



**Analysis of the Draft Methodology
and Procedures for Determining
Market Competitiveness and
Authorized Undertakings with
Significant Market Power against
the EU directives and UK guidelines
and existing legal framework**

KPMG

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GLOSSARY

Association Agreement	Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Georgia, of the other part
ComLaw	Law of Georgia on Electronic Communications
Commission	Georgian National Communications Commission
EU	European Union
Framework Directive	Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a Common Regulatory Framework for Electronic Communications Networks and Services
Methodology	Draft Methodology and Procedures for Determining Market Competitiveness and Authorized Undertakings with Significant Market Power
OTT	Over-The-Top
SMP	Significant Market Power
UK	United Kingdom
Magticom	Magticom LLC
KPMG	KPMG Georgia LLC
Report Definition	Analysis of the Draft Methodology and Procedures for Determining Market Competitiveness and Authorized Undertakings with Significant Market Power against the EU directives and UK directives guidelines and existing legal framework

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1. EXECUTIVE SUMMARY

Concerned with the potential impact of the Georgia's Methodology and Procedures for Determining Market Competitiveness and Authorized Undertakings with SMP regulation on the electronic communications sector, Magticom LLC commissioned KPMG to conduct an analysis on alignment of the Methodology with the EU legislation, best practices, and Georgian legislation. The objective was to make a bridge with EU and UK guidelines, assess potential impact of their misalignment and aspects of contradictions with the ComLaw to understand whether the Methodology may be enforced in practice in compliance with the overall legal framework. KPMG aimed to produce a comprehensive report, focusing on the Methodology, to indicate alignments, misalignments, and areas for improvement in fields like relevant market definition, competition analysis, and the imposition of specific obligations on entities with Significant Market Power (SMP). This report endeavors to offer valuable insights and suggestions to enhance regulatory practices in the Georgia's electronic communications sector, benefiting transparency and comprehension for the stakeholders, including Magticom.

While the Methodology partially aligns with the three frameworks used for analysis, specific points warrant attention due to potential significant impacts. The first one refers to the market definition where even though the analysis acknowledges a robust framework with emphasis on geographic boundaries, flexibility, and alignment with global standards, a crucial gap is identified - the absence of a defined basic geographic unit. To enhance the market definition process, it is recommended to incorporate the definition of a basic geographic unit as a precursor to delineation. Additionally, the Report highlights the possibility allowed by the Methodology to regulate the retail market, contrasting with regions governed by EU and UK regulations where such regulation is not present.

The challenges in aligning the Methodology with the ComLaw to comply with the EU-Georgia Association Agreement are highlighted. Since ComLaw was not amended to harmonize with EU legislation and guidelines, there are disparities, especially in the Significant Market Power (SMP) definition. The Commission's decision to initiate public administrative proceedings for Methodology approval shows a commitment to EU principles, but concerns arise about its adequacy in achieving Association Agreement compliance. The Methodology, a sub-legislative normative act, complements ComLaw but should not stand alone. Misalignments are identified in certain aspects, including definition of SMP, service substitutability, application of primary and secondary criteria for market segment determination and joint SMP. Such contradictions warrant the need for first, amending the ComLaw and then, adopting the Methodology to ensure compliance of the secondary legislation with the primary law.



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2. METHODOLOGY OVERVIEW

To give a short summary of the Methodology, it was grouped into five main parts, with each part being the main focus:

