



Feasibility Study of New Terminal
Facilities of the Georgian Ports
Phase 3 Report
Outline Privatisation Concept

Outline Privatisation Concept

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1. Definitions and Remarks

1.1 General Remarks

The definition of the term privatisation has a great variety of meanings and is not used in a standardised way. Some authors already describe the introduction of a private legal form and/or guidance and incentive systems of private business as privatisation. Also, the decline in sovereign-administrative market-entering-barriers or regulations specific for certain branches is often called privatisation in the political discussion; those processes will, in the work on hand, be defined as liberalisation and deregulation. The most precise definition sees privatisation exclusively as a process in which ownership of enterprises is transferred from the state to a private person.

Following Yarrow, a practicable definition for the research on hand, privatisation is understood as the transfer of claims of corporate profit from the public to the private sector. Besides the sale of public enterprises this definition includes the placing of orders (Contracting Out, Franchising) to private businesses as a substitute for formerly state production of output.

It is characteristic, that within OECD-countries privatisation is formed in those countries which have a high income per capita, developed capital markets and relatively stable, democratically elected, governments. They differ fundamentally from the development in developing countries and countries with formerly communist governments. The special features of privatisation in non-OECD-countries include the following aspects:

- non-existent or underdeveloped capital markets,
- underdeveloped legal systems, blurred or difficult to carry through conditions of ownership,
- lack of private management and entrepreneur's know how,
- political instabilities that make rationalisations and the reduction of price subsidies impossible,
- the dominating position of the old-established management (so called "nomenclature-privatisation" in Eastern Europe),
- discrimination or preferential treatment of certain ethnic and religious groups in the course of the privatisation
- special methods, e.g. mass privatisation in Eastern Europe or Debt-Equity-Swaps in Latin America.

A lecture of the UNCTAD points at the fact, that every port faces decisions which can only be made with state agreement:

"Land use and strategy considerations are generally a matter for government. The question, what a private port is, finds its answer in the formulation:

a private port is one where the assets are privately owned and incomes accrue to the private owner, not to the public or a public-owned body. A typical wholesale port privatisation tends to be limited to waterfront property and operating rights.

But: privatisation is not the answer to improve the efficiency of a port, it merely provides the frame conditions."

And the report finishes:

"Call it privatisation or call it commercialisation or corporalisation, it should make no difference to how the port performs. Regardless of who the owner is, the quality of management will be the factor that determines the success or otherwise of the port."

With regard to the Georgian ports, the conclusion is, that through privatisation by preservation of state interests frame conditions must be created, so that the ports' competitiveness is increased and secured, investment funds are made available, and generate an acceptable return for the shareholders.

Referring to the frame conditions, Prof. Papava, Minister of the Economy of Georgia, explains:

"To continue economic reforms in Georgia (and in other post communist countries in a similar situation) we offer the system of 'social selection', or what might be called the method of 'social promotion' of economic reform. The essence of the method is that the government should create the conditions promoting quick information of the stratum of entrepreneurs. At the same time, it is necessary to render target-orientated assistance to that stratum which is most in need, so that the poor do not prevent the process of reform.

The method of 'social promotion' of economic reform involves three essential measures:

- Improvements concerning the criminal situation, to relieve the fear of formal or partially formal military formations. Without settlement of this problem, it will be a serious obstacle to activate either domestic and foreign entrepreneurs, and prevent the arrival of foreign investors in Georgia.
- Promotion of the development of entrepreneurial activity. Without this, the entrepreneurial stratum will continue to be developed in the shadow economy, which is fertile soil for the consolidation of illegal activities and prevents the creation of legal entrepreneurial activity.
- Carrying out purpose-orientated social assistance to the most needy stratum of society, so that they are able to overcome difficulties which arise in the reform process. This targeted social policy would be the guarantor of support for the reform process."

1.2 International Solution Concepts in the Traffic Sector

There are world-wide tendencies to let the extension and the operation of transport devices respectively transport infrastructure to be carried out by private sector enterprises or let them, at least, be pre-financed with private capital. This development is not a new one, because in the history of many countries the set-up of a railway infrastructure and, more recently, the construction of motorways, was realised in this manner.

The enormous increase of transport on the whole and, connected with it, enormous investment requirements have all over the world led to reflections about the highest optimal procedure possible.

Because of the obviously very divergent national respectively regional objectives and political notions there are merely comparable basic models, which in their details show considerable differences:

- The simplest form is based on a license agreement, into which the mortmain enters with a selected operator/consortium. As a rule, the operator takes care of the investment and operation duties, but he also enjoys a high degree of freedom in terms of tapping of the market, property utilisation etc. These actions are not necessarily in accordance with the interests of the public.
- New ways of enlisting private investment are: BOT (Build-Operate-Transfer) and BOOT (Build-Operate-Own-Transfer)
- models, where the transport infrastructure is passed to the mortmain or new agreements will be concluded after a fixed period of time (20 to 40 years). 'Build' could also be substituted by 'Rehabilitate' the existing facilities.

These models are not only brought into effect for the whole of infrastructure facilities, but also for investment in intensive plant parts, such as the container terminal or the multipurpose terminal.

Apart from private financing, fundamental advances are seen in the shorter building periods, economical construction and operation as well as the assumption of the risk.

These results are obtained by:

segregation of capital requirements from public budgets.

- creation of the prerequisites for private sector business management,
- large degree of detachment from political influences.

The transfer of the ports into private hands is normally done via the sale of capital stakes; the extent is directed by the objective and capital requirements.

During every privatisation arises the important question of the availability of premises and the amount of assets owned by the company. The possibilities reach from a complete take-over of the entire infrastructure by one or more private operators, via various intermediate models, up to the division into an ownership company and one or more operating companies.

In the first case, the state as owner of the port is to alienate its entire shares to one or more private enterprises with the consequence, that the influence of the state in business policy is going to be massively restricted, if not ruled out altogether. Because of the ports' essential function for the country this cannot be in the interest of the Georgian state.

Feasibility Study of New Terminal Facilities of the Georgian Ports.

Aspects of the Privatisation

. **Authority** : A Port Authority will be established as a part of the Georgian Maritime Administration and will be dependent on the Ministry of Transport. The port itself, in case of Poti, the Port of Poti will be established as a legal entity, will control the commercial activities of the port and detain 48% of the shares of a Joint Stock Company (JSC) involved in the operations and the development of the port.

. **JSC Shareholder** : 48% : Port of Poti (Ministry of Transport/ the Government of Georgia)
 49% : private foreign investors (Companies, Banks,...)
 3% : private Georgian investors
 The total Georgian shareholding will be 51%.

. **JSC Share capital** : US\$ 37.5 Millions share capital (19.5 Millions cash for investments, 18 Millions for equity).

. **Process of the privatisation** : Logistical units of the ports will be privatised step by step by in order of priority and profitability. Privatisation can start immediately eg. for the port of Poti , the container terminal and RoRo unit could be privatised as soon as investors are identified.

The step by step privatisation offers a flexibility in the privatisation of the port according to the economic and financial needs . Due to this flexibility, the privatisation might be faster and attract a larger number of investors each of them specialised in their activity. A better return on investment can then be expected when the privatisation of the all port will be completed.

. **Ownership** The ownership of the different parts of the port (land, infrastructure....)will remain unchanged for the time being. As, the privatisation focuses on the activities of the port, the ownership is in itself not an obstacle .

