruel, Inhuman or Degrading Treatment or Punishment), 10/03/1992.

The sensitive approach requires the use of disciplinary measures on prisoners with disabilities and the decisions should be discussed carefully with the appropriate specialists. The change of the environment, especially deterioration of the living conditions, puts a negative impact on any person and possibly a disastrous impact on the person with disabilities.

4.6. Care and Healthcare Service at Penitentiary Establishments

The existence of caretakers and ancillary personnel is vital for prisoners with disabilities, but, except for few exceptions, such members of the personnel are inaccessible for the accused/convicted persons with disabilities. According to the report of the NPM, which talks about the care of persons with disabilities, prisoners with disabilities are dependent on cell-mates and their good will, in order to satisfy the basic needs related to their physiological requirements and other daily activities. "Such an attitude puts them in an undesirable subordination and generates a risk of manipulation, which may easily turn into oppression and violence".[29] This kind of care is part of the medical service, and the right to health is recognized, regardless of the status or condition of a person – "equivalence of health care is a principle that applies to all prisoners, who are entitled to receive the same quality of medical care that is available in the community".[30] However, in spite of the guaranteed rights, the relevant health services are confronted with the criticism in different reports and decisions, for example, there are instances where the European Court of Human Rights found a violation of Article 3 on the grounds that "the authorities did not ensure the applicant's safety and appropriate treatment for his health condition".[31]

4.7. Nutrition at Penitentiary Establishments

Based on the analysis of the Georgian legislation, the administration of the penitentiary system is obliged to provide special/dietary meals for prisoners who need it for medical purposes. Such liability is guaranteed by the relevant legal act. However, none of the legislative acts consider cases where special nutritional needs are necessary not due to health conditions but are related to physical conditions, for example, when a person has mobility impairment. Such a person may not need special nutrition for medical purposes and does not fall under the regulation of this legal act. It is, however, noteworthy that due to the physical condition, proper feeding may be the main mechanism for preventing further complications. Inadequate nutrition can lead to deterioration of physical or mental health and/or creation of new problems.

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29 Public Defender of Georgia, National Preventive Mechanism: State of Rights of Persons with Disabilities in Prisons, in Institutions for Involuntary and Forced Psychiatric Treatment – Analysis of the Fulfillment of the Recommendations, 2014, 17, <http://www.ombudsman.ge/uploads/other/1/1726.pdf>, [11.09.2017].

30 *Atabay T.,* Handbook on Prisoners with Special Needs, Criminal Justice Handbook Series, United Nations Office on Drugs and Crime (UNODC), New York, 2009, 14.

31 Arutyunyan v. Russia, [2012] ECHR, 48977/09, Council of Europe: European Court of Human Rights, Fact sheet – Persons with disabilities and the European Convention on Human Rights, 2019, 4, <https://www.echr.coe.int/Documents/FS_Disabled_ENG.pdf>, [19.03.2019].

4.8. Access to Rehabilitation Programs and the Service of a Psychologist at Penitentiary Establishments

Participation in prison rehabilitation programs in penitentiary establishments is of particular importance for persons with disabilities, as along with the stress caused by the imprisonment, the person also has disabilities. One of the ways to overcome this stress is to participate in different programs. One of the main priorities of the 2016-2017 Government Action Plan of Georgia is the introduction of habilitation/rehabilitation programs for the needs of persons with disabilities.[32] If we look at the international practice, we will see that the participation of prisoners with disabilities in the rehabilitation programs and their return to the full membership of the society is the main purpose of the country's penitentiary system. For example, while reviewing the British practice, we come across documents regulating the work of the penitentiary system, which determine that reasonable adjustments must be made to the programs to allow prisoners with disabilities to participate. It is important to take account of specific communication needs in the running of these courses, "prisoners who are deaf may need a sign language interpreter present in order to take effective part in the discussions".[33] Also should be considered the role of physical exercises and sports, which can play a significant role in maintaining their health, so that "disabled prisoners should have access to sports and physical exercises".[34]

In the context of rehabilitation, educational and employment programs are significant, since on the one hand it is often possible that people with disabilities are socially vulnerable and previously did not have access to normal educational and vocational training programs. On the other hand, there are people with learning disabilities and need to be provided with appropriate training programs in order to be able to adapt to the establishment regime. The administration should assess the extent to which educational programs are accessible to the PWDs. As for employment, there are often cases when the administration unilaterally decides to refuse a person with disabilities due to their condition, where there is an expectation at an establishment that prisoners should work, disabled prisoners should have equal access to that opportunity.

4.9. Preparation for Release from Penitentiary Establishments

The early conditional release from the sentence is one of the sensitive issues and two sides should be discussed here: the convict whose main motivation is to be released early and the security of the society in which the convict is to be returned. It is noteworthy that if the prisoner returns equipped with different skills, then the possibility of integrating into society is higher. However, in most cases,

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[32] Task 4.6.9., activity 4.6.10.1., Human Rights Action Plan of the Government of Georgia (for 2016-2017 years), Ordinance of the Government of Georgia of the 21st July of 2016, № 338, 22.

[33] Sub-chapter 11, HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.-doc>, [12.03.2019].

[34] Department of Health and Prison Reform Trust, Information Book for Prisoners with a Disability, Offender Health and Prison Reform Trust 2009, 18, <http://www.prisonreformtrust.org.uk/Portals/0/Documents/-pibs/Disability%20pib%20-%20easy%20read.pdf>, [09.09.2018].

people with disabilities are deprived of trainings for developing such skills and are also deprived of the possibility of participating in further support programs after release.

The handbook on prisoners with special needs includes information about the difficulties involved in the process of release of PWDs from serving the sentence and how to resolve this issue effectively. It points out that the key area, neglected in most prison systems, is the need to assist and facilitate prisoners' transition from prison to the outside world. This can be reached by providing comprehensive preparation for release and post-release support programmes.[35] These programs should be offered not by one system only, but by the penitentiary system, probation service, social service agencies and the public, in order to avoid repeated crime and other adverse consequences, especially considering the difficulties in which the persons with disabilities find themselves after release.

5. A Short Excursion of International Practice

In many cases this Article recalls the successful practice of Great Britain where the rules of treatment of persons with disabilities are detailed in a special order that explains: "the Prison Service will ensure that prisoners with physical, sensory and mental disabilities are able, as far as practicable, to participate equally in prison life".[36] Thus, the treatment and provision of the living conditions for the prisoners with disabilities depends not on the specific decision of the prison administration, but is guaranteed through the legal act. The second chapter of the same document is based on Disability Discrimination Act[37] and determines the legal and policy requirements of the prison service.

However, we come across the opposite approach in the practice of some of the post-Soviet countries, such as Kyrgyzstan, for example. The legislation of Kyrgyzstan,[38] uses not the term "persons with disabilities", but the term "invalid". Also, when the law talks about special conditions, it refers to group I and II invalids. Analogous approach was evident while reviewing the Russian legislation,[39] which considers persons with disabilities in the context of ill persons. For example, the law states that ill prisoners and group I and II invalids are eligible to additional parcels in the quantity and assortment, which corresponds to the medical report (Article 90). In addition, considering that the word "invalid" means "disabled" and not someone "with a disability", the perception of PWDs is in the context of a medical and not a social model. Consequently, the legislation does not speak about equal access for persons with disabilities to the living conditions and programs, which other persons have access to.