- 1. Clarification of definitions and key terms used in the Methodology.**
- 2. Procedures and criteria to identification of relevant market segments** starting with establishing the product or service boundaries of the relevant market through the determination of intersubstitutability based on objective characteristics, prices, function, and competition conditions; assessing the supply and demand substitutability and establishing geographic boundaries.
- 3. Procedures for determining the level of competition of the relevant market segment** assessed through an analysis of the segments outlined in the previous step, considering the anticipated development of it, its end-user perspectives, demand and supply side substitutability, and current and future market conditions.
- 4. Assessment of the SMP in the relevant market segment(s)** considering its market shares, infrastructure control, technological advantages, and the level of absence of competition. Additionally, the extension of the single SMP to the concept of joint SMP, where a group of companies may collectively dominate a market.
- 5. Conditions and criteria to apply ex-ante regulations by the Commission** highlighting the prioritizing on imposing these types of regulations on the relevant wholesale market segments but extending to the possibility of regulating the retail part when the wholesale regulation fails. The criteria for ex-ante regulations are summarised in three factors, the presence of significant and lasting barriers to entry, the market structure is evaluated to determine if effective competition is achievable within a reasonable timeframe, and the sufficiency of competition law is assessed in addressing persistent market failures. If all of these criteria are met, specific regulatory obligations may be deemed necessary to ensure fair competition and address market challenges.

3. METHODOLOGY VS OTHER EUROPEAN REGULATIONS

3.1. Description of the EU Guidelines and their Comparison with the Methodology : Alignments and Divergencies in Determining Market Competitiveness and Authorized Undertakings with SMP

In assessing whether an undertaking has SMP, that is whether it "*enjoys a position of economic strength affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately consumers*"¹, defining the relevant market is of fundamental importance since effective competition can only be assessed against this definition. This definition is not a mechanical or abstract process but requires the analysis of all available evidence of past market behavior and an overall understanding of the mechanics of a given sector.

Beginning with an exploration of regulatory methodologies, we underscore the parallels between Methodology's approach and the guidelines set forth by the EU and UK for evaluating market competitiveness and discerning SMPs within the electronic communications sector. Key points of convergence include the shared emphasis on accurately defining relevant markets and evaluating products or services based on interchangeability and substitutability. The use of the Hypothetical Monopoly Test and acknowledgment of chain substitutability are common methods. The criteria test for implementing *ex-ante* regulation are consistently used, considering substantial barriers to entry, market structure, and inadequacy of competition law. This alignment ensures a comprehensive and consistent assessment of markets potentially requiring regulatory intervention.

However, there are discrepancies among the EU, UK guidelines and the Methodology regarding the percentage thresholds for defining SMP, whether in the context of a single SMP definition or a joint SMP definition. In EU and UK frameworks, when defining a single SMP based on market share dominance, two crucial concepts emerge: (a) **Very Large Market Share** is generally considered evidence of a dominant position, except in exceptional circumstances, and (b) **Significant Threshold** at which concerns about dominance begin to arise. The following table will outline these distinctions:

Single SMP	UK ²	EU ³
Very Large Market Share	>50%	>50%
Significant Threshold	>40%	>40%

The Methodology does not cover these two concepts, instead it mentions that an authorized undertaking shall be identified as having SMP if it holds at least 40% of the market share. In contrast with UK and EU framework, 40% threshold does not give rise to concerns about dominance but rather effectively acts as the absolute threshold for determining the SMP (please see section 4.2.1 of this Report). In addition, the Methodology defines limits on market share percentages for Joint SMP whereas such

¹ Article 14 (2) of Directive 2002/21/EC

² Point 7.9, Sub-Section Approach to SMP assessment, Section 7 of Business Connectivity Market Review

³ Point 55, Sub-Section 3.1. of (EU) 2018/2374 of the European Commission and footnote 54.

limits are not defined neither in the EU or UK frameworks. ,So it is necessary to revise the Methodology in accordance with the practices of both the EU and the UK in terms of market share thresholds in the context of a Single SMP definition or a Joint SMP definition.

Additionally, the EU and UK guidelines incorporate a crucial initial phase involving the definition of a primary geographic unit, a step absent in the Methodology. Notably, the EU guidelines underwent evolution in response to concerns expressed about the previous legislation. According to the 2002 regulations, market definition process was initiated by determining behavioral constraints, but by 2020, this was deemed insufficient. In response, the EU introduced a foundational step, defining a basic geographic unit as the starting point for assessing competitive conditions, *“For the purpose of the geographic market definition, national regulatory authorities should define a basic geographic unit as a starting point for assessing competitive conditions”*⁴. Complementary, UK guidelines has emphasized the necessity of this foundational step, as per their document on geographic market definition, *“(…) we used three main steps to undertake a detailed geographic market definition exercise based on identifying variations in competitive conditions: the selection of the basic geographic unit, for example postcodes or exchange areas or administrative areas (…)”*⁵. The absence of this step in the Methodology raises concerns about transparency and potential inefficiencies in market boundary definition.

