EUROPEAN UNION, GEORGIA AND INSTITUTIONAL ENVIRONMENT OF COMPETITION

Abstract. The article discusses the theoretical and practical issues of competition in Georgia. The article analyzes the problems existing within this area in Georgia as well as the dynamics of gradual improvement of the competitive mechanism and competition policy. In the light of the experience gained in different countries and particularly in Georgia for the recent years, the article reviews the directions for competition improvement mechanisms. In addition, the article focuses on improvement of the individual mechanisms of the internal competition in Georgia, as well as provision of consistency for the institutional competition environment. As a result of the conducted studies, it was concluded that when discussing the issues related to promotion of competition and identifying the development level of each area of the country’s socio-economic system, the Global Competitiveness Index may be applied.

The main factors, which ensure the sustainability of the community institutional structure of both the competition institutional environment and the country's overall socio-economic development, can be identified and monitored by the Economic Freedom Index. According to 2014 data, Georgia belongs mainly to the group of commonly free counties rated 22nd in the world, and in Europe it has 12th position among 43 European countries according to the Economic Freedom Index. The recent positive changes in Georgia include the creation of more attractive business environment, anti-corruption activities focused on the law enforcement and judicial systems, as well as on reconstruction of the fiscal and public services sector, which led to a noticeable improvement in the fiscal management and decrease in the country's shadow economy, implementation of the liberal trade policies, development of preferential trade regimes. However, there are some setbacks including the level of market openness (investment freedom and financial freedom) and development of Law and Order institutes (protection of property rights and
freedom from corruption). In this respect, the implementation of a complex of certain activities has been considered within the Georgia-EU Association Agenda, as well as in the socio-economic development strategy of Georgia (Georgia 2020).

**Key words:** competition, competition policy, institutional environment, institutional environment monitoring

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**Introduction.** Under the contemporary globalization conditions, it is of great importance to ensure competition in the economic activities for a country's socio-economic development and the effective business operations. For Georgia, this issue has become particularly important after the EU association agreement. Naturally, it is urgent for the country to improve the separate mechanisms of the internal competition, as well as to ensure consistency of the competition institutional environment.


Due to the nature of transition period from the centralized economy to the market economy, Georgia began the accelerated privatization process of the state property in order to form private property rights (in some cases it was even undocumented and sometimes unreasonable), which was implemented in few stages by free transferring to employees of the housing fund and other small-scale facilities of food and service area, through universal vouchers, lease-redemption and various methods of auction (including zero auction); In some cases, direct sale of property was used (sometimes for the symbolic price). We will not dwell on the assessment of the results of the privatization methods and procedures conducted in Georgia, which is the area of independent research and is an extremely interesting, topical and important problem for all and especially the post-socialist countries. It should be noted that the privatization process (notwithstanding its many shortcomings) managed to achieve the main goal - formed many private properties and private owners. This in turn automatically created the essential component of the market economy-competition. It led to the fact that in the list of the primary normative-legal acts, which were hastily adopted by the State Council of Georgia at the beginning of 1992 after the infamous 1991-1992 events before the restoration of the parliamentary activities, there was the decree "On Restriction of Monopolistic Practices and Promotion of Competition Development" which until the adoption of the competition law in 1996 performed the role of the document which defined the competition and regulatory relations. The decree, and since 1996, the law
"On Monopoly Activities and Competition" defined the major directions of the country's competitive economic policies, the mechanisms for formation and protection of the competition environment and considered the interests and rights of a wide circle of customers. They contributed to the implementation of the economy de-monopolization along with the privatization process.

As the development process of the competition legislation of Georgia took into consideration the international experience in this field, as a whole, it was still considered as a progressive legislation despite a number of deficiencies and shortcomings, which were pointed out by Georgian as well as foreign experts. Unfortunately, the legal and institutional reforms carried out in the field of competition in 2005 neglected a number of very important competition rules and regulations that led to estrangement of the country’s competition law instead of its approximation to the European legislation, the harmonization of which is Georgia’s officially declared priority and targeted criterion. This applies first of all to the law "On Free Trade and Competition", which was the framework law within the competitive legislation of Georgia in both hierarchical and functional point of view. The major competition law adopted in 2005 unfortunately did not regulate the universally recognized key issues of the competition law such as:

- Improper use of the position by economic agents having a dominant position;
- Anticompetitive horizontal and vertical agreements and concerted actions of economic agents in the goods market;
- Merging of economic agents;
- Competence spheres of exclusive property owners (natural monopolies);
- Detection and eradication of cases of unfair competition.