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35 *Atabay T.,* Handbook on Prisoners with Special Needs, Criminal Justice Handbook Series, United Nations Office on Drugs and Crime (UNODC), New York, 2009, 6.

36 Sub-chapter 3, HM Prison Service, Prison Service Order – PSO 2855, Prisoners with Physical, Sensory and Mental Disabilities, 20/12/1999, <https://bulger.co.uk/prison/PSO_2855_prisoners_with_disabilities.doc>, [12.03.2019].

37 UK Disability Discrimination Act, c.13, 07/04/2005.

38 Criminal Executive Code of the Kyrgyz Republic, № 17, 31/01/2017.

39 Criminal Executive Code of the Russian Federation, № 1-ФЗ, 08/01/1997.

6. Conclusion

Analysis of legislation and practice gives us a reason to assume that the needs of people with disabilities are subject of care. Persons with disabilities are not fully satisfied with all the means which would ensure their full and effective involvement in all stages of the criminal proceedings and provide adapted accessible environment in places of serving the sentence.

In the context of creating an adequate environment for serving the sentence, we encounter such hindering factors as: unadapt environment; absence of special legal procedures regulating the proceedings from the moment of admission before the release of the accused/convicted prisoner with disabilities; absence of the care/ancillary service; status determination; inadequate access to prison regime information for persons with hearing and visual impairments, and finally, prison staff who may not be able to make relevant decisions at any stage of the sentence in relation to persons with disabilities due to insufficient training in the field. Considering the fact that in any country and for different reasons, persons with disabilities are among offenders and that the criminal justice system cannot be selective, the penitentiary system should be prepared to ensure effective and adequate conditions for serving the sentence for vulnerable groups of such categories.

Recommendations on Ensuring the Efficient Serving of Sentence by Persons with Disabilities in Penitentiary Establishments

1. Criminal legislation should be analysed, in the context of persons with disabilities, and the draft package of legislative amendments, taking into consideration the requirements of the Convention, shall be elaborated;

2. Specialists should conduct a study of penitentiary establishments that will examine the following issues:

2.1. Conformity of buildings and facilities for persons with disabilities;

2.2. The legal framework, which regulates the accommodation of persons with disabilities in the cells and the standards of risk and needs assessment;

2.3. Access to information for various types of persons with disabilities;

2.4. Quality of training of prison staff and quantity of professional staff, based on the needs of people with disabilities.

3. Based on a research study, new effective procedures for working with persons with disabilities in the penitentiary system should be developed as follows: procedures for admission; risk and needs assessment; placement; access to services; preparation for release and so on.

4. The penitentiary system shall elaborate an action plan for the creation of adequate conditions for the persons with disabilities to serve their sentence, in accordance with international standards and good practice examples.

5. The State shall develop the mechanisms for accelerated status determination for the persons with disabilities in penitentiary establishments to minimize the possibility of limiting access to the necessary services.

6. Besides the general statistical data, the penitentiary system shall also publish statistics of persons with disabilities according to the types of disabilities, in order to provide information to relevant organizations, structures and other stakeholders.

7. In order to create the efficient environment of serving the sentence for the persons with disabilities in penitentiary establishments, relevant non-governmental organizations and state agencies shall ensure their mobilization and involvement in all stages of execution of the sentence.

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5. Criminal Executive Code of the Russian Federation, № 1-ФЗ, 08/01/1997.
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12. *Atabay T.,* Handbook on Prisoners with Special Needs, Criminal Justice Handbook Series, United Nations Office on Drugs and Crime (UNODC), New York, 2009, 6, 14, 43, 52.
13. *Cavallaro J.,* Leading Human Rights Experts Call for Speedy Implementation of the Nelson Mandela Rules on Nelson Mandela International Day, Council of Europe, 2016, <https://www.coe.int/en/web/commissioner/-/leading-human-rights-experts-call-for-speedy-implementation-of-the-nelson-mandela-rules-on-nelson-mandela-international-day?desktop=false>.
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19. *Vallas R.,* Disabled Behind Bars, The Mass Incarceration of People With Disabilities in America's Jails and Prisons, 2016, 10, <https://cdn.americanprogress.org/wp-content/uploads/2016/07/18000151/2Criminal-JusticeDisability-report.pdf>.
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21. Political Unions of Citizens – New Rightists and Conservative Party of Georgia v. the Parliament of Georgia, decision of 17 September 2010, № 1/1/493, the Constitutional Court of Georgia, 14.
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Maka Khodeli[*]

Secret Eavesdropping of Telephone Conversation – from Operative-investigative Measure to Covert Investigative Action

In this article there will be analyzed a processual development of the secret eavesdropping of a telephone conversation. Particularly will be underlined the process of its creation as an operative-investigative measure and its later transformation into a covert investigative action. When discussing this topic, main focus will be made on the content and main tasks of secret eavesdropping of a telephone conversation as an operative-investigative measure, differentiating aspects of operative-investigative measures and investigative actions, also there will be analyzed the reasons and preconditions for development of secret eavesdropping of a telephone conversation as an investigative action.

Keywords: *Secret eavesdropping of telephone conversation, operative-investigative measure, principles/ legal basis for implementation/main tasks of operative-investigative measures, law on "operative-investigative activities", covert methods, legal form of legal relation, preventive nature of a measure, investigative control, prophylactic measure.*

1. Introduction

The issue of processual regulation of secret eavesdropping of telephone conversation does not lose its relevance. Therefore it is interesting to study its development, especially during the last few years. As a result of a reform of 2014 secret eavesdropping of telephone conversation, which used to be an operative-investigative measure, now is foreseen as a covert investigative action in Criminal Procedure Code of Georgia (GCPC).[1] In this article precisely this transformation of secret eavesdropping of telephone conversation from operative-investigative measure into covert investigative action will be analyzed. The research will be presented in the following order: The second chapter will cover the concept and history of origins of operative-investigative measures.

In the third chapter there will be discussed secret eavesdropping as an operative-investigative measure. Main focus will be made on the law of Georgia on Operative-investigative Measures and the place that secret eavesdropping of telephone conversation has in the past occupied in this law as one of the operative-investigative measures. In the fourth chapter a research will be presented on differences between operative-investigative measures and investigative actions. Precisely after analyzing these differentiating aspects it will be possible to observe a number of circumstences that have played a role in amending Criminal Procedure Code[2] in 201,4 regulating this procedural activity as a covert investi-

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[1] See Law of Georgia on amending law of Georgia on "Operative-investigative Activities", 01/08/2014, № 2635-RS, which deleted the secret eavesdropping of a telephone conversation from this law. Also, see: Law of Georgia on amending Criminal Procedure Code of Georgia 01/08/2014, № 2634-RS.

