TAX POLICY TRANSFORMATION IN GEORGIA: ASSESSING THE EFFECTIVENESS OF GENERAL STATE TAX AMENDMENTS ON ECONOMIC SUSTAINABILITY AND BUSINESS GROWTH (2017-2021)

Mamuka Lezhava
Ivane Javakhishvili Tbilisi State University, Tbilisi, Georgia

Nugzar Todua
Ivane Javakhishvili Tbilisi State University, Tbilisi, Georgia

Mikheil Chikviladze
Ivane Javakhishvili Tbilisi State University, Tbilisi, Georgia

Lolita Shengelia
Ilia State University, Tbilisi, Georgia

ABSTRACT
This research aims to determine the role of 2017-2021 general state tax amendments in terms of economic development and improvement of the business environment in Georgia. The following factors were used to evaluate the effectiveness of the tax burden: How the tax system is adjusted to the payer, whether it contributes to economic progress, and what the scope of taxes is. Tax policy experts were interviewed and asked to discuss tax policy reform objectives, options, and mechanisms. The interviews were semi-structured, supported by a briefing document and a topical guide, audio-recorded, transcribed, and analyzed. The efficiency of implemented changes for the EU Association Agreement was also evaluated. Compared to Georgian tax policy, EU tax policy is more liberal. The research revealed opportunities, future perspectives, and the significance of tax reforms and their positive effect on businesses. Based on in-depth interview findings, a detailed analysis of the financial sector is offered.

Keywords: general state taxes; tax burden; budget; investments; economic sustainability

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INTRODUCTION
Tax policy perfection is a compelling issue, and its achievement requires a great deal of effort and resources and involves the resolution of contradictory and ambiguous issues causing some confusion in the payer. It is possible to highlight the main findings where different positions and approaches are observed in relation to the taxable object/time. It should be noted that some instances are still unresolved by
the Tax Code of Georgia, such as taxation of legal entities under public law, the approach to accrual of depreciation of investment property, the issue of taxation of a resident of a foreign country with income tax and tax obligations of activities carried out by travel agents. The mentioned topics are still widely discussed and still confuse taxpayers.

Numerous scientific works have been dedicated to researching tax policy in Georgia. Our research casts light on many important questions, such as what challenges businesses face, where the tax policy needs additional reforms, and to what extent it responds to international and European standards. Considering the pending decision on Georgia’s EU candidate status, the conducted research becomes even more valuable. Awareness raising in the field of start-ups or medium businesses is an important factor. Quite often, certain issues are unclear to them. The reason for this is the linguistic complexity of the tax code and orders, which serves the state’s interest in implementing a taxation policy that ensures business reliability and allows it to develop. Against the background of changes in the tax policy in 2015-2022, it is relevant to know how significantly the changes influenced budget revenues and what the trend of the funds received from indirect taxes in the financial document looks like. The 21st century is the age of new challenges and progress; therefore, for a developing country like Georgia, the issue of business environment development is still topical, and the achievement of this is closely related to tax policy perfection. Naturally, the issue of perfection is a broad concept that includes tax system capacity, principles of fairness, and transparency. Nowadays, the development of incentive mechanisms for the business environment is a subject of wide discussion. Simultaneously, the tax policy undergoes constant changes and stages of development, which fundamentally change and shape taxation issues. On the one hand, these processes can be considered an important step forward, and on the other hand as a means of achieving new opportunities and development. The amendments implemented recently clearly revealed that tax mitigation is a positive factor in the priming of the economy.