. **Investment volume**. 116 Millions US\$ for the all port including the extension area within 15 years and a return of investment in same period of time. Additional 40 Millions for new infrastructures.

. **Employment** The JSC takes over the required personnel from the port activity by activity . A specialised fund has to be established to ensure that wages are available for pensioners of the port.

. **Competition**. The involvement of several operators and investors in the operations of the ports preserve a necessary competition considered as condition for a fair and harmonious development of the port.

. **Management**. Within the JSC, a management company will be employed and will under a long term contract manage the commercial activities of the JSC and its related operations..

. **Interest of Georgia**. The port remains in large part in the hands of the Government of Georgia and this preserves its financial interests. At the same time that the foreign investors and operators assist in the development of its activities and economic growth.

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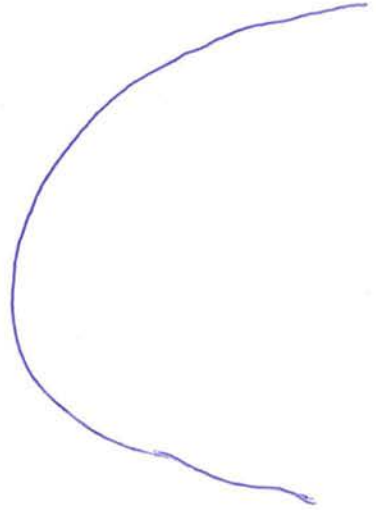
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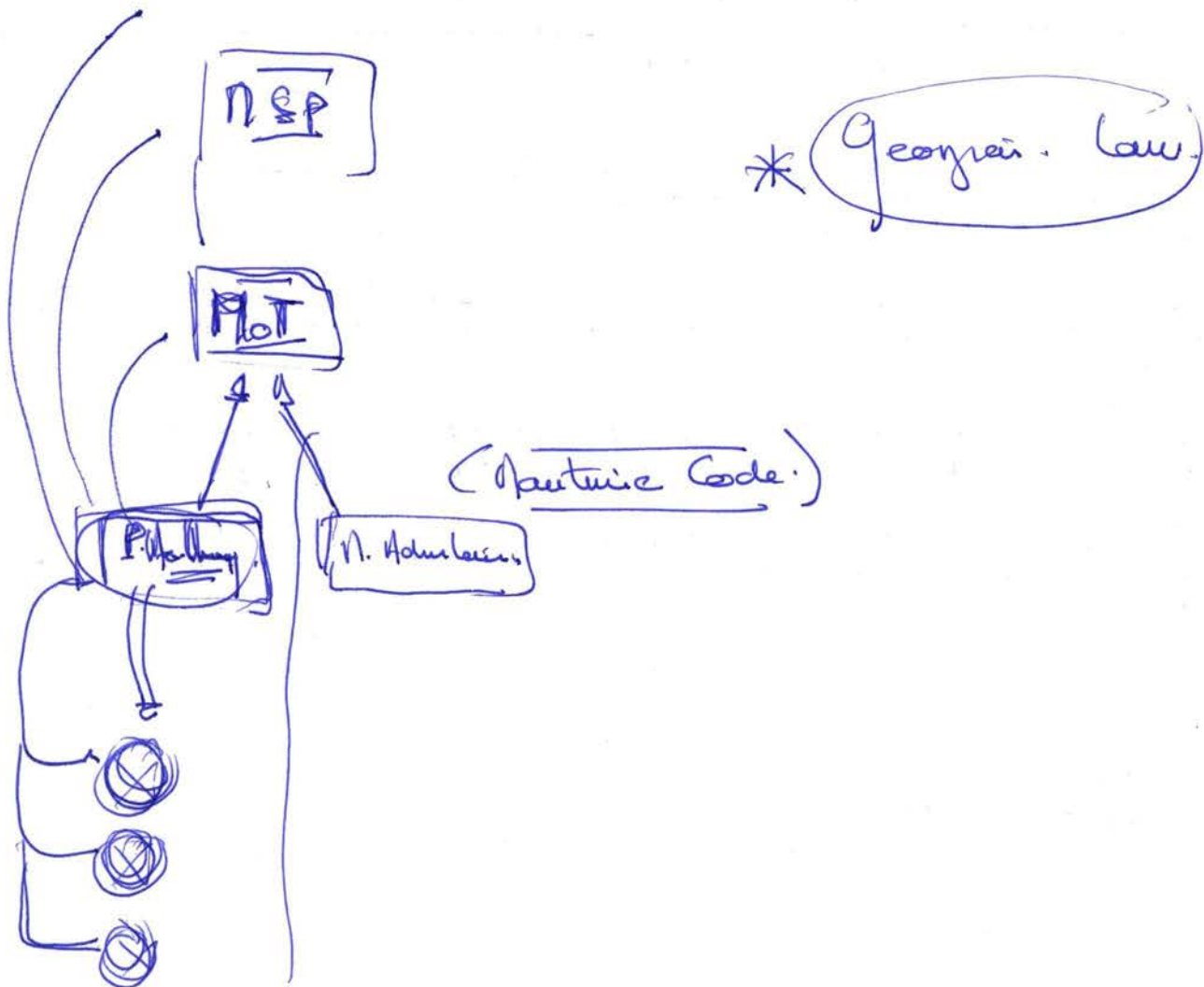
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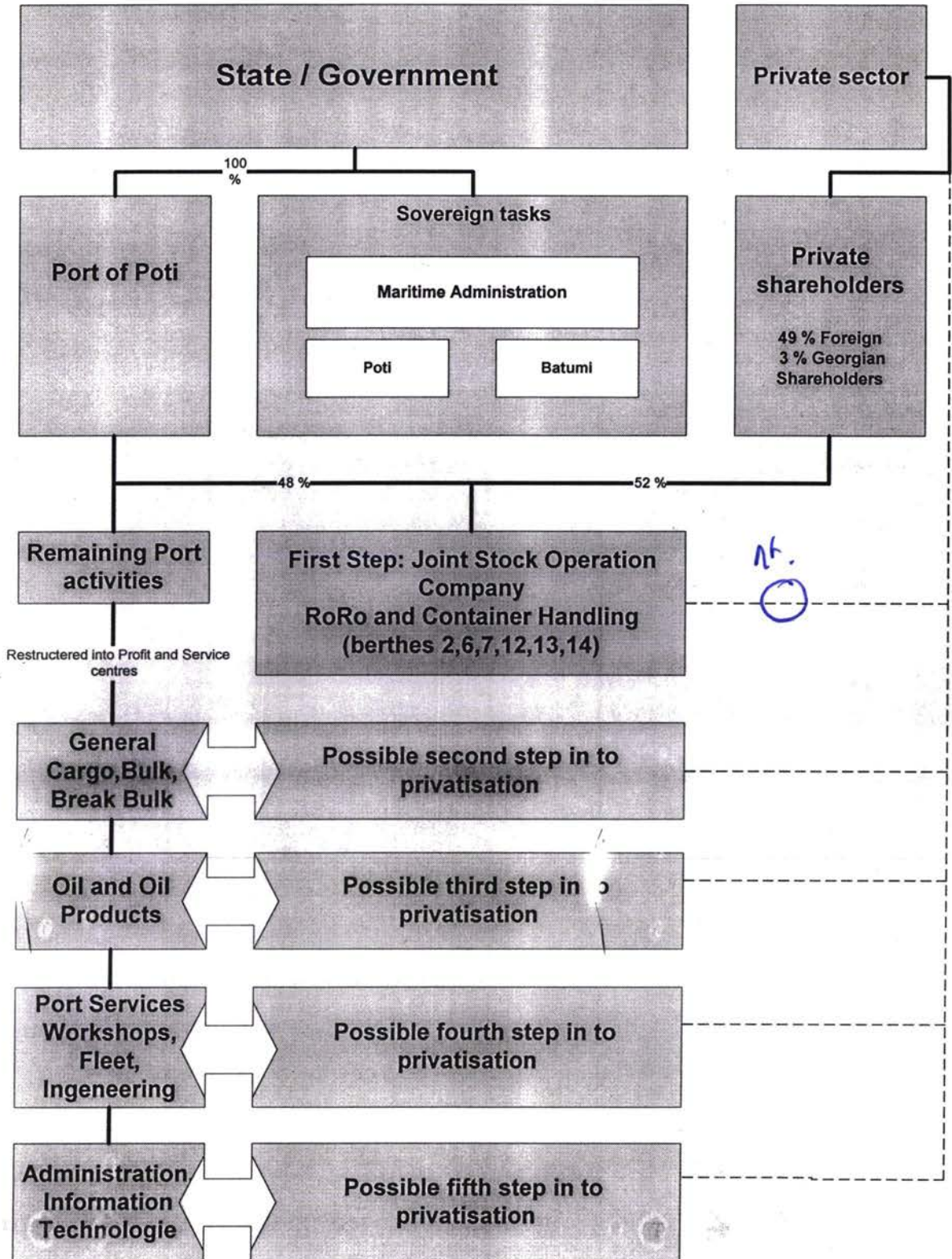
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2. Recommendation for a Specified Concept