[2] See Law of Georgia on amending Law of Georgia on "Operative-investigative Activities" 01/08/2014, № 2635-RS.

gative action. The article will of course also cover the critique that is presented in the literature regarding the transformation of secret eavesdropping of telephone conversation into covert investigative action. In the end there will be a conclusion that will serve as a result of a research on transformation and development of secret eavesdropping of telephone conversation.

2. Concept and History of Origins of Operative-Investigative Measures

In order to understand the legal nature of secret eavesdropping of telephone conversation as covert investigative action, first of all it is important to discuss its previous form – operative-investigative measure. It is interesting to analyze the history of origins, concept and meaning of operative-investigative measures.

2.1. Historical Aspect of Operative-Investigative Measures

Operative-investigative measures have an ancient history of origins. Conspiratorial, covert methods have always been an important and effective tool in the hands of government to ensure safety. Historically operative measures have been known under various names, such as "work of spies", "espionage", and "intelligence work".[3]

Throughout the history of Georgia conspiratorial work of spies has functioned well during the reign of Davit Agmashenebeli (Davit IV).[4] It is considered that in order to guarantee the safety of the country King Davit has transformed previously underestimated work of spies into an effective tool.[5] Historical sources claim that King Davit IV had an information on everything that happened in his country, in particular in the army, in the church or houses of the elite nobles.[6] With the help of the spies the king was probably aware of a situation in the neighboring countries and enemy territories.[7] According to the historian of King Davit, every person knew that every word spoken was instantly known by the king.[8] In this historical source the operative nature of the work of spies is underlined,

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3 *Aladashvili B.,* Sepcial Forces and Espionage, Book I, Tbilisi, 2005 (in Georgian)*; Aladashvili B.,* Secret of Espionage, Tbilisi, 2007 (in Georgian); *Aladashvili B.,* Special Forces and Espionage, Book II, Tbilisi, 2009 (in Georgian), cited in: *Usenashvili J.,* The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 89 (in Georgian).

4 *Lortkipanidze M.,* Georgia in the End of 11th Century and in the First Quarter of 12th Century, Davit IV Agmashenebeli, in: Research on Georgian History, *Anchabadze Z., Guchua V.* (eds.), Vol. 3, Tbilisi, 1979, 223-224 (in Georgian).

5 *Aladashvili B.,* Secret of Espionage, Tbilisi, 2007, 3, cited in: *Usenashvili J.*, The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 89 (in Georgian).

6 *Lortkipanidze M.,* Georgia in the End of 11th Century and in the First Quarter of 12th Century, Davit IV Agmashenebeli, in: Research on Georgian History, *Anchabadze Z., Guchua V.* (eds.), Vol. 3, Tbilisi, 1979, 223 (in Georgian).

7 Ibid, 224.

8 Ibid.

when mentioned that King Davit has done great deeds and has solved extremely urgent matters with the help of these spies and he has done all this only for a good cause.[9]

As one of the most well-known pieces of literature on the theory and practice of espionage is considered a tract written in 11th Century – "Sanet-name", which included a number of recommendations on espionage and suggested the nations to have many spies.[10] There is a considerable claim that King Davit Agmashenebeli has predominantly taken exactly this tract into consideration when creating a network of spies.[11]

As for later history of our country, in particular soviet era, there were special divisions for conspiratorial, operative actions (so-called "Special Forces"), which worked under "KGB" [12] and "GRU"[13].[14] Operative-investigative measures got a very intense and uncontrolled nature, but soviet officials and ideology agencies kept denying this.[15] The history has later revealed the invisible side of so-called Special Forces.[16]

In the modern era operative-investigative measures stay as one of the most effective mechanism when fighting against crime. Having information on every possible threat before the start of investigation has been and remains as an important tool in the hands of government in the context of prevention. Because having information is important and useful. Knowledge is power.[17] The majority of the citizens wants to live in a safe state, where government possesses all necessary information, for example about an expected threat and is able to prevent this threat by conducting effective activities.[18]

2.2. Concept of an Operative-Investigative Measure

The legal term "operative-investigative measure" was first used in the Principles of Legal Procedures of Soviet Union and Allied Republics (1958),[19] where Art. 29 stated that "operative-investigative measure is used in order to reveal the indications of a crime and a person that has committed it".[20] This definition was used in the correspondent laws of allied countries as well.[21] This legal definition was followed up by formulating a concept of an operative-investigative activity in the soviet

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9 Ibid.

10 *Usenashvili J.,* The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 90 (in Georgian).

11 Ibid.

12 KGB of the USSR — State Security Committee.

13 GRU — Main Intelligence Agency.

14 *Usenashvili J.,* The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 90 (in Georgian).

15 *Bakradze A.*, Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 126 (in Georgian).

16 *Mepharishvili G.*, Life and Law, 2nd ed., Tbilisi, 2008, 181 (in Georgian).

17 *Paeffgen H. –U.,* Vernachrichtendienstlichung des Strafprozesses, Goltdammer's Archiv für Strafrecht, *Wolter J., Pötz P. –G., Küper W., Hettinger M.* (hrgb.), Heidelberg, 2003, 659.

18 Ibid, 660.

19 *Bakradze A.*, Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 125 (in Georgian).

20 *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 16 (in Georgian).

21 Ibid, 16-17.

literature. For example, according to *Ratinov*, "Operative-investigative occupation is a system of intelligence activities which based on the law and other normative acts uses special tactical and technical methods in order to prevent crimes, solve cases and search for perpetrators. Operative-investigative measures are carried out with both overt and covert methods and tools. Using covert methods is a special competence of intelligence agencies, for what they possess necessary means and special staff. As for the overt forms of operative-investigative measures, they can be used by investigators as well, but only as a technical tool to ensure the effectiveness of investigative actions"[22]. *Bakradze* does not agree with this definition and states that use of operative-investigative measure by an investigator as a technical tool is wrong, because criminal procedural legislature of that period did not give an investigator permission to carry out actual operative-investigative measures.[23] *Bakradze* agrees with a Russian scientist *Yasinsky*, who criticizes *Ratinov* and thinks that operative-investigative activities in the intelligence agencies were an occupation outside the procedure.[24] For his part, *Bakradze* mentions that "the meaning of operative-investigative activities is defined based on the combination of all those covert measures and tools that represent activities outside the criminal proceedings and are focused on preventing the preparation of crime, uncovering the persons who should be prosecuted for open cases and on finding the location of and arresting wanted criminals"[25]. According to *Bakradze*, despite instigators of Ministry of Internal affairs and operating officer being workers under the same institution and fulfilling the same mission of fighting crime, each of them have their own rights and obligations, that are regulated by procedural law and also by interinstitutional instructions.[26]

The concept of operative-investigative measures developed by the soviet scientists had an influence on defining operative-investigative measures in the law of independent Georgia on "Operative-investigative Activities", which was passed in 1999 and is still being used. According to Art. 7 I of this law, an operative-investigative measure is an action carried out by a state body or an official duly authorized under this law, who/which, within the scope of their powers, ensures the fulfilment of the objectives specified in Art. 3 of this Law. These objectives are:

a) identifying, putting an end to and preventing a crime or any other unlawful act;

b) identifying a person who prepares, commits or who has committed a crime or other unlawful act;

c) for the purpose of presenting him/her to a relevant state authority, locating a person who, despite having been summoned, fails to appear before an investigation or a court; the search for an accused or convicted person and ensuring their appearance before a relevant state authority if such person avoids the application of an imposed measure of coercion or the serving of an imposed sentence;

d) the search for and identify the property lost due to criminal or other unlawful activity;

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22 *Ratinov A. R.,* Interaction between Investigators of the Prosecutor's Office and the Police in Investigating Crimes. Practice of Application of the New Criminal Procedure Legislation, Moscow, 1962, 86-90, cited in: *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 130 (in Georgian).