Another divergence relates to *ex-ante* regulation. While the Methodology recognizes the potential need for retail market intervention if wholesale market obligations are insufficient, the EU guidelines prioritize wholesale market regulation. *“Ex-ante regulation imposed at the wholesale level, which is in principle less intrusive than retail regulation, is considered to be sufficient to tackle potential competition problems on the related downstream retail market or markets”*⁶. The EU doesn't have any kind of a specific regulator for the retail market, on the contrary it is relying on public services for assessment and consumer protection. For example, in Portugal this public service is done by Competition Authority which is *ex-post*. The Georgian approach, allowing specific regulatory obligations on the retail market, may introduce additional complexities for operators compared to the EU and UK regulations where only the wholesale market is regulated. This divergence poses risks in ensuring a correct assessment of competitiveness by the Commission and potential impacts on SMPs operations and strategies within the retail sector. The findings underscore the importance of continually aligning methodologies with evolving regulatory standards for effective market analyses.

Another difference was identified in the guidelines on market analysis. Within the assessment of SMP under the EU framework, there is a specific reference to take into account OTTs when conducting product market analysis. This reference emphasizes the importance of considering these services on a

⁴ Article 37 of (EU) 2020/2245 of 18 December 2020

⁵ Section 5 (5.9) of Ofcom Geographic market definition

⁶ Article 173 of (EU) 2018/1972 of the European Parliament

forward-looking basis as partial or full substitutes to traditional telecommunications services. The Methodology omits this reference completely.

4. METHODOLOGY VS COMLAW

4.1. Justification of amendments of the Methodology before amending of the ComLaw

Obligations of Georgia in the field of electronic communication networks and services are determined in sub-section 5 of the Association Agreement. Article 113 of the Association Agreement highlights the importance of the gradual approximation of the existing and future legislation of Georgia to the EU legislation in the field of electronic communications. Key EU legislation regulating relevant product and service markets susceptible to *ex ante* regulation is Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a Common Regulatory Framework for Framework Directive.

With the purpose of approximation of the Georgian legislation with the Association Agreement in the field of the electronic communications, the package of amendments to the ComLaw was prepared in 2018. The 2018 amendments package included changes to the ComLaw to approximate certain regulations with the Framework Directive, including definition of SMP, powers to carry out *ex ante* regulation etc. ⁷ The amendments were not adopted.⁸

To demonstrate the need for adoption of the amendments to the Law, ComLaw provides definition of SMP as “*significant market power of the authorized person on the relevant segment of the service market i.e., the situation when the analysis conducted by the Commission confirms that the authorized person does not have competitors, is protected from the significant competition or its competitive position provides the entity with the possibility to have significant influence*. However, the Framework Directive (as amended) defines SMP as the situation when an undertaking “[...] enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers⁹”. Consequently, differences between ComLaw and the EU legislation may be observed at least on the level of definition of SMP.

In its decision on commencement of the public administrative proceedings on approval of the Methodology, the Commission stipulated that because of the consultations with the experts, it was decided to reflect the principles of EU legislation and best practice in the sub-legislative normative act (i.e., Methodology) before adoption of amendments to ComLaw. ¹⁰ While the choice of

⁵ Annex 5 of Annual Report of Georgia’s National Communications Commission (2018)

⁸ ComLaw, article 2.z⁶.

⁹ Framework Directive, article 14.2.

¹⁰ Decision #g-23-23/517 of the Commission, dated 9 November 2023.

legislative action from the available options is a matter of domestic law, whether the adoption of the Methodology is sufficient for implementation of the EU legislation should be evaluated considering the content of the Methodology itself.