LITERATURE REVIEW

Tax administration is a guarantee of solid and stable economic progress and growth. Small and medium-sized business development leads to the formation of a stable business environment. However, it is possible to consider the essential and fundamental change of the profit tax, which is a kind of incentive allowing businesses to reinvest cash and provide and develop entrepreneurial activities. Moreover, the introduction of special taxation regimes and status is a way for the taxpayer to avoid the draining of significant monetary resources at an initial stage, becoming quite a driving factor for start-up businesses. From January 2021, the objective of value-added taxation has been completely changed. The public and private sectors had to adapt to a new reality and deal with the changes properly. It is compelling to know what the consequences of Tax Code amendments were, how effective they were, and what challenges remain (Aslanishvili, 2013). It is generally accepted practice that the more money the government leaves for business, the more the business environment develops, and it gives a similar signal to local and foreign investors. It is noteworthy that the state treasury is primarily interested in receiving high income, although the severity of the tax burden subsequently entails tax evasion, regulation of which requires considerable financial and human resources from the state. A sound tax policy allows businesses to avoid tax evasion and income concealment (Belott et al., 2016). For developing countries, tax reforms are a determining factor of economic growth. The administration of state taxes is quite a complex issue that significantly shapes the social and economic background. EU tax policy is mainly based on liberal and egalitarian principles. The newcomer states in the European Union, including Georgia, strive to implement these two main principles (Gnangnon, 2022). For developing countries, the United Nations has set 17 specific goals on how to overcome poverty and create economic stability. According to the 8th goal, developed countries shall ensure the increase of gross domestic product’s annual growth by at least 7% (Hakim et al., 2022). Employment and wage rates remain an essential challenge for countries like Georgia, and tax policy plays a crucial role in overcoming and reducing unemployment.
The increase in production resources raises the country's overall export volume while reducing its dependence on imports. There is a negative relationship between tax increases and economic progress (Abdioglu et al., 2016), which is quite visible in developing countries. Countries with a stable economy react less painfully to interest rate growth. Based on the study of economic parameters in developing countries, the effect of the influence of common-state taxes on the issue of business expansion becomes clear; developing countries have to overcome painful stages during the period of tax rate reduction (OECD, 2021). In the short term, it will be necessary to reduce budgetary expenses, and the state should ensure cash savings. In the long term, however, it will have a positive effect, as production and employment rates will increase. The treasury will gradually be replenished, and the socio-economic background will be improved (Daoud, 2017).

Major taxpayers generate budget revenues. In developed countries, the number and indicators of paid taxes are large. Meanwhile, the number of businesses with medium and low income prevails in developing sub-regions. Therefore, economic productivity is low (Flaaen et al., 2020).

Developed countries have implemented significant tax reforms. In particular, they have reduced the amount of taxes, created offshore economical free zones, lowered rates, differentiated taxes according to taxpayers' income categories, and exempted start-up businesses from taxation. It is important for developing countries to follow the same path, which will guarantee economic growth (Hakim, 2020).

The economist Michael Hudson developed the idea that a diverse tax arrangement and its structure significantly affect the sustainability of the country's economy and its relevance to an individual (Hudson, 2023). Tax compliance is an intractable problem that has been the subject of many articles and scientific studies, in particular Minh Ha's (2022) "Impact of direct and indirect taxes on economic development: A comparison between developed and developing countries". Ha's main emphasis was on the techniques and advantages of taxpayer-state relations, summarizing the government's role in implementing good tax practices. Vincent' (2023) empirical assumptions examined the main circumstances of the basis that forces people to resort to such illegal actions as tax hiding and evasion. An economist, Rose Camille Vincent, developed the idea that a diverse tax arrangement and its structure have a significant impact on the sustainability of the country's economy and its relevance to the individual (see also Schlegelmilch, 2016).

The state is authorized to collect budget revenues from its citizens. However, this should not be done through business terrorization and coercion. Accordingly, the definition of the optimal taxation burden increases the growth rate of economic parameters. Liberal tax policy is a flexible formula for developing countries (Krechowicz, 2011). On a large scale, decision-making and implementation of changes should be based on the size of the country's GDP and should be oriented towards the development of small businesses (Arzaghi, 2012).

Collins Nnaman, a researcher in the field of technological progress and the impact of changes, noted that recent global developments have shown that the state's priority during a crisis should be given to financial sector sustainability and the introduction of alternative mechanisms in the field of tax policy (Nnamani et al., 2023).

Mohammad Arzaghi discussed the recent changes in the financial sector at the global level, noting that reduced tax rates encourage local businesses to provide positive long-term results. The course of global processes is the basis of economic cooperation between countries (Arzaghi et al., 2008).

Public finance researchers William Ongdon and Jeffrey Kling summarized the psychology of people's behavior toward economic reforms developed by the state (Kraan, 2004). According to them, each reform should be based on cooperation and argumentation principles (OECD, 2015). Without the abovementioned issues, public behavior would be negative and lead to an increase in distrust, preventing the reform's success (Congdon et al., 2011).