2.1.1 Shareholder Concept



It is intended to develop the Port of Poti into an important international port and furthermore to a multi functional logistic centre. For this purpose it is necessary to create an efficient company structure which then has the possibility to act as a modern market orientated company.

The following principle notes shall be made to describe the strategy (see graphic)

- The sovereign duties of the state/government (Ministry of Transport) will be separated from the economic activities.
- Land and quay is owned by the Port of Poti Joint Stock Company
- It will act as landowner and shareholder
- The Port of Poti joint Stock Company will have to be restructured into Profit and Service centres for the remaining Port activities.
- The shares of Poti Port in the first operating company should be 48 %, the Share of Georgian shareholders should be 51 % (including the Ports shares) and the shares for foreign shareholders should be 49 % accordingly.
- Port of Poti and the first operating company have to offer their services on market-orientated price levels.

2.1.2 Structural Contract Drafts

To sum up, the approach of a privatisation must include the ensuing basic elements:

- creation of the prerequisites and frame conditions for a positive entrepreneurial development of the port,
- detachment of operative business from the basic infrastructure and the connected investments,
- introduction of private sector elements as far as it is useful and representable from an operative point of view,
- far-reaching restriction of the financial contributions as well as the assumption of the risk by the mortmain.

2.2 Strategy Aspects of Privatisation

2.2.1 Future aspects

To describe strategic aspects of port privatisation, the long term expectations are to be described. These expectations are in fact the restructuring of the ports and the specific objectives out of this. The most important aspect is to enhance the efficiency of port services. Institutional reforms like deregulation or privatisation are to diversify services and/or to reduce costs. The most important objective is often to obtain new financial sources for financial requirements especially for new investments or for the rehabilitation of existing equipment, berth or other port related assets or for the development of new parts of ports in general. Other objectives like:

- to enhance the efficiency of port services
- to diversify port services
- to reduce the ports' service costs
- to promote the ports in the transport chain
- to acquire management expertise
- to implement modern management methods

are easier to introduce but improvement is in the first line a result of sound management. Within the Top 100 Container ports in the world only 4 ports are entirely Private, 1 port (Tilbury) is Private/Public, 15 Ports are Public (one is Singapore) and the remaining 80 Ports are Public/Private (source Cargo Systems, figures April95 to Dec95).

Most of these Ports are profitable and their ranking is based on efficiency and competitiveness .

The points left as the strategic objectives of privatisation for the Georgian Ports are:

- to finance port rehabilitation and port developments
- to eliminate or to minimise bureaucratic/political influence

The future requirements, based on sound traffic forecasts are described in the Port Master Plans and the Port Development Plans for the two Georgian Ports. Meanwhile the decision has been made to develop in Batumi as a first project the Multi Purpose Terminal and in Poti the extension of the existing Container Terminal. Consequently, the first parts of the Ports to be privatised are the Multi Purpose terminal in Batumi and the Container Terminal in Poti. Without these developments both Ports are not in the position to meet the requirements of the future and due to the specific Georgian situation this is only with private involvement possible.

2.2.2 Importance for Georgia

The Georgian ports are the entrance to the TRACECA route at the Black Sea. The growing economies in the Caucasus and Central Asian Republics will result in the growth of transport volumes. Considerable volumes will be shipped via the Georgian ports. This is a challenge and a chance for Georgia and the Georgian Ports.

The possible advantages for Georgia and the Ports resulting from the increasing transport volumes are job security in the ports, economic benefits for the country from taxes and profits from successful port companies. Georgia already has with its ports the basic assets and the strategic position to realise the possible advantages.

In 1993 an international agreement to develop a transport corridor on a West-East axis from Europe, across the Black Sea, through the Caucasus and the Caspian Sea to Asia had been signed by five Central Asian republics, three Caucasian republics and the European Union and in a later stage (1997) Mongolia and the Ukraine. The transit function and the role of Georgia in this corridor is of paramount importance for all the TRACECA member states. The fast growing states in the Caspian Basin, Kazakhstan, Azerbaijan, Turkmenistan and Uzbekistan as well as the European Union and the other member states of TRACECA will help and support Georgia as long as Georgia will fulfil their duties according to the signed agreements. To lose the influence on the entrance of one of the most import transport corridors, and that can be the case if the ports are going totally in the hands of private investors, might lead to the effect, that the support from the contract partners could be withdrawn and the image of Georgia as a reliable country could become negative.

There is now doubt, that the ports need private investors for the development of required new terminal facilities and the rehabilitation of existing ones but by strategic reasons the ports should be in the hands of Georgia.

Despite that, a privatisation and commercialisation project with strong involvement of Georgia will have a positive signal to push the Georgians to take more parts of their future in their own hands instead of selling their assets. Even by tax reasons it makes sense to have privatised and commercialised enterprises under control to avoid that benefits are not or not totally going to these mentioned enterprises. As already stated, the success of the ports in all countries in the world is a matter of management style, management qualification and management practise. This can also be generated by other methods than the privatisation.

2.2.3 Importance for TRACECA and the TRACECA States

After the breakdown of the Soviet Union the former Soviet Republics becoming independent states and in some respect unified in the Commonwealth of Independent States (CIS). Within the Tacis Projects (Technical Assistance for the Commonwealth of Independent States) TRACECA (Transport Corridor Europe Caucasus) had carried out since 1993 following projects:

22 Technical Assistance (TA) Projects in an amount of	28.155.000 ECU
5 Investment Projects for the rehabilitation of infrastructure	24.500.000 ECU

These projects include basically all transport related activities even the related activities hereto.