Here it is necessary to note that the latter due to its particular importance in many countries is regulated by a separate law whereas the Georgian competition law generally ignored it and did not even define it at the definition level.

The retrospective analysis of the normative documents related to the competition policy within the various sectors and areas enables to outline several typical and common shortcomings: absence of unified, comprehensive and consistent state policies; declarative character of regulations and provisions and therefore, the absence of the comprehensive mechanisms for specific objectives and their implementation.

The retrospective of the competition policy development points out the apparent lack of the state’s activities in 2004-2012. The analysis of the government programs indicates that Georgian government recognized the need for the development of competition, but there was not enough understanding how, by what means and ways to carry out these activities. The problem was not the underestimation of the role and importance of competition in the economic development of the country (in terms of market relations it would be nonsense to announce it), but the lack of appropriate valid mechanisms for promotion of sound competition environment and the constant protection of the competition. Otherwise, even the healthy competitive struggle is often followed by a gradual concentration of economic power in the hands of an economic agent and emergence of a monopoly entity with the relevant consequences and market behavior.

In response to the criticism of the European experts and the need for improvement of the competition policy, the systematic pseudo-intensive work
was carried out in the country for years for reconstruction and re-organization of
the competition policy and relevant executive bodies and increase (change) of
their powers, which never reported to have even the slightest positive result. In
fact, it could never happen as there was (at least was not visible) no desire and
the State’s will to achieve it. In December 2010, Georgian government, by
adopting the comprehensive strategy of the competition policy, expressed its
political will to develop the modern competition policy and to bring the
competition law into conformity with the international practices and at the same
time acknowledged that the law "On Free Trade and Competition" was developed
for the transitional period and actually it was necessary to adopt a new
framework law which would cover all the sectors of the economy, including non-
liberal and public procurement areas. Within the institutional reform provided
pursuant to the strategy, the Presidential Decree of 26 February 2010 created an
independent LEPL - Free Trade and Competition Agency with the promise that
with the further actions it would be granted respective powers and capabilities
outlined in the Action Programme. At the end of 2011, the agency merged with
the State Procurement Agency and at the beginning of 2012 it was operating as
a legal entity of public law- Competition and State Procurement Agency, whose
numerous structure completely "engulfed" a small group of employees working
on the issues of competition; In our opinion, it was even functionally
incompatible to assign powers of the two agencies to one.

After the long anticipation and permanent promises, in May 2012, a new
edition of the Georgian law "On Free Trade and Competition" was adopted, which
in its essence was behind both the European standards of the competition
regulations and rules and the criteria defined under the comprehensive strategy
of the competition. It is necessary to say that the wording of the above
mentioned edition of the law is more adequate than the version of 2005, which
was completely away from the EU framework of competition law, and as it was
mentioned above, it virtually did not meet any basic competition regulations.
However, the new law did not comply with the EU norms. Unluckily, the law did
not apply to the markets whose goods turnover did not exceed 0.25% of GDP; In
addition, with no reason it did not apply to the facilities important for the State’s
security and the goods and services required for the defense and public safety;
The horizontal agreements remained beyond the scope of the law if the parties' 
joint market share did not exceed 25%, and in vertical agreements - 40%, while
the relevant EU regulations account for 10% and 15%; The logic of the
competition is inconsistent with the fact that the regulatory provisions of the
state aid do not apply to the expenditures allocated from the reserve funds of
President, the Georgian Government and Tbilisi City Hall. Moreover, it is not right
that the legislation allowed any kind of tax cuts and restructuring if decisions
were made by the Georgian government; the similar situation is in respect of
the suspension of the actions ensuring the payment and write-off of tax liabilities.
Totally incomprehensible and illogical is the fact that the law did not allow the
competition body, if required, to act independently from the government and
make the analysis of the goods markets and make the decision in terms of
restoration of the competitive environment. Therefore, the Competition Agency
was not responsible for non-competitive situation on the markets, which was not
included in the priorities predetermined by the government.