Clemens Fuest, another researcher, supports the simplification of tax policy. His study proved that a reduction of the number of taxes and a decrease in the tax rate will not lead to a cash deficit. Moreover, it will ensure business expansion and provide additional motivation (Aghion, 2016).
The strict methods by the state cannot change the psychology of taxpayers' behavior. It will negatively affect and harm the economy and business development and worsen the social condition of the population (Bathena, 2018).

As a formula for unemployment rate reduction, Rose Camille Vincent imagined the full observance of the free market principle, with the government's non-interference in the functioning of the market, and according to the current approach, wage boosts and employment rate increases are possible (Vincent, 2022).

The improvement of socio-economic conditions is unimaginable without the implementation of proper taxation policies. Therefore, one may note that taxes play a crucial role in economic process management. They develop businesses and contribute to gross domestic product generation and job creation. Thanks to recent changes made in the field of taxation, Georgia is approaching the European tax model. It is for this reason that the modes of taxation with value-added tax fundamentally have been altered since 2021, and the amendments affected almost all provisions (Vincent, 2023).

The best European practice is being established gradually, which will contribute to and play an important role in establishing a close relationship between Georgia and the European Union in the future (Boadway, 1992).

The purpose of the implemented changes was to fully protect the taxpayers' interests and approximate the tax system to the European standard. Value-added tax is the largest and most important tax currently applicable in Georgia. Therefore, its fundamental alteration is directly related to the amount of cash flows included in the budget. And the taxes affect both the public and private sectors (International Monetary Fund, 2011).

In 2019, the worldwide COVID-19 pandemic significantly marked the pace of economic development. Domestic and foreign investments decreased while inflation and overall price levels increased. Businesses faced challenges and a shortage of cash. Accordingly, the tax authorities established certain types of benefits, which turned out to be effective. After the pandemic, the economic trends gradually recovered. Moreover, they exceed the indicators before the pandemic (Ahmadov, 2022).

The "Association Agreement" was signed by Georgia with the motive of joining the European Union. The Agreement entered into force in July 2016, aiming at political association and economic integration with the European Union. There is a deep and comprehensive free trade area between the European Union and Georgia, and since March 28, 2017, Georgian citizens have enjoyed the right to travel visa-free in the Schengen zone. The European Union is Georgia's largest trading partner, and it allocates more than 100 million euros annually in the form of technical and financial support for Georgia. The Association Agreement itself is a result of the European Union's Neighborhood Policy (ENP), an important part of the EU's foreign policy, in which Georgia is among the 16 partner countries. It enhances the prosperity, stability, and security of the expanded EU and its neighbors. In 2009, the European Union's Eastern Partnership Program (EaP) was launched, and Georgia also participated.

Along with supporting reforms, the EaP works towards greater mobility of citizens and stronger cooperation in several sectors, such as transport, the energy sector, and environmental protection. The European Union supports Georgia in developing its economic potential through international cooperation. This includes assistance in achieving compliance with the EU legal standards. Joining the European Union requires significant tax and economic reforms (Norway's County and Regional Governments Association, 2017).

Since Georgia aspires to join the European Union, the issue of common-state tax administration is essential. It is imperative that the taxation policy meets international standards and responds to the European Union's methodologies. Taking into account the abovementioned factors, it becomes even more relevant to study the existing challenge and outline scientific findings, as well as identify the problems related to tax code linguistic complexity and unresolved circumstances.

**METHODOLOGY**

The object of this study is the tax system of Georgia - its tax policy - which is a platform for the formation of the budget and sustainable development of the economy. The subject of the research is the changes that were implemented in the tax system and tax instruments, which are...
uniquely aimed at the economic stability and efficiency of Georgia. The purpose of the research is to determine the role of the changes in the general state taxes in 2017-2021 in terms of the economic development of the country, budget revenues, and improvement of the business environment. Have the changes ensured the flexibility of the tax burden and the development of a competitive business environment? To evaluate the effectiveness of the tax burden, it is possible to use the following determining factors: to what extent is the tax system in Georgia adjusted to the payer; whether it contributes to economic progress and provides answers to important and topical issues; where the tax policy excels and fails to achieve perfection; and what is the scope of taxes, etc.

The research objectives are defined as follows:

- determination of the positive trends developed recently in terms of the changes in the Tax Code of Georgia;
- identification of successful cases of the Georgian tax system in sharing foreign practices;
- definition of the tax role in business;
- identification of fields where the tax code achieves/fails perfection;
- evaluation of the challenges Georgian businesses and taxpayers are facing;
- investigation of how the implemented changes have affected the budget, business, and investment environment;
- Identification of factors that will improve tax culture and evaluation of the perspective of raising awareness among taxpayers so that as few people as possible avoid tax payments.