Only for the Georgian Ports TRACECA spends 1.5 Million ECU for the Feasibility Study of New Terminal Facilities in the Georgian Ports and more than 5 Million ECU for the building of a Rail-RORO ramp in the Port of Poti.

Not only the financial engagement is an indication about the importance of the Port Projects for the TRACECA and the member states of TRACECA. The industrialised countries of the European Union are going to explore the markets of the States in the Caucasus, the Caspian Basin and Central Asian Republics and the before mentioned States are going to export their products to the West-European Markets.

To be competitive in the world markets all TRACECA states need a reliable transport route under their jurisdiction to avoid influences and uncertainties from third parties or not TRACECA countries. This transport way is TRACECA and it is the only one.

3. Prerequisites in Georgia

3.1 Taxes and Regulations

The following part will cover questions of taxes and regulations relevant to investments and privatisation of Georgian port facilities and in particular to the container terminal of the port Poti.

The Georgian tax system aims at the further promotion of transitional economic development. In the past substantial progress in adjusting the tax system to modern market mechanisms were made.

3.1.1 The planned privatisation of port facilities under the aspect of the current Georgian tax system

At present the tax system in Georgia is diversified on the basis of the main activities of enterprises (agricultural, traffic and industrial, banking and insurance). The tax base is the source of money. E.g. agricultural enterprises pay 10% profit tax, industrial including port facilities 20% and banks 35%. This system is only orientated on the subject of business and refers to domestic as well as to the registered international firms or joint venture enterprises. The legal form of enterprise has no influence on taxes in Georgia.

In private interviews with the local administration during May in Georgia the local authorities expressed the opinion that in the future a modification of the tax base applied can not be excluded. In July of this year the Parliament session is expected to make amendments on 103 articles of 273 articles of the Georgian Tax Code. It is most probable that the tax system will be shaped further in accordance with the German model. This fact can give further incentives on investments and development of private business increasingly meeting international standards. The modifications of the Georgian tax system will be directed at the promotion of medium and long term economic development in Georgia by activating activities of domestic resources and international capital. The tax system guarantees long term and reliable conditions for domestic and international investments. In regard to the privatisation process and the planned investment in the Georgian ports it is rather important that in Georgia there is no special tax for transit cargo. There is a customs fee of 0,3 % from cargo value. The Poti Port Administration considers that this favourable condition remains in the future and will not be changed by next tax modifications.

3.1.2 Kinds of Taxes in Georgia

For information here a survey of current taxes for enterprises resident in Georgia and an assessment of their relevance in regard of the planned privatisation is given.

Name of tax	Rates for Georgian Ports	Remarks
Profit tax	20%	As usual in industry, to reduce indicated profit by creating reserves for further investment should be possible
Company property tax	1%	Fixed assets
Income tax for employees	12%-20% of the salaries	paid by the enterprise, progressive counting due to the amount of income
VAT	20%	taxable transaction or import, see below
excise	special regulation	luxury goods, refers not to the transport

Name of tax	Rates for Georgian Ports	Remarks
land tax	1.44GEL/hect	without difference concerning use
social tax	27%+1% of salaries	paid by the enterprise, 1% by the employee, for medical insurance, pension fund,
tax for usage of natural resources	1%-15%	volume of extracted natural resources
tax on environmental pollution	e.g. the port pays 0,01 % of profit at the time	depends on the actual damage, decision of ecological inspection
various local taxes		no relevant impact on investments, decided by local administration

The VAT in Georgia is not different from western analogies. The present tax system takes 20% from added value of services and goods. In connection with the further diversification of the Georgian industrial and entrepreneurial landscape the questions of sophistication the VAT mechanism will be given more importance in the future. Goods produced in the CIS and realised in Georgia are not taxed by VAT. Goods for export out of countries of the CIS are zero rated. Goods produced in Georgia and exported in CIS countries are charged with special excises.

Enterprise Profit Tax is based on the subject of business and the amount of taxable profit. The tax base is subject to the business sector: industrial 20%, agriculture 10% and bank/ insurance 35%. The taxable profit consists of

- trading profit
- profit on the sale of an enterprise property during the year
- income received from investments during the year
- other income and gains

Personal Income Tax for individuals resident in Georgia more than 182 days rates between 12 and 20%. It is progressed in accordance with the total of personal income. The tax is imposed on all forms of personal income. There is a graduated scale depending upon the amount of annual income.

Property Tax is based on the assets on the annual average value of the enterprise fixed assets and stock. The rate of enterprise property tax is currently %.

Social Tax is paid by the enterprises on the basis of the amount of salaries. 27% are paid by the enterprise and 1% by the employee.

Georgia has agreements on double taxation. Georgia has not yet concluded agreements on avoiding double taxation with Germany. There are agreements on avoiding double taxation with Armenia, Azerbaijan, Turkmenistan, Kazakhstan, Romania, Uzbekistan, Iran, Ukraine. Double tax relief for foreign tax paid is given to Georgian tax payers by means of a credit against income tax payable in Georgia. The tax authorities gives formal confirmation of taxes paid in Georgia.

3.1.3 Relevance of the legal form of the enterprise in regard of taxes

The tax rates (see table above) are the same for all legal forms of enterprises in Georgia. Thus, the investor/consortium's choice of the specific legal form of the enterprise has no impact on taxes to be paid. Nevertheless, there are important other factors which influence the options for legal forms of privatised enterprises. These factors and their relevance for the investor's option regarding the legal form can be fully compared with legal conditions in western industrial countries.

3.2 Legal forms of enterprises in Georgia

3.2.1 The legal forms of private enterprises

In Georgia the following main legal forms of enterprises can be registered:

- joint stock company
- company limited
- general partnership
- comandit partnership

It is also possible to start business as a physical person or as a co-operative. But both of these forms do not play any role for privatisation of port facilities and foreign investments in the transport sector. To complete the list it has to be mentioned that there are not yet privatised enterprises (transition of legal form). The Ports are state owned and are directly subordinated to the Ministry of Transport. The legal form in-between, the state enterprise and the privatised one is the state treasure enterprise .

Concerning the general, basic legislation (regulations on private ownership - except of the land -, entrepreneurs and foreign investments) in Georgia the legal Georgian business environment does not essentially differ from western standards. Under the aspect of foreign investments the forms of a joint stock company and company ltd. can be considered as being most common in Georgia. Investors operating in joint ventures in Georgia mainly decide to use the form of the joint stock company.

This form meets the specific conditions of privatisation (state majority of stocks, participation of employees) of larger economic subjects in Georgia and this form can be efficiently applied in connection with foreign investments.

3.2.2 The legal form of state treasure enterprise

This legal form is established in Georgia in order to promote and to ease the transitional process by the Georgian Law on Entrepreneurs in 1997. The legal form of treasury is crucial for the country and the whole social development under the aspect of economic reforms. Decision about the establishment of the treasury (state) enterprise is made by the state or the appropriate local authority. These directing bodies decide about the further type of the enterprise's activity, the composition of the board of administration, it appoints the director, defines the rights and responsibilities. The treasury enterprise is a legal person and has its own company name. The treasury enterprise is registered in the Entrepreneur Register.

Treasury enterprise is a specific legal and new form of enterprise in Georgia. So it is not included in the list of typical enterprises in other laws concerning privatisation. After the decision of state or local authority the treasury enterprise can be restructured into the JSC or LTI according to the Georgian legislation, if the enterprise is already registered in the Entrepreneur Register.