The Georgian authorities (the Government and the Parliament), who in
their pre-election programs provided the regulation of the competition and its
approximation to the European standards, have been working intensively with
the non-governmental organizations and foreign experts in this direction for over several years and discussed various bills and drafts for implementation of the radical changes in order to improve the current competition legislation and develop the optimal structure of the relevant executive body. Indeed, in response to the recommendations of the EU's relevant competition authorities, the Georgian government approved for the operation a new competition legislation compatible with the new and modern requirements, implemented an institutional reform, which will enlarge and enhance the Agency's authorities, considerably improve its structure, promote the work efficiency and ensure transparency. In particular, after the new government came to power, in March 2014 the law "On Competition" was amended and a new body was established – the Competition Agency.

In addition, we believe that the following measures should be considered, without which the work of the new competition agency will be inefficient.

The activities of the Agency will not be effective without the adequate cooperation between the regulatory bodies (the Communications Regulatory Commission, Energy and Water Supply Regulatory Commission).

It is necessary to develop the methodology for qualitative and quantitative assessment of the market, as well as to develop and improve the methods for detection of significant monopolies. Each of the above document should focus on the question: Does it limit the number of suppliers? Does it limit customers’ choice?

The competition agency should be a regulatory body, which will regulate the conduct of companies in the market to ensure maximum welfare of the community and it should not be necessarily identified with the body fighting against crimes. Combat against crime is the prerogative of the law enforcement agencies and not of the regulator’s.

The opinion that the competition law will be an obstacle for the business is incorrect. The essence of the competition law includes the inadmissibility of any actions against free competition in any country. This can be done by both governments and private businesses, for example, such as cartel arrangements. The competition law is aimed at disallowance of competition restriction regardless the party implementing thereof. None of the valid legislation prohibits the monopoly conditions that can be achieved through a successful strategy. Merely, there is a list of the actions that fall within a certain amount of monitoring.

The regulatory agency should impose appropriate sanctions on violations, including monetary penalties and pricing restrictions. The amount of such penalty shall be at least equal to the size of the loss; Otherwise, the mechanism of resources allocation will be inefficient and generate more losses rather than it happens during the monopoly.

The Competition Agency was created with the view to implementing the effective state supervision of free, fair and competitive environment in the market. The powers of the Agency include the implementation of any effective measures in order to prevent an economic agent which has a dominant position from abusing its position in the market, promotion of small and medium businesses, timely and appropriate response to any violations of the competition regulatory legislation.

Pursuant to the article 109 of the Treaty (TFEU - Treaty on the Functioning of the EU), the regulatory authority shall be authorized to carry out a market analysis in the relevant goods and services markets, which are subject to
regulations. The regulator agency, in accordance with the Treaty, shall determine, impose, maintain, amend or suspend obligations. Based on the market analysis, it shall determine whether the market is competitive or not.

In the event that the regulatory authority considers that the market is not competitive, it shall identify some service providers with significant market power on the market and impose, maintain or amend any specific obligations in accordance with Article 107 of the Treaty.

The governing provisions of the competition institutional framework established the independence guarantees for the Competition Agency: the implemented changes led to increase of the Agency’s independence. In particular, the Agency may independently start investigation of any market segment if there is any sign of competition restriction in the area and the situation requires intervention of the competition authority. Since the effectiveness of the Agency activities and provision of the fair competition in the market requires timely decision making from the Agency, the Agency introduced some amendments to its regulatory provisions to ensure timely investigation of each individual case. The Agency service fee was cancelled and an applicant does not have to pay it when filing any claim or submitting any application.

Generally, according to the EU law, the common monetary penalties apply to subjects of the Cartel. Very often, the cartel subjects admit their guilt on the grounds that with the "cooperation" with the State they are partially or fully exempted from the sanctions.

It is important that the Leniency Program - one of the basic tools for fighting against anti-competitive behavior of economic agents in the US and Europe- is being introduced into the Georgian legislation.

As it is known, the program involves a full or partial exemption of an economic agent from any liability established by the law if it during the investigation of anti-competitive conduct cooperates with the Agency. Through the cooperation program, the Agency will be able to obtain the necessary information for the purpose of investigation of the anti-competitive behavior of any economic agent.

According to the experts, the real practice has revealed a number of problems, which should be solved in order to effectively implement the new mechanisms of the competition. In particular, the insufficient period for consideration of concentration cases; imperfections of the mechanism for identification of cartels arrangements with indirect evidence; functional failure of the State aid agreement procedures; non-binding nature of obtaining the data requested from any economic agents operating in any relevant market under the concentration; immaturity of the legal mechanisms for obtaining any information at own initiative requested from economic agents during the investigation; ineffective penalty sanctions for non-provision or incomplete provision of any information requested from any economic agent; inefficiency of the mechanisms against dishonest competition provisions; absence of the legal mechanism for obtaining primary data required for the assessment of the competitive environment in the relevant markets from the National Statistics Office of Georgia; imperfections of the mechanisms for checking economic agents in place; Insufficient term of limitation applicable to any breach of the competition law.