To achieve the research goals, a qualitative research method, particularly in-depth interviews with experts in the field, was applied. Simultaneously, information was collected and analyzed within the framework of a desk study. Interviews were analyzed deductively using the framework analysis. Qualitative research takes an interpretive, naturalistic approach to its subject matter; that is why it studies things in their natural settings, attempting to make sense of or interpret phenomena in terms of the meanings that people bring to them. It is accepted that there is a range of different ways of making sense of the Common State Taxes, and we are concerned with discovering the meanings seen by those who are being researched and with understanding their view of the Common State Taxes rather than that of the researchers. While qualitative and quantitative research may investigate similar topics well, each will address a different type of question. As the research team decided to evaluate the effectiveness of the tax burden, the following factors were used: How is the tax system adjusted to the payer? Does it contribute to economic progress? What is the scope of taxes? Tax policy experts were interviewed and asked to discuss tax policy reform objectives, options, and mechanisms. Interviews were semi-structured, supported by a briefing document and topical guide, and were audio-recorded, transcribed, and analyzed. Incorporating qualitative research methodologies into the research field, which means incorporating expert qualitative researchers into research teams, will enrich the analysis process on the Common State Taxes. In addition to ensuring that the right methodology is brought to bear on the right question, a creative dialogue between the two traditions is likely to be of considerable mutual benefit. In addition to strengthening capacity in research, a comprehensive approach to public services and economic research should begin to close the gap between the sciences of discovery and the sciences of implementation. Also, the efficiency of implemented changes for the EU Association Agreement was evaluated not only through documents but also based on interviews with 10 top experts in economics in Georgia. Expert vision on the current tax policy of Georgia compared with EU tax policy is more liberal. The research revealed opportunities, future perspectives, the significance of tax reforms and their positive effect on businesses.

**DISCUSSION**

Economic and payment field experts evaluate the implemented changes as an important step forward, contributing to the development of both small and medium-sized businesses. Regardless of the abovementioned circumstances, there are still different remarks or instructions from the promoters of the field, although the Ministry of Finance and the Revenue Service are actively working on this issue. Currently, more than one definition and methodology has been published on how the taxpayer should be guided to minimize
confusion and various uncertainties. The draft law developed by the Ministry of Finance of Georgia can bring many positive results in the short and long term. For example, numerous ambiguous terms in the Tax Code that used to confuse taxpayers have been specified and explained.

Furthermore, a natural person registered as a VAT payer was obliged to keep financial records only on an accrual basis. Since 2021, a VAT payer has the right to perform accounting using the cash method. The study revealed that the abovementioned fact would significantly ease the tax burden and obligation of an entrepreneurial individual to the state because the cash method of accounting for income and expenses implies the moment of direct payment or cash receipt. Within the research, an important discrepancy was identified - the place of service provision for VAT purposes, for the determination of which two basic principles were put into effect. On the one hand, in the case of providing services by businesses to businesses, the place of establishment of the purchaser of services should be considered as the place of service provision. On the other hand, if the business provides services to an individual, the place of service provision is considered to be the place of establishment of the suppliers (Bakradze, 2014).

According to tax experts, there has been a significant change in the free supply of goods/services. Compliant with the new reform, a free supply of goods will be taxed only if VAT is fully or partially included in this particular cost. Accordingly, the mentioned taxing will significantly help the taxpayer to avoid burning the tax burden. There are many facts in the Georgian market, such as repairs made to buildings and fixed assets of their production, and companies used them to obtain economic benefits. According to the new reform, the abovementioned transaction will be taxed with VAT only if the person is not able to get the VAT deduction for the purchase of these goods/services from another person. As an example, the Estonian profit tax model involves taxation of distributed profits at the time of enrollment (Bosquet, 2000).

The Georgian economy is still in a stage of development, as evidenced by the challenges faced by Georgian businesses. Table 1 describes the rates of investment revenue growth resulting from liberal tax reform. Despite the tax policy simplification, income and value-added tax remain a significant challenge for start-ups until the stage when the company is strong enough to reserve cash. The business environment research report focuses on the current situation.