The port of Poti is a state enterprise and the port of Batumi a municipality port. The port of Poti has to be transferred into a state treasure enterprise before changing into a joint stock company.

Name	Definition	Advantages	Forms of taxes	Remarks
Joint-stock company JSC	<p>JSC is the company which has the equity capital divided into shares. The minimum nominal capital should be 15.000GEL (11.500\$). The cost of one share 1GEL or more. A company, having more than 50 partners or more than 500 employees must be established as J-S company.</p>	<ol style="list-style-type: none"> 1. The existence of the company does not depend on the change of company shareholders. 2. It is responsible with its property against the creditors 3. Each shareholder has the right to take part in the decision-making process 4. Due to the on-going transitional period the joint stock company meets the requirements of privatisation in the most efficient way 	<p>According the Georgian Tax Code all types of organisations have same form and rate of tax. Income tax from salaries (12%-20%) profit tax 20%, VAT, land tax, environmental tax, road tax for State budget and non-budget taxes on social insurance.</p>	<p>This form meets very well the requirements of the specific conditions of large company's privatisation. Nowadays, the Port of Poti is a State enterprise under the direction of Ministry of Transport, but distributing the profit independently. In the nearest future the reconstruction is foreseen. From the interviews with senior managers of the port it can be concluded that J-S is the most acceptable form for Poti Port.</p>
L.T.D	<p>The partnership responsibility regarding creditors is limited by its whole property, is Ltd. It can be founded by one person. The equity capital should be more than 2.000 GEL (1.500\$)</p>	<ol style="list-style-type: none"> 1. Can be established by one physical or juridical person 2. The minimum equity capital requires not a big amount of money 3. LTD is the juridical person and the owner of its property 4. LTD is established by the unification of the capital and the member of this organisation can leave the organisation at any time. 5. Responsibility is limited 	<p>see above, the legal form of enterprises has no influence on the tax rate</p>	<p>This form should be used especially for the spin off of clearly defined parts of larger former state enterprises and for the creation of small and medium sized enterprises in Georgia</p>

Name	Definition	Advantages	Forms of taxes	Remarks
General partnership - (GP)	<p>A partnership, which includes a number of physical persons doing independent business activities under a united company name and are responsible before creditors by their whole property.</p>	<p>Is established by agreement of two or more persons. The relations between partners are based on mutual confidence. Partners can be only physical persons.</p>	<p>see above</p>	<p>It is in principal the German society GbR it plays no role in the transport sector in Georgia at the time</p>
Comandit Partnership (CP)	<p>Is established by number of persons, that make entrepreneurial activities independently. Partners are divided into two categories: complementary and comanditor.</p>	<p>Does not require a minimum equity capital. Comanditor can be also the state. The complementary should be only physical persons</p>	<p>see above</p>	<p>It is very similar to the Kommanditgesellschaft</p>

3.3

3.3 Political Situation and Projects around the Ports

With their neighbour countries Georgia has good relationships. The southern neighbour Turkey needs Georgia as transit country on the way to the Caspian Basin and Central Asia, the northern neighbour Russia is together with Georgia member of the CIS and the eastern neighbour Azerbaijan is member of TRACECA and needs Georgia as well as transit country. Armenia, south-east of Georgia has good relationships by tradition.

Nevertheless, some conflict areas are existing. Georgia has almost 18 provinces with many different religious and cultural backgrounds. Open conflicts are existing with Abkhazia and North and South Ossetia. Here UN forces are involved in order to avoid that these conflicts are becoming hot again. In the rest of the republic the situation is quiet and safe.

Figures published recently show, that in 1997 the inflation rate was 6.5 %, the GIP increased by 12 % and the contribution of private enterprise to the GIP reached 80%. Nevertheless, the Republic of Georgia is committed to the IMF (International Monetary Fund) and therefore the state is not giving sovereignty guarantees. Worldbank and European Bank for Reconstruction and Development (EBRD) have stated, that they will give credits for the development projects, but only, if the projects are privatised and this means in accordance to the understanding of the two banks, a minimum 51 % of the shares has to be in the hands of private companies. It is also stated, that these companies should be foreign investors and only occasionally they will accept well known Georgian Companies amongst these 51 % shares.

For the time being, especially the Port of Poti is subject to various interests and projects. Below are the projects and activities stated:

- GTZ - Project on training for the Ports of Batumi and Poti
- Tacis TRACECA project "Feasibility Study on New Terminal facilities in the Georgian Ports"
- USAID project Privatisation of the Seaport of Poti
- SeaLand project CONTAINER terminal Poti
- Romanian Project on RAIL ferry connection Constanca and Poti including a Multi purpose Terminal in the extension Area
- Poti Port Projects for the extension area
- Project of the City of Poti for a new Port (south of the existing one)
- Japan International Co-operation Agency (JICA) preliminary studies on Georgian Ports
- Rail Ferry Project Illiychevsk Poti

In addition to this, many interested parties are coming up with proposals and ideas about the ports and the privatisation projects.

Within the near future the Government of Georgia will decide about the future privatisation concept for the port of Poti. The interest of the various parties in Poti Port shows, that the expectations are very high/

So far, only in Poti a joint venture company has been established with 50 % foreign and 50 % port shares.

This company has one berth and is handling basic scrap.

4. Commercial results of the privatisation concept

4.1 Revised figures

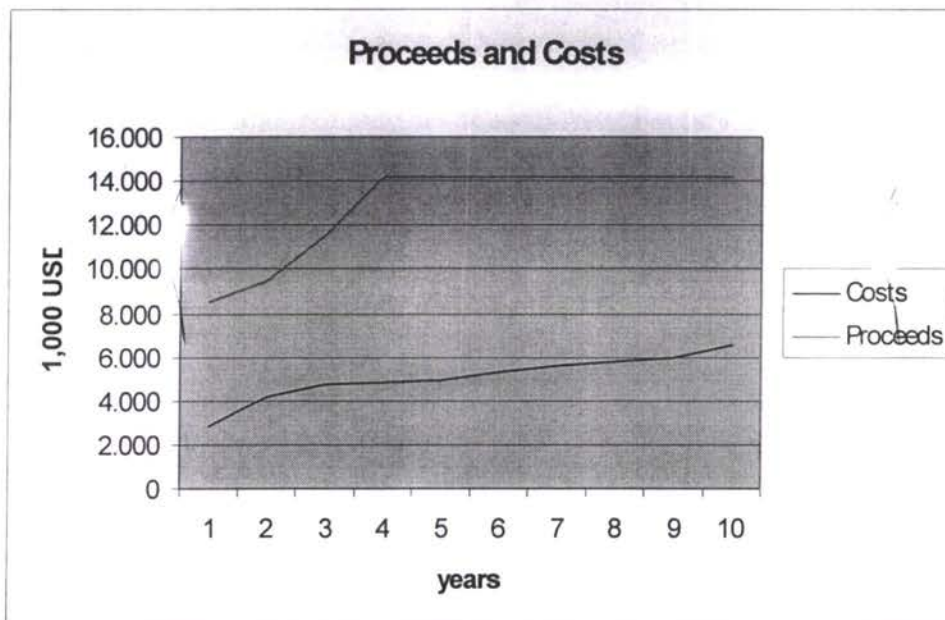
The figures of the revised Profit/Loss-Calculation for the first step of investments in the Poti Container Terminal Extension show a total investment sum of 19,840,000 USD (Volume VI table 4.3-1). There are included preparation, rehabilitation and new investments for the berths 6 and 7 with an area of 60,000 sqm and for the berths 12 to 14 with an area of 25,000 sqm.