23 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 130 (in Georgian).

24 Ibid, 131.

25 Ibid, 127.

26 Ibid, 156.

e) the search for a missing person;

f) obtaining necessary facts in a criminal case;

g) identifying (name, surname, age, citizenship of) a perpetrator of a crime or of any other unlawful act;

h) providing information and analytical support to the management of prison facilities.

After a short review of history of origins and concept of operative-investigative measures it is useful to analyze secret eavesdropping of telephone conversation as an operative-investigative measure itself.

3. Secret Eavesdropping of Telephone Conversation as an Operative-Investigative Measure

It is worth mentioning that there are two main models of legal regulations in various national legal systems.[27] They are conventionally called post-soviet and west European models.[28] In various western European countries (among them in Germany), operative-investigative activities are considered to be ordinary procedural actions that are regulated by the criminal procedure code; As for the legal model of the post-soviet countries (for example, Azerbaijan) such kind of activities are regulated by independent normative acts.[29] In Georgia such activities are regulated by an independent act as well, precisely, by abovementioned law on operative-investigative activities.

3.1. Overview of the Law on "Operative-Investigative Activities"

Law of Georgia on "Operative-investigative Activities", issued on 30.4.1999, determines legal preconditions, general principles, goals and types of operative-investigative activities.

According to Art. 1 I of the law, operative investigative activity is a system of measures implemented by the special services of state agencies within the scope of their authority by overt or covert methods provided for by this Law in order to protect human rights and freedoms, the rights of legal persons, and public security against criminal and other unlawful encroachments. Thus protection of a human from a criminal activity is underlined in the very first article of the law.[30]

In the explanatory note of the law on operative-investigative activities, passed on 30.4.1999, it is stated that this draft law covers one of the important issues of law-enforcement. Solving this issue will benefit the fight against crime.[31] This explanatory note confirms that in Georgia there was no legal framework that would regulate operative-investigative activities; in the same document it is mentioned that "as in earlier post-soviet period, in Georgia this extremely hard and sensitive area of law-enforcement is still regulated by agency-level acts. These acts are strictly confidential and most of

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27 *Usenashvili J.,* The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 87 (in Georgian).

28 Ibid.

29 Ibid.

30 *Mepharishvili G.,* Journalism of Law, Tbilisi, 2014, 115 (in Georgian).

31 Explanatory note of the law on Operative-investigative Activities, №1933, 05/04/1999, 1.

them are issued during the soviet period."[32] According to the explanatory note, the draft law acknowledges the reality that was in Georgia during that period in regards to the fighting crime.[33] "An attempt has been made to achieve the noble goal of fighting crime not to violate human rights and freedoms" – is stated in the document.[34]

In the notice of former president of Georgia – *Eduard Shevardnadze*, that was attached to the draft law when presented to the legislative body, as a goal of this draft law, prepared by the executive body, is set protection of human rights and freedoms, the rights of legal persons, and public security against criminal and other unlawful encroachments.[35] In the same letter it is mentioned that the draft law "regulates the mechanisms for prosecutorial supervision and judicial review over operative-investigative activities, principles of protecting and respecting human rights and freedoms, legality, secrecy and the combination of overt and covert methods".[36] President also underlines that the draft law was discussed and supported by the national Security Council as well.[37]

It would be reasonable to briefly analyze the principles of operative-investigative activities and the legal basis for their enforcement according to the version of law on operative-investigative activities before August 2014. According to the version of the law before 1.8.2014, more precisely according to the Article 3, operative-investigative activities are based on the principles of protecting and respecting human rights and freedoms, safeguarding the rights of legal persons, as well as on legality, secrecy and the combination of overt and covert methods. [38]

According to the Art. 3 II, an operative-investigative measure was not allowed to be implemented if it:

a) posed a threat to human life, health, honour, dignity and property;

b) prejudiced the rights of legal persons;

c) was connected with deceit, blackmail, coercion or with the commission of a crime or other unlawful acts.[39]

According to the Art. 8 I of the law on operative-investigative activities, the grounds for implementing an operative-investigative measure were:

a) an instruction of an inquiry authority on an open criminal case, investigator or prosecutor on implementing an operative-investigative measure in respect of a case conducted by them (An operative-investigative measure is implemented upon an instruction of a person of a final decision or a person giving an order on criminal case – head of an inquiry authority, investigator prosecutor)

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32 Ibid; Compare, *Papiashvili Sh.,* Issues of General Methodology of Investigation of a Crime, Tbilisi, 1991, 64 (in Georgian); *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 125 (in Georgian).

33 Explanatory note of the law on Operative-investigative Activities, №1933, 05/04/1999, 2.

34 Ibid, 2.

35 A Letter of the President of Georgia to the Parliament of Georgia, №151/1, 16/04/1999.

36 Ibid.

37 Ibid.

38 It is worth mentioning that Art. 2 I of the current version of the law, contains a regulation identical to this norm.

39 It is worth mentioning that Art. 2 V of the current version of the law, contains a regulation identical to this norm.

b) after duly receiving a report or notification about a crime, an instruction of an inquiry authority, investigator or a prosecutor, that a crime or other unlawful action is being prepared, is being or has already been committed, which requires the conduct of a preliminary investigation, but there is no sufficient information for proving an existence of the elements of a crime or of any other unlawful action;

c) an order to search for a person who is hiding from an investigation, or from the court or who is avoiding the serving of a sentence;

d) a person gone missing, or the discovery of an unidentified body or ownerless property;

e) an inquiry and request of a body conducting operative-investigative activities;

f) an inquiry and request of an international law enforcement organization or of a foreign law enforcement body under an agreement on legal assistance.[40]

Hereby, is the strictly secret nature of operative-investigative activities to underline. According to Art. 5 III of the law before 1.8.2014, it was prohibited to access data and documents about the operative-investigative activities even for the scientific or other purposes until 25 year had passed after conducting them.

3.2. Secret Eavesdropping and Recording of a Telephone Conversation According to the Law on "Operative-Investigative Activities" before August, 2014

According to the law on operative-investigative activities before 1.8.2014 among the operative-investigative measures there was secret eavesdropping and recording of telephone conversation. It is important to briefly summarize the regulations on secret eavesdropping and recording of telephone conversation from that time.

The secret eavesdropping of a telephone conversation was used by the authorities who conducted operative-investigative activities in order to reach the goals stated in Art. 3 of the law.