Tax policy liberalization has significantly increased the volume of direct foreign investments in Georgia (see Table 1); a low tax burden has made the business environment more attractive and secure.

**Table 1:** Investment revenues in Georgia over the 2020-2022 years, in million US dollars

<table>
<thead>
<tr>
<th>Year</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quarter 1</td>
<td>589.8</td>
<td>1241.8</td>
<td>1675.6</td>
</tr>
<tr>
<td>Quarter 2</td>
<td>173.8</td>
<td>134.3</td>
<td>576.9</td>
</tr>
<tr>
<td>Quarter 3</td>
<td>246.4</td>
<td>322.5</td>
<td>353.4</td>
</tr>
<tr>
<td>Quarter 4</td>
<td>296.9</td>
<td>373.9</td>
<td>745.3</td>
</tr>
<tr>
<td>Sum</td>
<td>1,306.9</td>
<td>2072.5</td>
<td>3351.2</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance of Georgia (2022).

Today, most companies established in the Georgian market are engaged in retail or wholesale trade. Among them, the sale of food, non-food, and tobacco products can be mentioned. Defined, revealed during the inventory/census, are quite natural. For Tax Code purposes, the identified deficit is considered to be a sale and delivery. Correspondingly, the mentioned case is taxable.

It should be noted that until 2021, the loss of goods was taxed according to the market base and at what price it was sold. As a result of the change, free supply will be taxed on the 'cost' of the goods/services supplied and not on the market price. Of course, taxpayers will have significantly fewer budget obligations and will be able to save money. It is an internationally recognized practice that the greater the tax pressure is on the taxpayer, the more they develop the instinct to hide the tax from the budget. Therefore, the current changes have increased the state's care policy; a new term for qualified and non-qualified VAT payers was established in 2021.
General-state taxes in Georgia have the following structure:

Value-added tax (VAT) is number one in size, scope, and budget revenues. Any natural or legal person who carries out economic activity is obligated to pay the tax. In case of exceeding 100,000 GEL of the total income received within the framework of entrepreneurial activity during twelve continuous calendar months, the person is obligated to register as a mandatory value-added taxpayer, at a rate of 18%.

Income tax - belongs to the general-state tax type, which resident natural persons of Georgia pay, with a rate of 20%.

A 15% profit tax shall be paid by resident and non-resident enterprises that carry out businesses in Georgia through a permanent establishment.

Import tax belongs to the series of general state taxes. Like value-added tax, it is an indirect tax that is added to the customs value.

The obligation to register as an excise taxpayer shall be imposed on the person before the delivery of the goods. The following are subject to taxation - alcoholic beverages, tobacco products, and petroleum products.

Revenues from specific taxes are presented in Figure 1.

Figure 1 shows the structure of state taxes in Georgia and the revenues received from them over the years. It should be noted that within the framework of implemented reforms, the budget revenues have increased:

![Figure 1: The structure of state taxes in Georgia and the revenues received over the 2019-2022 years in million US dollars. Source: Ministry of Finance of Georgia (2022).](image)

A newly registered company will automatically be assigned the status of a non-qualified VAT payer, which, at this stage, will not have the opportunity/right to calculate VAT on the transactions carried out. After the Revenue Service examines the activities of the company and the integrity of the taxpayer, it will receive the status of a qualified VAT payer. The current amendment aims to protect the state from allowing taxpayers to evade VAT through fictitious operations. Consequently, the risk that the state will be harmed is considerably reduced.

Tax field specialists working on the bill agree that effective changes will be most fruitful for legal entities under public law because, as a result of the implementation of reforms, their activities will not be attributed to economic goals and, therefore, they will no longer be taxed with value-added tax. Of course, this specific taxing will contribute to the development of public law legal entities, the success and the introduction of innovations, and the funds that should have been paid in the budget. At the same time, they will get a chance to create more state power. The study
found that the determination of the qualified status of value-added tax helped to identify risks from the side of state bodies to reduce the incorrect or inappropriate registration of VAT payers. The introduction of the register of hired persons was made public, and thus, it is difficult to comply with the actual circumstances of the submission of the declaration. It has become possible to protect the labor rights and interests of hired individuals and reduce cases of tax evasion. Changes to the federal tax administration, which came into force in 2021, have had a significant impact on complaints registered with the Disputes Board. At the same time, budget revenues have increased. Table 2 shows the revenues received from general state taxes in 2020, 2021 and 2022. Based on the data, it can be concluded that the budget revenues have increased significantly after the implemented changes. Accordingly, the reforms have had a positive effect on the growth rate of the budget revenues received from the business (see Table 2).