As shown by the time axe, the main investments for berths 6 and 7 take place in the first two years, for the berths 12 to 14 in the second and third year. According to the depreciation time some replacement investments have to be done in the 6th and 7th year. Concerning the cost elements a deviation from the figures in the financial analysis (Vol. VI) is made for the land lease rate: it is reduced from 4 USD to 1 USD per sqm. The costs for the Operational company is calculated with a lumpsum of 1,000,000 USD per year.

The earnings depend on the forecasted container moves. The figures are:

Year	Container (TEU)	
	full	empty
1 (1998)	48,000	16,000
2 (1999)	52,940	17,500
3 (2000)	64,960	21,650
4 (2001)	79,730	26,580

The development during the first three month of 1998 confirms the forecasted container moves with 12,502 TEU. The capacity of the Extension Container Terminal will be attained in the 4th year, so that after this year the earnings will have the same amounts. The profit before the financing costs shows a sound basis between 5,2 mill. USD and 9,4 mill. USD. The following graph shows the course of the proceeds and the costs.



With the same assumptions as described in Vol. VI the calculation runs for the cash flow analysis for the container terminal extension were made.

The finance model calculates investments and the operating of the terminal for a period of ten years. Within this period the investments shall be reduced by operational earnings (cash flow). The cash flow is the sum of earnings after interest and tax and depreciation. A calculation run were made: with a calculated interest rate of 10%. This interest rate is not cost relevant, because the financing of the investment will be effected out of the share capital.

The total cash flow during the ten years amounts more than 60 mill. USD. After the 4th year there will be formed reserves, which sum up to 35 mill. USD in the 10th year. This amount can be used to invest e.g. in the new container terminal.

The operational turnover will increase from 8,6 mill. USD in the first year to 14,2 mill. USD in the 4th and the following years by reasons of capacity restriction (the max. possible container moves are 80,000 TEU)

**.Poti Container Terminal Extension: Cash flow analysis, real case,
calculated interest 10% but the finance will be out of share capital**

	approx.		1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Investment	in 1,000 US\$		9,962	7,935	1,258	0	0	285	400	0	0	0
Investment berth 6+7	in 1,000 US\$											
Investment berth 12-14	in 1,000 US\$											
Incidental expenses	in 1,000 US\$											
Investments total (per year)	in 1,000 US\$	100%	9,962	7,935	1,258	0	0	285	400	0	0	0
present value of investment	in 1,000 US\$		9,962	7,409	1,097	0	0	202	265	0	0	0
net total accumulated	in 1,000 US\$		9,962	17,897	14,391	10,377	5,193	-1,723	-8,423	-15,305	-22,045	-28,644
financed per Earnings incl. Deprec.	in 1,000 US\$		0	-4,764	-4,014	-5,184	-7,201	-7,099	-6,882	-6,740	-6,598	-6,437
present value of cash flow	in 1,000 US\$		0	-4,448	-3,499	-4,220	-5,473	-5,038	-4,560	-4,170	-3,812	-3,242
total accumulated	in 1,000 US\$		9,962	13,133	10,377	5,193	-2,008	-8,823	-15,305	-22,045	-28,644	-35,081
Proceeds	in 1,000 US\$		8,559	9,430	11,572	14,203	14,203	14,203	14,203	14,203	14,203	14,203
Handling	in 1,000 US\$											
Storage	in 1,000 US\$											
Other	in 1,000 US\$											
Proceeds total	in 1,000 US\$	100%	8,559	9,430	11,572	14,203	14,203	14,203	14,203	14,203	14,203	14,203
Total costs (with depreciation)			2,812	4,196	4,686	4,796	4,924	5,333	5,615	5,792	5,993	6,572
Costs (with depreciation)	in 1,000 US\$		7,427	7,757	9,249	9,403	13,749	14,076	14,236	14,416	15,771	17,117
Costs (without depreciation)	in 1,000 US\$	100%	2,247	2,859	3,151	3,261	3,389	3,687	3,886	4,063	4,264	4,843
EBITDA (Cash Flow)	in 1,000 US\$		6,312	6,571	8,421	10,942	10,814	10,516	10,317	10,140	9,939	9,360
Depreciation	in 1,000 US\$		564	1,337	1,535	1,535	1,535	1,646	1,729	1,729	1,729	1,729
EBIT	in 1,000 US\$		5,747	5,234	6,886	9,407	9,279	8,870	8,588	8,411	8,210	7,631
Accumulated Capital Requirements	in 1,000 US\$	10%	498	1,888	2,324	2,324	2,324	2,324	2,324	2,324	2,324	2,324
Earnings before Tax	in 1,000 US\$		5,249	3,345	4,561	7,083	6,955	6,545	6,264	6,086	5,885	5,306
Tax	in 1,000 US\$	20%	1,050	669	912	1,417	1,391	1,309	1,253	1,217	1,177	1,061
Earnings (after Interest & Tax)	in 1,000 US\$		4,199	2,676	3,649	5,666	5,564	5,236	5,011	4,869	4,708	4,245
Cash-Flow (after Interest & Tax)	in 1,000 US\$		4764	4014	5184	7201	7099	6882	6740	6598	6437	5974

5. Project financing

The project should be financed out of the share coming in from Georgian and Foreign Shareholders.

The Port of Poti will claim 48 % of the shares with an equity of 18 Million US\$.
The remaining 52 % will have an value of 19.5 Million US\$.

The total share capital of the Operation JS Company will be US\$ 37.500.000,--

With the US\$ 19.500.000 the whole investment plans of the first 3 years can be financed.

Remark: The Port of Poti equity of US\$ 18.000.000 are including the existing cranes at berth 7, the rail ferry ramp under construction as well as the new equipment delivered by the European Union and the "Goodwill" out of the existing business (Container handling, RoRo and forthcoming Rail-Ferry Operations).

6. How to attract investors

It is a decisive target of the suggested privatisation to exclude demands of the public budget for investment measures or trading losses of the port (res. the privatised part of the port, these are first of all the Poti Container Terminal and the Batumi Multi-Purpose-Terminal) widely. Therefore, the enterprise's continuous strengthening, the fulfilment of port-specific functions, and securing the country's transport market aims have to be the long-term-objectives. The step-by-step privatisation of the further terminal areas of the port is included here.

Following basic variants of the investor's interests can be described:

- A) Drawing in private capital (without specific business interest), e.g. from banks, financial institutions, and trading companies;
- B) Enlisting operators of the transport chain (transport enterprises, shipping companies, operators);
- C) Enlisting users and architects of the transport chain (shipping agents, integrators);
- D) Enlisting of supplementary service enterprises (depository operators, repair shops, hiring services).

The impact that each of these variants may have on the ports' res. the terminal areas development in terms of business is clarified by their different objectives.

Variant A:

The capital provider is orientated towards a return that lies above average and is riskless, or else promises a significant appreciation in connection with company shares. Normally he does not have an entrepreneurial interest.

Variant B:

The private transport chain operators expect effects of synergy, influence on further market shares, and a strengthening and stabilisation of their main business.

Variant C:

Users and organisers of the transport chains expect an increase in service performance, security of handling, and a strengthening of their market position. Know-how-transfer and an reasonable return could be a incentive to invest.