Interesting are the formal preconditions for implementing secret eavesdropping of telephone as an operative-investigative measure. It is noteworthy that according to the law, conducting an operative-investigative measure that restricts the privacy of communication over telephone or other technical device, which is guaranteed by the law, is allowed only with an order of a judge and a motivated ordinance of an official or upon the written notice of a person, who is a victim of unlawful actions or if there is an information on an unlawful action, which is punishable with the imprisonment for more than 2 years according to the criminal law (Art. 9 II of the law on operative-investigative activities before 1.8.2014).

Also, according to the Art. 7 III secret eavesdropping and recording of telephone conversation after opening criminal case would be conducted with an order of a judge. A motion would be discussed by a judge with a prosecutor and a representative of inquiry authority within 24 hours after receiving it on a closed hearing, where judge would receive one of the following decisions:

a) an order on conducting operative-investigative measures;

b) an ordinance on rejecting the motion.

On the other hand, in case of urgent necessity, as an exception with a motivated ordinance of the head of inquiry authority there was a possibility to conduct such a measure even before opening a

[40] It is worth mentioning that the current version of the law, contains the same regulation with minor changes.

criminal case (Art.7 IV of the law on operative-investigative activities before 1.8.2018). According to the same law, the abovementioned person was obliged to notify the prosecutor within 24 hours after beginning of conducting the measure, who on the other hand, within 48 hours after beginning of implementing operative-investigative measure would report to the court. The court would discuss the motion of the prosecutor within 24 hours after it was made on a closed hearing and would issue an ordinance on declaring an operative-investigative measure lawful or unlawful and therefore on canceling its results and deleting the information obtained by these activities (Art. 7 IV of the law on operative-investigative activities, before 1.8.2014). As the main significance of this law was considered exactly this most important precondition, which required judicial review on conducting certain operative-investigative measures. However it is arguable how real and effective a judicial review on a strictly confidential measure, such as secret eavesdropping and recording of telephone conversation, could have been. As mentioned above, secret eavesdropping has existed as an operative-investigative measure till 1.8.2014, after which it was foreseen as a covert investigative action in the GCPC.

After an overview of secret eavesdropping of telephone conversation as part of legal regulations of the law on operative-investigative activities, it is interesting to identify which main tasks and purposes operative-investigative measures have, according to the opinions in the scientific literature, in order to later differentiate them from the covert investigative actions.

3.3. Content and Main Tasks of Operative-Investigative Measures

A big part of the operative-investigative activities stay unnoticed for the society, because of what it is almost impossible to exercise public control over them.[41] Therefore, exact and clear legislative regulation of operative-investigative measures shall be considered as the most important mechanism to ensure protection of human rights.[42] It is worth mentioning that the core difference between so-called models of legislative regulation of operative-investigative activities lies precisely in having the pre-regulated strict restrictions. The so-called west European model, differently from post-soviet model, fundamentally declares the prohibition of gathering information using operative measures.[43] For example, this applies to the group of the crimes that are subject to operative measures. Generally, in the post-soviet model countries the legislator does not specify any restriction by including specific panel or categories of crimes, when corresponding agencies would not have a right to implement operative-investigative measures, which are subject to judicial review.[44] Therefore the panel of crimes stays in fact without any restriction.[45] The main part of west European model countries give allow to conduct operative-investigative measures only in case of pre-determined group of crimes.[46]

41 *Usenashvili J.,* The Issue of Exercising the Right to Privacy when Implementing the Operative-investigative Measures under the Court Supervision, Journal "Law", № 2, 2012, 91 (in Georgian).
42 Ibid.
43 Ibid, 94.
44 Ibid, 95.
45 Ibid.
46 Ibid.

When characterizing operative-investigative measures, some authors underline that they have special state importance, strategic and also more preventive nature.[47] The borders of operative-investigative measures, according to some authors, are significantly wide. Such kind of measures can be conducted even before opening a criminal case, while conducting an investigation and in particular cases, even after closing the criminal case.[48]

The idea of operative-investigative measures is to obtain the information, identify and arrest the wanted perpetrator.[49] According to the opinion prevailing in the literature, the most important task of operative-investigative measures is to prevent, uncover and open a crime, also to identify the persons, who are preparing or have committed a crime.[50] Generally, an operative-investigative measure is used only when an act can be qualified as a crime; the information that contains the indications of an administrative offence, disciplinary misconduct or a civil tort, does not justify using an operative measure.[51]

Some authors indicate that using an operative-investigative measure does not mean executing criminal procedural norms, but it is induced by the requirements of the criminal and criminal procedural law and serves to the fulfillment of their goals.[52] An operative-investigative action is a tool that uncovers all aspects and details of a criminal activity and provides the preliminary investigation with them.[53] Generally, operative-investigative measures result in conducting investigative actions; however, it is worth mentioning that operative-investigative measures are not only used as the initiation of the procedural activities, but also, frequently with these measures crimes are prevented, wanted person is arrested, etc.[54]

In the literature it is often emphasized that information, obtained in the process of investigation of a crime, among them operative-investigative information, must be revised, studied and when needed, attached and registered by an investigator using procedural tools.[55] Such kind of materials are later transformed into the evidence using the procedural norms.[56] Therefore operative-investigative materials without procedural revision are not an evidence and on the contrary – the investigation cannot gather the total amount of evidence needed independently.[57] This means that information obtained by the operative-investigative measures can first be checked if it is true and afterwards it should endure the "oven"

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47 *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 17, 25 (in Georgian); *Bakradze A.*, Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 127 (in Georgian).

48 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 129 (in Georgian); *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 71 (in Georgian).

49 Ibid.

50 Ibid, 22.

51 Ibid, 19.

52 Ibid, 20.

53 Ibid, 23.

54 Ibid, 145.

55 *Papiashvili Sh.,* Issues of General Methodology of Investigation of a Crime, Tbilisi, 1991, 64 (in Georgian); *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 129 (in Georgian).

56 *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 23 (in Georgian).

57 Ibid, 23-24.

of the criminal procedural law to transform into the legal evidence.[58] The information obtained by the operative-investigative measures is only documented according to the law and this document is confidential; therefore according to *Mepharishvili*, it is forbidden to use an operative-investigative data as an evidence in criminal proceedings, if it is not checked according to the general rules of the criminal procedure law.[59]

It is also to consider that the result of operative-investigative activities may always not have a procedural meaning and may not be used in the legal proceedings. They are often used only as an informational source that is legalized through the operative-investigative activities.[60] Interesting is that in the case of secret eavesdropping of telephone conversation legislator did not restrict this operative-investigative measure only with such kind of crimes that require preliminary investigations. In the practice it could have been used for the purposes of inspection as a prophylactic measure as well.[61]

4. Differentiating Aspects of Operative-Investigative Measures and Investigative Actions

In order to answer the main question of this research – why was the law changed to transform the secret eavesdropping of the telephone conversation into covert investigative activity, it is essential to understand the differences between operative-investigative measures and investigative actions.