Encouraging the effective functioning of the economy and business within the context of improving the competition mechanisms in the country, it is particularly critical for Georgia to present the individual areas of the Georgian
community and the institutional environment in a clear system, to monitor the
dynamics of their structures and to solve relevant problems adequately
[Bedianashvili 2015, Bedianashvili 2014].

**Research outcomes.** When identifying the development level of
individual areas of any country’s socio-economic system, in our opinion, Global
Competitiveness Index - GCI can be used, which has been reflected in annual
reports of Global Economic Forum since 2004-2005 [The Global Competitiveness

The report deals with the factors which ensure the sustainable
development of the national economies. According to the experts’ opinion who
are involved in the research, the country's competitiveness in its essence is the
combination of institutions, policies and factors, which to a certain extent
determines the productivity level of a particular state, and ultimately the
potential possibilities for provision of well-being of citizens [The Global

It is known that the study of the global competitiveness is based on the
analysis of up to 110 socio-economic indicators and the final report is prepared
according to twelve indicators, such as Public Institutions, Infrastructure,
Macroeconomic Environment, Health and Primary Education, Higher Education
and Training, Goods Market Efficiency and Labor Market Efficiency, Financial
Market Development, Technological Readies, Market Size, Business
Sophistication and Innovation. The first four indicators reflect the basic
requirements (basic factors), the following six – the factors of efficiency increase
(enamement), and the last two include innovations and business sophistication
factors.

Pursuant to 2012-2013 data [Global Competitiveness Index (GCI), Scores
2004 - 2013], Georgia’s position compared to Estonia and Switzerland shows the
areas the development of which requires special attention. Obviously, Georgia
should strive to implement the best European model of the country's socio-
functional arrangement system (Fig. 1):

**Figure 1** – Georgia, Switzerland and Estonia according to the development level
of particular spheres

Source: own development
The recent report (2014-2015) on the Global Competitiveness Index shows the improvement of Georgia’s position in terms of individual indicators (Fig. 2).

In the overall ranking, Georgia, which moved to the 69th place (4.22 points) from the 72nd among 144 countries, improved some of the local indicators, such as the Macro-economic Environment; Healthcare and Primary education; Business development; Property rights; Intellectual property protection; Independence of the judiciary system; Efficiency of legal disputes settlement; Effectiveness of legislation; Transparency of the government policy; Level of organized crime (reduced); Enhance support for investors; Quality of infrastructure; Infant mortality rate on 1000 newborns; Life expectancy; Quality of the educational systems; Internet access in schools; expenditures (financial investments) in agriculture; Burden of customs procedures; Access to financial services; Stability of banks; As well as the improved access to the latest technologies (see : [The Global Competitiveness Report 2014-2015]). However, it remains important to promote and substantially improve the areas such as Higher Education and Trainings (3.89 points – the 92nd place), Innovative Potential (2.71 points - the 121st position) and Business Sophistication (3.49 points – the 113th place). Clearly, these are the areas which greatly contribute to the country’s sustainable socio-economic development and its prospects.

As for the institutional structure, the key factor which ensures the interstate competition, as well as the country’s sustainable socio-economic development, in our view, [Bedianashvili 1995] can be identified and monitored using the various indices of the country’s development, including, for example, the Economic Freedom Index.

It is known that the Economic Freedom Index has been processed (calculated) by The Wall Street Journal and the Heritage Foundation Research Center since 1995 every year for the majority of the countries. The indices are published once a year and according to 2014 data, they cover 186 countries [http://www.heritage.org/index/].

Also it is worth noting that for the first time regular index development
was initiated in 1985 by Milton Friedman, the American economist and Nobel Prize winner in 1976, and the common methodology of his calculations is based on Adam Smith’s famous common principles (which refer to non-intervention of the state into the economy, labor distribution, market functions, international importance of free trade), conveyed in his well-known XVIII century (1776) work "The study of the nature and causes of nations’ wealth" (abbreviated "Wealth of Nations") [Smith 1938].