Since the Framework Directive requires change of definition of SMP and other key amendments in ComLaw, adoption of the Methodology may not be considered as necessarily the most appropriate policy action to comply with the Association Agreement. To begin with, the Commissions' regulatory powers in the telecommunications sector are defined and limited by the ComLaw. The ComLaw is the key legislation setting out the sector regulatory framework i.e., primary normative act. It may be clarified or supplemented by secondary legislation. However, such secondary legislation cannot change the primary law or increase the powers of regulatory bodies as defined in it. Moreover, the Framework Directive itself requires Member States to “adopt and publish the laws, regulations, and administrative provisions necessary to comply with this Directive [...]”. Therefore, the need to amend primary legislation is highlighted in the Association Agreement as the form of approximation with the EU Legislation.

4.2. Certain Misalignments of the Provisions of the Methodology with ComLaw

Georgian legislation is divided between the legislative and sub-legislative normative acts. Sub-legislative normative acts may be adopted by the relevant authorities only to implement the legislative act and in cases determined in the relevant legislative act.¹¹ Therefore, the sub-legislative normative acts do not have statutory capacity of extending or modifying the regulation of matter established by the legislative act.

The Methodology, as suggested, represents the draft sub-legislative normative act. The Methodology provides the rules and procedures for conducting *ex ante* evaluation. However, it is not a self-sufficient document to fully regulate the scope of application. Rather, the Methodology is and should be construed in conjunction with the ComLaw. While using the Methodology to conduct the *ex-ante* evaluation, the Commission should make sure that the applicable legal framework established by the virtue of ComLaw is duly observed and enforced.

We have identified certain misalignments, requiring due attention to avoid contradiction of the sub-legislative normative act with the primary legislation.

4.2.1. Definition of Authorized Entities with SMP

Due to the non-alignment of definition of the significant market power in the ComLaw with the EU legislation, the first notable difference between the Methodology and the ComLaw should be observed in definition of the SMP itself. Article 14.1 of the Methodology provides that “*an authorized undertaking shall be deemed to have significant market power if, either individually or jointly with*

¹¹ Law of Georgia on Normative Acts, article 7.

others, it enjoys a position equivalent to dominance, namely a position of economic strength affording it the power to behave independently of customers and competitors.” This definition is fully aligned with the definition of SMP in the Framework Directive, however, contradicts the wording in the ComLaw. Definition of SMP in the ComLaw refers to not having competitors or protection from significant competition as well as ability to unilaterally influence market and limit competition. On the other hand, Methodology refers to a position equivalent to dominance and giving power to act without regard for customers and competitors. The criteria for determining whether an authorized person has significant market power is a key area of regulation under the Methodology. Therefore, its compliance with the ComLaw in this regard is essential.

ComLaw refers to the primary and secondary criteria in relation to defining significant market power of an authorized person.¹² ComLaw further stipulates that determination of the SMP takes place based on the primary and secondary criteria.¹³ Further, while determining the SMP and specific obligations of entities having significant market power, except for the primary criteria, secondary criteria are applied that “objectively evaluates the possibility of the SMP defined as per the primary criteria to limit the competition on the market and to carry out anti-competitive actions”.¹⁴ ComLaw clearly determines that the Commission shall define the secondary criteria considering the analytical factors.¹⁵

Methodology also stipulates that for determining SMP, secondary criteria shall be used together with the primary criteria.¹⁶ However, in article 14.4, the Methodology states that if a particular criterion listed as one of the secondary criteria is not sufficient for determining that entity has SMP, Commission shall decide the matter by using several or all of the secondary criteria in combination. Moreover, the Commission is also authorized to rely on ‘other criteria’ in parallel or as an alternative to the secondary criteria determined in the Methodology for evaluating the market power of the authorized entities.¹⁷

Provisions of the ComLaw in relation to the application of criteria to defining SMP may be interpreted to require use of primary criteria as determined in the ComLaw (referring to the market share) and the secondary criteria which is defined by the Commission separately, limiting the power of the Commission to go beyond the secondary criteria. This understanding of the ComLaw is supported with the need to have clear guidance for the market for the authorized entities as to what actions or situations qualify them as those having significant market power. By adding “other criteria” beyond the primary and secondary criteria (defined in the Methodology), the Methodology may be

¹² ComLaw, article 21.4.