The difference between operative-investigative measures and investigative actions is a quite vague and unclear issue of the criminal procedure. Secret eavesdropping of a telephone conversation as an investigative action is an important precondition and a capable tool for effectively fighting crime in the world of modern technical developments;[62] especially when, considering the technical innovations and accessibility, secret eavesdropping and recording of telephone conversation have become easily available for perpetrators and any other interested person.[63] The result could be a paradoxical situation, when other persons could violate privacy of others by secretly eavesdropping a telephone conversation that could stay unnoticed and therefore unpunished, while the investigation bodies would not have a right granted by the law to use this important source for gathering the evidence in order to investigate the crime and uncover the truth on the matter.[64] Precisely because of this and other aspects, some authors consider the regulation of secret eavesdropping of telephone conversation in GCPC as an

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58 *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 146 (in Georgian).

59 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 52 (in Georgian).

60 *Buadze K., Mzhavanadze Z.,* Legal Basis for Operative-investigative Measures, Kutaisi, 2011, 145 (in Georgian).

61 Ibid, 72.

62 *Yurina L. G., Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 6, 8 (in Russian); *Daniluk S., Vinagradov S., Sherba S.,* How to Eavesdrop Telephone Conversation, "Socialist Legislation", № 2(676), 1991, 32 (in Russian); *Meurmishvili B.,* Secret Investigative Activities, in: Georgian Criminal Procedure Law, Special Part, *Papiashvili L.* (ed.), Tbilisi, 2017, 518 (in Georgian); *Krüger R.,* Rechtsfragen bei verdeckten Ermittlungen aus verfassungsrechtlicher Sicht, Juristische Rundschau, Heft 12, 1984, 490.

63 *Yurina L. G.*, *Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 9 (in Russian).

64 Ibid.

investigative action inevitable.[65] On the other hand, a part of scientists are skeptical to this; they believe that secret eavesdropping of telephone conversation, considering its nature, is a pure operative-investigative measure and it is unacceptable to regulate it in GCPC.[66]

First of all, are those aspects to underline that differentiate the goals and tasks of criminal proceedings and operative-investigative activities. While general goals and tasks of criminal proceedings are investigation of a crime, prosecution and rendering of justice.[67] The tasks determined for operative-investigative measures by the law are identifying, putting end to and prevention of a crime or other unlawful acts.[68] This article of the law defines more precise tasks for such kind of activities, such as search for a missing person or property, obtaining necessary facts in a criminal case, identifying a person who committed a crime or other unlawful act, etc.

When discussing the example of secret eavesdropping of telephone conversation some authors underline that if secret eavesdropping of telephone conversation is foreseen as an investigative measure, a defining feature of investigative measure will not be given, such as obtaining and attaching evidentiary material from the source directly by the investigator, because investigators themselves do not perform secret eavesdropping and recording of telephone conversation.[69] They have no capacity and resources to practice secret eavesdropping of telephone conversation themselves.[70] *Gia Mepharishvili* is against the existence of secret eavesdropping of telephone conversation as an investigative measure and supports the idea of strict distinction between operative-investigative activities and investigative actions; He finds it unacceptable to merge operative-investigative activities with the criminal proceedings. He calls this obviously false and scientifically unacceptable view.[71] Also, *Bakradze* finds it necessary to strictly differentiate between the competences of investigative staff and operative-investigative service, in order to exclude any parallelism in implementing certain measures.[72] A part of the authors consider clear differentiation between the matters of criminal proceedings and operative-investigative activities as an objective necessity as well.[73] *Mepharishvili* believes that it is absolutely unacceptable when an investigator adopts operative-investigative competences and investigative bodies and the prosecutor's office are declared as an operative-investigative body.[74] *Mepharishvili* considers that prosecutor's office is responsible for supervision of exact and consistent enforcement of the

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65 *Yurina L. G.*, *Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 9 (in Russian).

66 *Petrukhini I. L.,* Justice: Time of Reforms, Moscow, 1991, 81 (in Russian); *Sheifer S. A.,* Russian Criminal Procedure, *Petrukhin I. L.* (ed.), 2nd ed., Moscow, 2006, Chapter 22, §8, 375 (in Russian).

67 Art. 1 GCPC.

68 Art. 3, Law of Georgia on "Operative-investigative Activities", 30/04/1999.

69 *Sheifer S. A.,* Russian Criminal Procedure, *Petrukhin I. L.* (ed.), 2nd ed., Moscow, 2006, Chapter 22, §8, 375 (in Russian).

70 *Petrukhin I. L.,* Personal Secrets (Human and Government), Moscow, 1998, 87, 92, (in Russian); *Petrukhini I. L.,* Justice: Time of Reforms, Moscow, 1991, 81 (in Russian); *Papiashvili Sh.,* Issues of General Methodology of Investigation of a Crime, Tbilisi, 1991, 60 (in Georgian).

71 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 50 (in Georgian); *Mepharishvili G.*, Life and Law, Tbilisi, 2007, 26, 38 (in Georgian).

72 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 155.

73 *Mamniashvili M., Gakhokidze J., Gabisonia I.,* Georgian Criminal Procedure, Special Part, Tbilisi, 2012, 106 (in Georgian).

74 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 50 (in Georgian).

operative-investigative law.[75] *Bakhradze* mentions that the role of prosecutorial supervision in this field is big and important.[76] When one state authority conducts the operative-investigative measures itself and at the same time is responsible for the supervision of its legality, then, according to *Mepharishvili*, the result will be an unusual legal symbiosis and the situation will look like the plot of "Inspector-General" by *Gogol*, where the widow of a non-commissioned officer flogs herself after committing a bad behavior.[77] The reason according to *Mepharishvili*, why such kind of system is unacceptable, is that the information received through the operative-investigative way shall under no circumstances be excluded from investigatory control.[78] Such kind of step, according to the author, could put the guarantees of human rights protection under major threat.[79] As mentioned by *Mepharishvili*, operative-investigative data is always characterized with the high level of possibility; this is exactly why there should exist a certain procedural filter that will ensure legal revision of this data according to the law; The role of such kind of filter should be adopted precisely by the investigator and the prosecutor.[80] *Bakhradze* thinks that the credibility and evidentiary power of uncovered factual circumstances should be inspected and evaluated according to the law with the procedural means.[81] In opinion of *Mepharishvili*, in case of procedural regulation of secret eavesdropping and recording of telephone conversation the evidentiary sources will expand in exchange of restriction of constitutional rights of the citizens, which is unacceptable for the author.[82]

It is worth mentioning, that the information obtained by operative activities is not always perfect[83] and it really is characterized with a high level of possibility[84]. This can be explained among many reasons with the fact that operative measures are very specific and have a wide scope of tasks.[85] As *Foinitski* mentions, the bodies conducting operative-investigative activities work on the hot pursuit, which requires promptness from these bodies and therefore it is expected from them not to fully consider formal preconditions determined by the law.[86] In addition it is practically impossible to take an operating officer to the court to check the credibility of obtained material.[87] Considering exactly this

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75 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 50 (in Georgian).

76 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 153, 34, 138 (in Georgian).

77 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 51 (in Georgian).

78 Ibid.

79 *Mepharishvili G.,* Life and Law, Tbilisi, 2007, 40 (in Georgian).