Variant D:

The supplementary service enterprises expect an expansion of their business activities, securing of new sites, entering new market segments as well as a reasonable return, at least in a long term view.

A qualitative evaluation of the variants' positive (+) and negative (-) effects on the entrepreneurial development of the ports reveals the following picture:

- | | | |
|------------|---|--|
| Variant A: | + | no ability to influence the company policy, it a reasonable return will be obtained |
| | - | sale/reversion of shares under misfortunate business development |
| Variant B: | + | Securing the expected development of volume, additional volume is to be expected |
| | - | Preferential treatment compared to other operators could lead to volume decrease |
| Variant C: | + | The port sites are secured within the transport networks |
| | - | Dependence on the disposal norms of the major forwarders and integrators |
| Variant D: | + | Spreading of the entrepreneurial risk, specific know-how increase and transfer |
| | - | Dependence on business development, bad risk, often weak capital foundation of the enterprises |

A weighing up of advantages and disadvantages by the prospective customers/investor groups can lead us to the recommendation to strive for a mixture of investors as broad as possible. The canvassing of investors should be laid out accordingly.

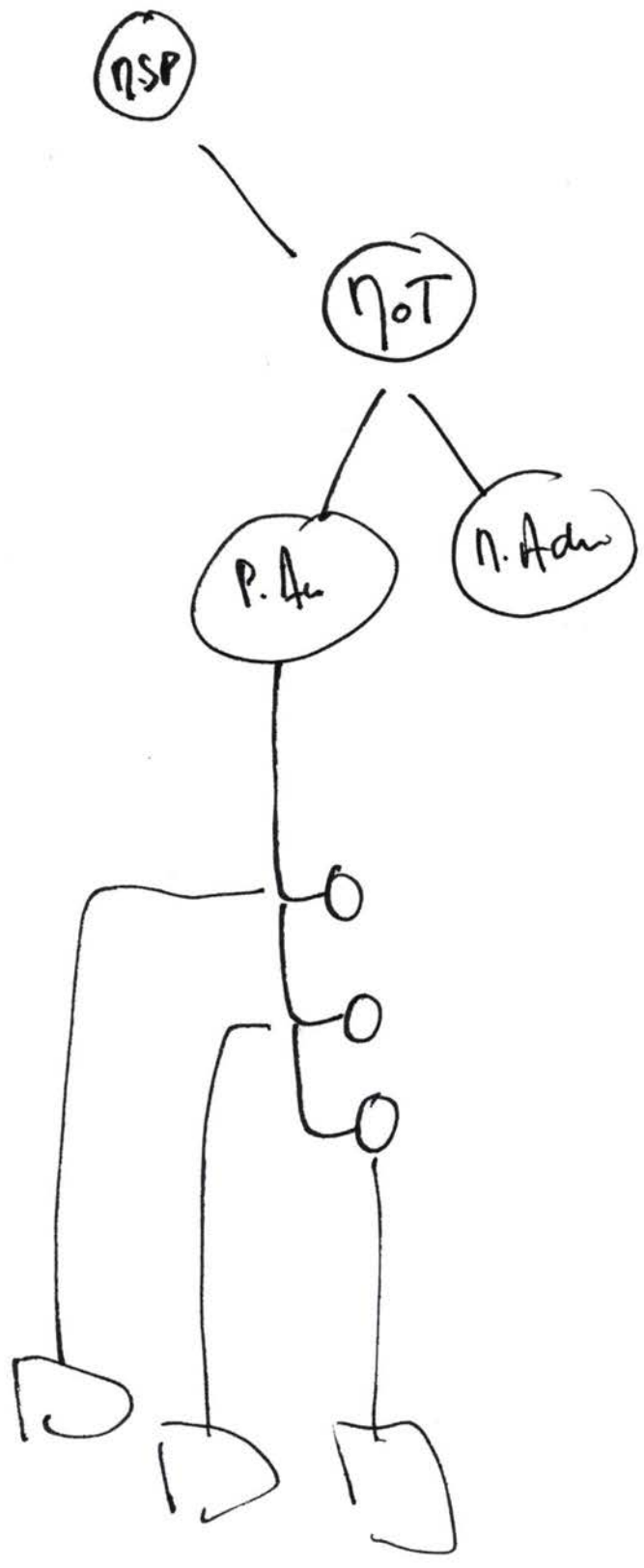
The complexity of the matter demonstrates that a general tendering for investors does not seem to recommend itself here. Rather than that the investors should be addressed directly, so each interest situation can be sounded out and frame conditions can be discussed about in individual preliminary meetings.

Thus the investor groups described above are to the fore of attention.

Conversations with investors res. potential shareholders were held. These conversations had an informal character.

In all conversations was made clear:

- A clear concept for the development of the ports exists.
- The financial involvement is required to be able to manage the rehabilitation and extension.
- The step-by-step proceeding and a broad investor basis lessen the risk and limit the financial involvement.
- The real development of port sites and the region as well as Georgia's transit function can be observed along with simultaneous limited involvement.
- The investors are partners from the very beginning and thus are able to secure a good market position.



Feasibility Study for New Terminal Facilities in the Georgian Ports.

Privatisation Concept

- . **Authority** : Three levels of authority will be established :
 - A Port Authority which will depend from the Georgian Maritime Administration and will cover the sovereign tasks such as maritime safety.
 - The port of Poti which will be established as a legal entity and will organise the common and commercial activities of the port
 - A Joint Stock Company with majority of private investors which will be in charge of the running of operations (container, RoRo) in the port and of the development of its commercial activities.

- . **JSC Shareholder** : 48% : Port of Poti (Ministry of Transport/ the Government of Georgia)
49% : private foreign investors (Companies, Banks,....)
3% : private Georgian investors
The total Georgian share holding will be 51%.

- . **JSC Share capital** : Total capital :US\$ 37.5 Millions capital :
 - 18 Millions equal to 48% held by the Port of Poti (existing installations, equipment)
 - 19.5 Millions equal to 52% of capital brought by Georgian and foreign investors.

- . **Process of the privatisation** :Logistical units of the ports will be privatised step by step by in order of priority and profitability. Privatisation can start immediately eg. the container terminal and RoRo unit could be privatised as soon as investors are identified.

The step by step privatisation offers a flexibility in the privatisation of the port according to the economic and financial needs . Due to this flexibility, the privatisation might be fast and attract a large number of investors each of them specialised in their activity. Higher proceeds can then be expected from the sale of each activity when the privatisation of the whole port will be completed.

- . **Ownership** The ownership of the different parts of the port (land, infrastructure....)will remain unchanged for the time being. As the privatisation focuses on the activities of the port, the ownership is in itself not an obstacle . The JSC will lease the land and berths to the State.

- . **Investment volume**. 116 Millions US\$ for the all port including new container terminal and new berth within 15 years and a return of investment in same period of time. Additional 40 Millions for new infrastructures (new breakwater).