¹³ ComLaw, article 22.1(d).

¹⁴ ComLaw, article 22.12.

¹⁵ ComLaw, article 22.12.

¹⁶ Methodology, article 14.3.

¹⁷ Methodology, article 14.5.

understood as extending the scope of the Commission's powers in relation to evaluating the market beyond the authority granted under the ComLaw.

Another aspect of relevance is the list of secondary criteria itself as provided in article 14.2 of the Methodology. As emphasized above, the ComLaw requires use of the primary and secondary criteria in conjunction to determine whether entity has significant market power. More specifically, secondary criteria should have a function of incorporating the qualitative conditions in defining the market power by focusing on the actual potential of the entity to limit or restrict competition in the market. Therefore, the ComLaw may be interpreted in a way to requiring the Commission to use the secondary criteria to challenge the primary criteria (market share) by not only considering entities with less than 40% market share as having SMP due to secondary criteria, but also, determining that despite being above the threshold, the entity may still not be qualified as having SMP due to the existence of secondary criteria.

4.2.2. Elements for Analyzing Competitiveness

ComLaw requires consideration of conditions of the demand-side and supply-side substitution while conducting competitiveness analysis.¹⁸ In addition, ComLaw gives value to the persons having intention to get authorization for providing the similar service in the market.¹⁹

ComLaw defines 'demand-side substitution' as: "ability of a user to switch to available substitute services that satisfy his/her requirements with a similar price, quality and volume".²⁰ As for the 'supply-side substitution' the definition reads as follows: " (...) *the possibility of providing intersubstitutable service types to users by authorized persons in a competitive service market.*"²¹

The Methodology does not provide separate definitions of demand-side or supply-side substitutions. Rather, while addressing the factors for the competitiveness analysis, it refers to the set of indicators that should be evaluated for determining the substitutable services from the side of consumers. According to the Methodology, "*the categories of such indicators may include user preferences for the specific service characteristics, prices, barriers to and costs of switching to any other service.*" The Methodology further clarifies that if the cost of switching to another service is significant, service will not be considered as intersubstitutable.²² In relation to the supply-side substitution, the Methodology determines that supply side substitution may be considered "[...] *if the incumbent service providers may switch to the production of an alternative intersubstitutable unit without significant additional costs in a short period of time in response to small intransitive changes in product/service prices.*"²³

¹⁸ ComLaw, article 22.4(b).

¹⁹ ComLaw, article 22.4.

²⁰ ComLaw, article 2.z¹¹

²¹ ComLaw, article 2.z⁴

²² Methodology, article 6.2.

²³ Methodology, article 6.10.

While regulating the consideration of the demand-side and supply-side substitution, the wording used in the Methodology may be interpreted as effectively extending definition of both terms as given in the ComLaw. Adding the criteria of the cost of switching from one to another service (from the perspective of the provider or consumer) is not supported by the ComLaw. Therefore, the Methodology may be understood to limiting the level of impact of demand-side or supply-side substitution in market competitiveness analysis since the cost of switching between the services may in fact be the factor decreasing intersubstitutable services in the market.

ComLaw requires considering the existing level of concentration and existing authorized persons on the market as well as market entry hindrances for the persons willing to get authorization. However, the Methodology stipulates that while determining the relevant market segment, the Commission shall identify all market actors as well as those authorized persons who potentially have possibility (technical, technological, financial, investment etc.) to provide the intersubstitutable services in the relevant segment in a brief period of time.²⁴ This provision may prove problematic in two areas. First, Methodology no longer considers the persons attempting or planning to get authorization in the market analysis, therefore, the number of relevant market actors is limited as compared with the law. Second, the Methodology may be interpreted to determine additional criteria – existing other authorized persons with potential to provide substitutable service without any evidence of any willingness to enter the market. Therefore, the misalignment of the Methodology with the ComLaw in this regard may have the impact of changing the number of entities to be considered while market analysis considering the particulars of market – whether other authorized persons having potential to provide similar services or whether there are non-market participants with the intention to enter the market and compete with the existing authorized entities.