80 Ibid; *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 51 (in Georgian); About the so-called legalization procedure of the information obtained with operative-investigative measures see: *Karneeva L.,* Criminal Procedure Legislation and Practice of Proof, "Socialist Legislation", № 1(663), 1990, 35 (in Russian); *Petrukhin I. L.,* Personal Secrets (Human and Government), Moscow, 1998, 92-(in Russian); *Petrukhin I. L.,* Theoretical Grounds of the Reform of Russian Criminal Procedure, Part 1, Moscow, 2004, 167-168 (in Russian).

81 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 128 (in Georgian).

82 *Mepharishvili G.,* Life and Law, Tbilisi, 2008, 181 (in Georgian).

83 *Yurina L. G., Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 6, 10 (in Russian).

84 *Petrukhin I. L.*, Theoretical Grounds of the Reform of Russian Criminal Procedure, Part 1, Moscow, 2004, 167 (in Russian).

85 *Yurina L. G., Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 6 (in Russian).

86 *Foinitsk I. A.,* Russian Criminal Proceedings, Part 3, Saint-Petersburg, 1893, 5-6 (in Russian).

87 *Petrukhin I. L.,* Theoretical Grounds of the Reform of Russian Criminal Procedure, Part 1, Moscow, 2004, 167 (in Russian).

specific circumstance – that bodies, which conduct operative-investigative activities, often cannot ensure to thoroughly meet all the precondition stated by the law when implementing certain measures, the obtained data should be evaluated with a great care[88] and it should be subject to exclusion from the case and to be considered inadmissible.[89]

Mepharishvili underlines different specifications of conducting operative-investigative activities and investigative actions regulated by the criminal proceedings and concludes that that criminal proceedings are absolutely different from operative-investigative activities.[90] Author believes that despite operative-investigative activities having tight connection with the criminal proceedings, they radically differ from each-other with their nature.[91] Operative-investigative activities have informative characteristics[92] and are more part of the field of administrative law[93]. Also, bodies conducting the operative-investigative activities have usually no competence to implement coercive measures (such as for example, search, seizure, interrogation).[94] This means that these bodies are prohibited from practicing executive power.[95]

It is true, that among the tasks of operative-investigative measures belong uncovering and preventing crime or other unlawful actions, but as mentioned above, these activities have more preventive character[96] and unlike procedural measures are not directed against certain person.[97] An operative-investigative measure is mostly implemented before opening of criminal proceedings.[98] According to some authors, operative-investigative activities are an independent type of activities of state bodies. They are cummulation of non-procedural measures that are conducted outside of the scope of criminal law. Operative-investigative activities fulfill more wide-scale objectives and have only that in common with the criminal proceedings that they help the court, prosecutor's office and investigative bodies to open crime or other unlawful activities, also to reveal and identify the perpetrators.[99] Unlike operative-investigative measures, an investigative action cannot be conducted without specific doubt, belief[100] or in case of the specific investigative actions foreseen by the Criminal Procedure Code[101] — without reasonable belief. Therefore investigative measures unlike operative-investigative measures,

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88 *Petrukhin I. L.,* Theoretical Grounds of the Reform of Russian Criminal Procedure, Part 1, Moscow, 2004, 167 (in Russian).

89 *Yurina L. G., Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 6 (in Russian).

90 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 52 (in Georgian); *Mepharishvili G.,* Life and Law, Tbilisi, 2007, 28 (in Georgian).

91 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 51 (in Georgian).

92 *Mepharishvili G.,* Life and Law, Tbilisi, 2007, 39 (in Georgian).

93 Ibid, 39.

94 *Sandkuhl H.,* Die Befugnisse von Nachrichtendiensten, in: FS für *Rainer Hamm*, Berlin, 2008, 625.

95 Ibid.

96 *Zakhartsev S. I.,* Operative-investigative Measures, Saint-Petersburg, 2004, 79-80 (in Russian).

97 *Kniesel M.,* Neue Polizeigesetze contra StPO, Zeitschrift für Rechtspolitik, Heft 11, 1987, 377.

98 *Laliashvili T.,* Georgian Criminal Procedure, General Part, Tbilisi, 2015, 44 et seq (in Georgian); *Mamniashvili M., Gakhokidze J., Gabisonia I.*, Georgian Criminal Procedure, Special Part, Tbilisi, 2012, 110 (in Georgian).

99 *Mamniashvili M., Gakhokidze J., Gabisonia I.,* Georgian Criminal Procedure, Special Part, Tbilisi, 2012, 106 (in Georgian).

100 *Tumanishvili G.,* Criminal Proceedings, Overview of General Part, 2014, 42 (in Georgian).

101 Art. 3 XI, GCPC.

do not cover preliminary stage of investigation, until there is an official precondition for beginning the investigation.[102] This is why some authors underline the advantages of the investigative measures, because at the time of opening of criminal proceedings investigation already has enough evidentiary material and can decide on conducting an investigative action in a more competent way.[103]

It is true, that a significant difference is that the purpose of criminal procedural measures is not to prevent future danger, but to investigate an offence committed in the past;[104] but it is worth mentioning that the prosecution, fight against crime and prevention of the crime in a way fill each-other.[105] Fight against a crime is not done by a prosecutor (at the desk) by planning only repressive measures, but it also implemented by conducting operative-investigative measures (in the streets).[106] A lot depends on correct, collaborated work of an investigator and operating officer in regards to opening crime in a short amount of time and uncovering objective truth on the case.[107]

Operative-investigative activities are implemented with overt and covert methods (more frequently in a covert way and confidentially).[108] This is not a process between parties as it is in criminal proceedings and a party does not even know about their existence.[109] Differently from this, an investigator and a prosecutor are participants of criminal proceedings,[110] whose competences are regulated by the procedural law.[111] Criminal procedural relations always imply a normal and legal form of legal relations, where parties have an information about legal proceedings, have proper rights and correspondent obligations. [112] Russian scientist *Filipov*, underlines that unlike operative-investigative measures, secret eavesdropping of telephone conversation as an investigative action is conducted according to the rule stated by the law, which has a purpose to open a crime and provide the investigation with important factual information.[113] Regarding this matter, *Mepharishvili* mentions that criminal proceeding take place only between the parties and only with adversary process, where parties have a right to familiarize with the evidence gathered from the opponent party and have a big variety of right

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102 *Kniesel M.,* Neue Polizeigesetze contra StPO, Zeitschrift für Rechtspolitik, Heft 11, 1987, 380; *Yurina L. G.*, *Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 20 (in Russian).

103 *Yurina L. G.*, *Yurin V. M.,* Control and Recording of Conversation, Moscow, 2002, 10 (in Russian).

104 *Kniesel M.,* Neue Polizeigesetze contra StPO, Zeitschrift für Rechtspolitik, Heft 11, 1987, 382.

105 Ibid, 378; *Papiashvili Sh.*, Issues of General Methodology of Investigation of a Crime, Tbilisi, 1991, 64 (in Georgian).

106 *Kniesel M.,* Neue Polizeigesetze contra StPO, Zeitschrift für Rechtspolitik, Heft 11, 1987, 378.

107 *Papiashvili Sh.,* Issues of General Methodology of Investigation of a Crime, Tbilisi, 1991, 58, 71 (in Georgian).

108 *Bakradze A.,* Prosecutorial Supervision and Fight against Delinquency, Tbilisi, 1977, 125 (in Georgian).