<table>
<thead>
<tr>
<th>Year</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax revenues</td>
<td>10 964</td>
<td>13 380</td>
<td>18 180</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance of Georgia (2022).

The research that was conducted has offered important scientific innovations, though the short time during which the changes were implemented should be considered a study constraint. The long-term effects of the implementation of reforms are the subject of further research that needs further investigation. Despite its contributions, the study is limited by a small number of tax experts. Additionally, significant regional developments, such as the Russia-Ukraine war and subsequent international sanctions, have reshaped the economic climate. Nonetheless, this research lays the groundwork for further investigation into such issues as the effect of tax rate reduction on budget formation.

**CONCLUSION AND RECOMMENDATION**

In the course of this study, the successes achieved as a result of reforms and changes implemented in the general state taxes, as well as gaps and shortcomings, have been revealed, discussed, and characterized. The specific issues that the tax code cannot resolve, and the cases where they reach or fail to succeed in perfection, will be justified. Based on the findings revealed through in-depth interviews, a detailed analysis is offered for the financial sector, in which specific tax reform develops business, has had a positive effect on the correct formation of the budget, and opportunities and future perspectives have been reviewed as well. Accordingly, ways to improve tax administration are proposed. Constant communication between the tax authority and the taxpayer significantly contributes to raising the taxing culture, as well as the comprehensibility and linguistic simplicity of tax legislation. Low tax pressure and liberal policies encourage the entrepreneur to promote the culture of tax payment and avoid tax evasion.

Tax administration is a guarantee of solid, stable economic progress and growth. Small and medium-sized business development is vital for developing countries, leading to the formation of a stable business environment and job growth. Judging by the established practice in the world, one can see that the development of small and medium-sized businesses contributes to reducing labor force outflow from the country and improving the social background. Within the framework of this research, the stages of the tax policy reform were assessed in legal and practical terms. Conclusions were developed, which will be of great value to state bodies in issuing methodological instructions regarding problematic issues and specifying the relevant articles in the tax code. The results show that the increase in the difference between the statutory maximum tax rate in the parent country and the domestic tax rate will increase foreign firms' pretax profit margin. This effect is more pronounced for younger firms and wholly foreign-owned firms. It still is necessary, however, to solve the following issues: taxation of legal entities under public law, the approach to the accrual of depreciation of investment property, the issue of taxation of a resident of a foreign country with income tax, and tax obligations of activities carried out by travel agents.

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ABOUT THE AUTHORS

Mamuka Lezhava, email: mamukalezhava1@gmail.com (Corresponding author)

Mamuka Lezhava graduated from Ilia State University, Faculty of Business Administration (2020). He is a doctoral student at Tbilisi State University in the Faculty of Economics and Business. He is a lecturer at the university/course Introduction to the Tax Code of Georgia. He is the chief auditor - the auditing company “Elan” LLC and a Credit Risk Department Specialist.

Dr. Ngzar Todua graduated from Ivane Javakhisvili Tbilisi State University, Faculty of Commerce (1986). He has PhD degrees in technical Sciences at the Moscow State Institute of Commerce (1990) and Doctor of Economics Sciences at the Georgian Institute of Economic and Social Problems (1995). He is a Head and Full Professor of the Marketing Department, School of Economics and Business, Ivane Javakhishvili Tbilisi State University, Tbilisi, Georgia. He is a member of the Senate of Tbilisi State University (2006), the Georgian Economic Scientific Academy (2000), and the International Social Marketing Association (2013).

Dr. Mikheil Chikviladze graduated from Ivane Javakhisvili Tbilisi State University. He is a full professor of the finance department of the School of Economics and Business, Ivane Javakhishvili Tbilisi State University, Tbilisi, Georgia.; Council of the Faculty of Economics and Business Chairman - Tbilisi State University. He is a member of the Senate of Tbilisi State University (2007); He is Chairman of the Tax Department of the Revenue Service of Georgia.

Lolita Shengelia graduated from Ivane Javakhisvili Tbilisi State University, Faculty of Economics and Business (2011). She is a Lecturer at Ilia State University School of Business Technology and Education; He is a doctoral student at Ilia State University.