The Economic freedom Index is designed to reflect significant institutional characteristics significant for a country’s economic growth. The index includes several dozens of indicators, which in turn fall in the following 10 groups: 1. Business Freedom; 2. Trade freedom; 3. Fiscal freedom; 4. Government spending; 5. Monetary freedom; 6. Investment freedom; 7. Financial freedom; 8. Property rights; 9. Freedom from Corruption; 10. Labor freedom. The above indicators are presented in 4 large groups: Order of law (8, 9), Government limitations (3, 4), Effectiveness of regulation (1; 5; 10), Market openness (2; 6; 7). These indicators in turn can be considered as the indicators of a country’s competitive environment. Each of the mentioned index is measured from 0 to 100 scale. A value of 100 corresponds to the maximum freedom, and 0 - minimum. Each factor from the above top ten is included into the integral indicator with the equal weight (Economic Freedom Index), which represents their average rate.

According to the quantitative importance of the integral indicator, the world’s countries are divided into five respective groups by levels of the economic freedom: Free within the range of 80-100; Mostly Free within the range of 70-79.9; Moderately Free within the range of 60-69.9; Mostly Unfree within the range of 50-59.9 and Repressed in the range 0-49.9.

The data of 2014 shows that Georgia ranked 22nd in the world, and the 12th position among 43 European countries mainly belongs to the group of Mostly Free countries. Pursuant to the integral indicator value (72.6), it stands alongside the countries such as Sweden (73.1), Lithuania (73.0), Austria, Iceland and Japan (72.4) but Switzerland (81.6) is included in the top five. It should be noted that the average global value of the index is 60.3, while the average European is - 67.1. Thus, Georgia with the integral index of economic freedom occupies high level in Europe and the world.

For the comparative analysis of Georgia’s level of development and to determine the targeted guidance, except for Georgia’s immediate neighbors Azerbaijan, Armenia, Russia and Turkey, we will outline Estonia (the EU member) from the post-communist countries, and Switzerland from the developed European countries, as well as the average European level.

The dynamics of integral indicators of Georgia’s economic freedom (the digital data were used from the materials: [http://www.heritage.org/index/explore]) shows that Georgia’s economic freedom index was noticeably growing in the periods of 2005-2007 and 2012-2013, which can be perfectly explained by the institutional development of the country and implemented activities. It includes the creation of more attractive business environment, implementation of anti-corruption measures directed at the law enforcement and judicial systems, as well as the realignment of the fiscal and public service sector, which led to a noticeable improvement in fiscal management and the reduction of the shadow economy in the country, implementation of the liberal trade policy, establishment of preferential trade regimes and so on.
The business freedom index should be especially highlighted by which Georgia is ahead of the countries under question (Fig. 3):

**Figure 3** – Business freedom index according to 2014 data
Source: own development

In respect of the institutional systematicity, there was a relatively low level in Georgia over the years, while individual subsystems of the institutions were developing quite rapidly (Fig. 4):

**Figure 4** – The dynamics of institutional systematicity level in Georgia
Source: own development

In comparison with the average European and the benchmark countries as for 2014 data, Georgia’s position improved, although it lags behind with the market openness (Investment freedom and Financial freedom) and development of Law and Order institute (Property rights, Freedom from corruption) (Fig. 5).
**Figure 5** – The comparative position of Georgia according to the institutional systematicity level

Source: own development

**Conclusions.** A naturally raised question - are there any substantial setbacks for the country in terms of the indicators such as Market Openness (Investment freedom and Financial freedom) and development of Law and Order Institute (Property rights and Freedom from corruption). One can confidently say that in general for any country insufficient development of the Law and Order Institute is the impediment to develop the competitive environment of European type, to ensure high standards of the socio-economic development and provide efficient business operations. To prove this thesis, a number of studies [Lisin 2013] were conducted. The history of the socio-economic development of various states in the world and contemporary practice shows that the main determinant in this respect is the property institute (Guarantee of property rights) and the effective mechanism to protect individuals, businesses from arbitrary actions of governments [Mill 1980].

Thus, the gradual reduction of the above mentioned deficit should be the main direction to consistent institutionalization of Georgia, which will allow to fully use the potential of modern European institutional structure and the EU business environment for the country’s socio-economic development. The implementation of the complex of some actions is included in the Association Agenda between the European Union and Georgia as well as the socio-economic development strategy of Georgia (Georgia 2020) [Social-economic Development Strategy of Georgia, “GEORGIA 2020”].

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