109 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 51 (in Georgian); *Mepharishvili G.,* Life and Law, Tbilisi, 2007, 38 (in Georgian).

110 *Akubardia I.,* Criminal Procedural Relations, in: Criminal Proceedings, *Gogshelidze R.* (ed.), Tbilisi, 2009, §2, 81 (in Georgian).

111 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 51 (in Georgian).

112 Ibid; *Mepharishvili G.,* Life and Law, Tbilisi, 2008, 38 (in Georgian); *Akubardia I.,* Criminal Procedural Relations, in: Criminal Proceedings, *Gogshelidze R.* (ed.), Tbilisi, 2009, §2, 79 et seq. (in Georgian).

113 *Filipov A. G.,* Tactics of Eavesdropping and Recording of a Conversation, Vol. 2, Omsk, 1993, 216-223 (in Russian).

protection mechanisms,[114] what, according to the author, is impossible in case of operative an investigative activities.[115]

5. Conclusion

There is an opinion that taking in account the rights and freedoms guaranteed by the law, in modern state physical survival is only than possible, if the state is a "preventive state".[116] This underlines the necessity and effectiveness of intensive use of preventive measures. Particularly noteworthy is the latest trend in the criminal procedure law, which persistently proves the importance of existence of such kind of operative measures in a form of investigative actions.

However, there is a risk that these preventive measures will slowly cover the entire legal system, will go beyond the scope of preventive activities and the result will be giving "security, intelligence"[117] or "police" authority[118] to the criminal proceedings. Generally, in the presented "scenario of effectiveness" of operative activities as the weakest and most unprotected player stays a human.[119] This is exactly why the state is obliged to ensure detailed legal regulation of the activities restricting human rights, such as secret eavesdropping of telephone conversation and create a transparent and legal framework for conducting them. Such kind of wish and decision cannot be fulfilled in a totalitarian and police state, for example, during the regime of Stalin or during the period of dissident-hunt.[120]

Noteworthy is the trend of the abovementioned historic development of operative-investigative activities. If initially only a small group of people knew about conducting operative-investigative measures, later it was unavoidable to establish judicial review on these activities and a court decision was needed. Did not this already suggest the trend of the operative-investigative measures and investigative activities coming closer to each-other? As a result of the research, it is interesting, against the discussed practice, to summarize the important points, related to the transformation process of transformation of secret eavesdropping and recording of telephone conversation from operative-investigative measure into the investigative activity:

– The certain operative measures, among them the secret eavesdropping and recording of telephone conversation, were foreseen in the Criminal Procedure Code as covert investigative activities.

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114 *Mepharishvili G.,* Life and Law, 2nd ed., Tbilisi, 2008, 52 (in Georgian).

115 Ibid.

116 *Paeffgen H. –U.,* Vernachrichtendienstlichung des Strafprozesses, Goltdammer's Archiv für Strafrecht, *Wolter J., Pötz P. –G., Küper W., Hettinger M.* (hrgb.), Heidelberg, 2003, 647. This view has gained a notable importance especially after the occurrences of 11.9.2001 and therefore the fantasy of security politics became free of restrictions.

117 *Paeffgen H. –U.,* "Vernachrichtendienstlichung" von Strafprozeß-(und Polizei-)recht im Jahr 2001, Strafverteidiger, 2002, 336-341.

118 *Paeffgen H. –U.,* Vernachrichtendienstlichung des Strafprozesses, Goltdammer's Archiv für Strafrecht, *Wolter J., Pötz P. –G., Küper W., Hettinger M.* (hrgb.), Heidelberg, 2003, 652.

119 Ibid, 663.

120 *Daniluk S., Vinagradov S., Sherba S.,* How to Eavesdrop Telephone Conversation, "Socialist Legislation", № 2(676), 1991, 32 (in Russian).

The term – operative was replaced by covert[121] which is justified and necessary for these two measures that have different legal nature.

– Covert investigative measures in the GCPC have preserved their special character, what is not surprising, considering the process of their origin and development. Here is to mention that the preventive, so-called informative nature of operative measures is emphasized in the scientific literature. The statement in the GCPC,[122] which indicates national or public security, prevention of riots or crime, protection of the country's economic interests and the rights and freedoms of other persons as a legitimate aim of the covert investigative actions, implies the specific legal nature of covert investigative measures. The above mentioned shows the operative and proactive[123] nature of such kind of activities.

– The GCPC requires a higher standard for conducting the covert investigative activities than for the operative measures and not only his formal but also material preconditions are given in details as well;[124] As a result, after the amendments of 2014 stronger guarantees of protection of human rights were foreseen.[125]

– The main point of the criticism shown in the literature that prosecutorial supervision is conducted on the operative-investigative activities, which is necessary and serves as a filter, could be weak and insufficient. When these measures are foreseen as investigative actions, state control on their implementation is stronger. Noteworthy is also the existence of judicial review. All this is conducted according to the Criminal Procedure Code with legal and transparent methods.

– As for the opinion stated in the scientific literature that an investigative body has no capability and resources to conduct secret eavesdropping of telephone conversation itself, the legal reform has already answered this question and according to the Art. 3 XXXII an exclusive competence to conduct covert investigative actions was given to the LELP Operative and Technical Agency, which has no investigatory competence. Therefore, a prosecutor or an investigator does not have so-called operative-investigative authority; Investigation body receives the required information form the Operative and Technical Agency.

– Conducting the secret eavesdropping of a telephone conversation already means restricting a fundamental right and intervention in it, despite the gathered information being used against a person or not. The maximal restriction of preventive accessibility of personal information should be a goal of a legal state. Therefore, regulating such kind of measures by GCPC and implementing them only for the purposes of criminal proceedings should be welcomed.

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121 *Tughushi T., Burjanadze G., Mshvenieradze G., Gotsiridze G., Menabde V.,* Practice of Human Rights and Case-Law of the Constitutional Court of Georgia, Judicial Practice of 1669-2012 Years, *Kopaleishvili M.* (ed.), 2013, 200 (in Georgian).

122 Art. 143^2 II, GCPC.

123 *Albrecht H. –J., Dorsch C., Krüpe Ch.,* Rechtswirklichkeit und Effizienz der Überwachung der Telekommunikation nach den §§100a, 100b, StPO und der anderer verdeckter Ermittlungsmaßnahmen, Freiburg, 2003, 465.

124 See Art. 143^1-143^{10} GCPC.

125 *Gegeshidze T.,* Use of Information Obtained by the means of Electronic Communication in Criminal Proceedings – Georgian and International Standards, "Deutsch Georgische Strafrecht Zeitschrift (DGStZ)", № 2, 2017, 45 (in Georgian).

– In the end, it is true that using the information obtained by secret eavesdropping of telephone conversation as an evidence carries a significant risk, even when it is conducted according to the requirements of the law, however the judicial practice itself should ensure that the evidence gathered as a result of such measures have high standard of permissibility in the criminal proceedings.

To conclude, the differences between operative-investigative measures and investigative activities and the points discussed above justify the existence of secret eavesdropping and recording of telephone conversation in criminal procedure law.

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