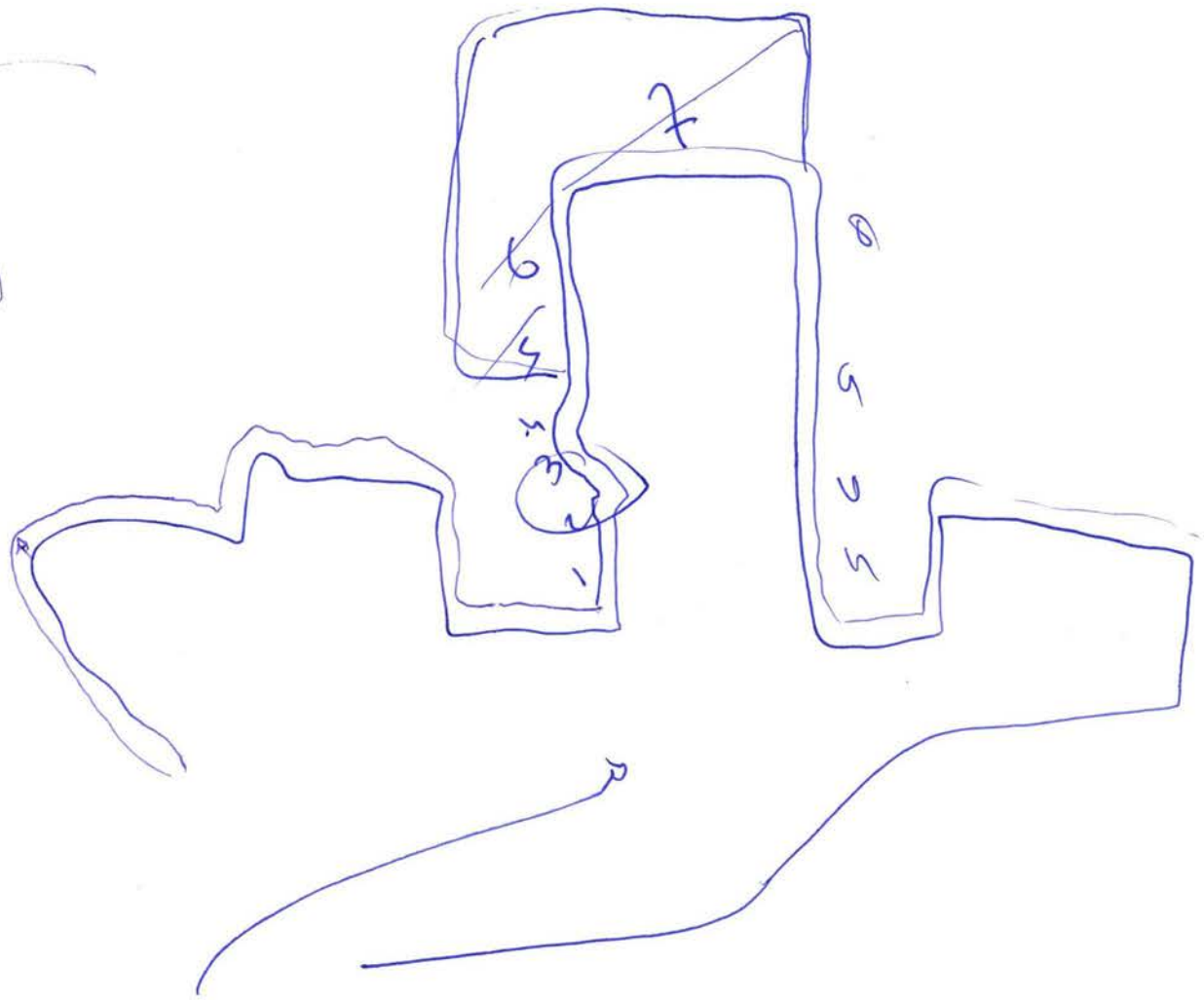
- . **Employment** The JSC takes over the required personnel from the port activity by activity . A specialised fund has to be established to ensure that wages are available for pensioners of the port.

- . **Competition**. The involvement of several operators and investors in the operations of the ports preserve a necessary competition considered as condition for a fair and harmonious development of the port.

- . **Management**. Within the JSC, a management company will be employed and will under a long term contract manage the commercial activities of the JSC and its related operations..

Conclusion . The proposed privatisation by activities allows for a better control by Georgia of this strategic asset and for a fast privatisation. It also preserves its crucial financial interests. Multiple shareholders in the JSC prevent the creation of a monopoly.

W/S



7. Potential investors

Conversations with immediately interested companies are to be continued. For this it recommends itself to outline an information memorandum, in which the most important information is concealed. The existing feasibility study is going to be the source from which the fundamental aspects will be gathered.

List of companies interested in a participation as shareholder of the Port Operation JSC:

B.Dettmer, Berlin, Germany
Barwil, Georgia
Barwil, Norway
Betz, Willy Germany
Calbertson, France
Ceres
Danzas Holding, Germany
Deugro, France
Dr. Lassmann, Austria
EBRD, London
GTE, Georgia
GTG, Georgia
Johann Birkart, Germany
Kavtrex, Georgia
Ketner Spedition Germany
Kuehne & Nagel, Switzerland
Maersk, Danmark
Militzer & Muench, Switzerland
MSC, Italy
Murphys International, Great Britain
Neshtrans, Georgia
P & O, Nedlloyd, Great Britain
Panalpina, Germany
Schenker - Rhenbus A.G., Germany
Sealand, USA
Voucher Leader Invest, Georgia
W.Willemsen, Norway

+ Cahalis. Creece -

This list is not complete, because there are ongoing discussion in West Europe about other interested companies.

8. Consequences of privatisation

The suggestions for the step-by-step privatisation of the ports have to orient themselves according to the targets of the leading participants.

From the port administration's perspective following targets come to the fore:

- The rescue operation of the port plants via the rehabilitation of the suitable plant parts;
- Substitute investment for obsolete machinery and property;
- Rationalisation of procedures through training and further qualification of the required staff as well as the use of modern equipment;
- And so safeguarding of the required jobs;
- Possibility to develop a social plan for the necessary socially justifiable job cuts (e.g. the retrenchment of 100 employees is going to require annual funds of approx. US\$ 100.000);
- Know-how-transfer via integration of Western enterprises and experts into the port activities;
- Creating the prerequisites to increase and ensure the competitiveness and attractiveness of the ports within an international competition;
- Fund influx from the private capital market as a supplement to the public national and international funds;
- Strengthening of the port's independence against political influences.

The interests of the mortmain res. the government tally in some points with those of the port. Beyond this the state and government see the following effects and uses:

- Stabilisation of the port's activities;
- Economic development for towns and regions;
- Strengthening of Georgia's international position;
- Safeguarding of jobs through sound jobs with a guaranteed future;
- Effects on the job market situation through enterprises and businesses linked to the transport industry (multiplier effect);
- Security and increase of tax revenues;
- Reducing of public funds for the ports through increased use of private capital;
- And so release public budgets from investments and from trading losses;
- Improvement of traffic infrastructure as an important over-all economic task.

The hoped for benefits for the private sector have already been mentioned; to summarise:

- Priority berthing or priority handling of container, trailer within the Terminals
- Long-term return for the used capital;
- Improvement of the competition situation within the Trans-Caucasian and Central Asian transport and trading market;
- Securing and stabilisation of logistic chains;
- Forming of strategic advances for the firms;
- A right to a say in terminal-relevant matters.

9. Next Steps

The Government of Georgia should make a formal decision in which direction the Port of Poti has to be developed. In case, that the decision will be in line with the proposals made by the Tacis Team, the Government of Georgia should nominate and entitle the Team to attract the Investors together with the Port and to form the Joint Venture Company and to tender the necessary construction work and required equipment.

The Tacis team will work out after the decision is made in line with the European Proposal a folder, containing all relevant data about this first privatisation project.