4.2.3. Combined Markets and SMP

ComLaw defines the geographic borders of the service market as “*the geographic (territorial) segment of the service market differentiated with the homogeneous competition conditions*”.²⁵ Furthermore, the ComLaw clearly refers to the single market segment and allows consideration of closely connected market segment only while evaluating the significant market power in such segment.²⁶

The Methodology authorizes the Commission to include two or more markets in the same market segment if either: separate services have homogenous competitive characteristics or there is common tariff restriction on the market. The Methodology also allows inclusion of non-intersubstitutable services in the single service segment if services are provided in package to the consumer by the authorized person.²⁵

²⁴ Methodology, article 6.3.

²⁵ ComLaw, article 2.z⁸

²⁶ ComLaw, article 22.7.

ComLaw does not provide the Commission with the possibility to unify or join market segments. Market segment unifications may have substantial impact on the determination of the significant market power which is measured in relation to the specific market only. Therefore, the Methodology may be interpreted as contradicting the ComLaw.

Moreover, in defining the 'closely connected segments', the ComLaw refers to contractual relations between one or more operators or structural connection of their networks giving such operator(s) possibility to use significant market power in one segment to gain or increase such power in another segment.²⁷

The Methodology (article 8.1) provides different definition of the connected segment.²⁸ More specifically, there is reference to not only contractual relationship and infrastructural connections of networks, but also, overall vertical integration and horizontal connections and qualitative characteristics of the operators, nature of inter-relation and potentiality of joint actions. As a result, the Methodology may be interpreted to be effectively extending the definition of the closely connected markets as provided in the ComLaw.

Finally, definition of the joint significant market power should be analyzed. In the ComLaw, several authorized entities are considered as having joint significant market power if on the relevant service market: a) total market share of two authorized persons is at least 60% and each has at least 25%; b) market share of three authorized entities is at least 80% and each has at least 15%.²⁹ Unlike the ComLaw, the Methodology adds qualitative criteria. In addition to the market share requirement, which is treated under the Methodology as the primary criteria, the three cumulative conditions of silent coordination shall also be present to determine that entities jointly have significant market power.³⁰ Therefore, the Methodology may be understood as establishing new criteria - qualitative conditions for evaluating the entities.

²⁷ ComLaw, article 2.z¹²

²⁸ Methodology, article 8.1.

²⁹ ComLaw, article 22.11.

³⁰ Methodology, article 15.

5. CONCLUSION

In conclusion, the draft Methodology for Determining Market Competitiveness and Authorized Undertakings with SMP in the Georgian electronic communications sector is a comprehensive and forward-thinking regulatory tool. It has been developed to align with the evolving landscape of the industry and aims to foster fair competition, ensure a level playing field, and promote sustainable growth. The methodology prioritizes transparency, adaptability, and inclusivity in regulatory processes, contributing to a regulatory framework that supports innovation and industry development.

When compared with the EU and UK guidelines, while some alignments may be observed, the methodology demonstrates significant divergences, particularly: (1) in the market share percentages to define a single SMP and a joint SMP, (2) in the methodology's approach to geographic market definition, absence of a foundational step in defining a basic geographic unit, and (3) in the potential imposition of regulation in retail market. These differences raise concerns about transparency, efficiency, and the methodology's alignment with European best practices.

Furthermore, the report identifies that in some points the draft Methodology aims to align with EU standards as per the EU-Georgia Association Agreement. However, notable misalignments with the existing Law on Electronic Communications raise concerns. Key points of contention include discrepancies in the definition of SMP, elements for analyzing competitiveness, and the treatment of combined markets and joint SMP. The Methodology's approach to combined markets may conflict with the ComLaw's insistence on a single market segment, and the qualitative criteria for joint significant market power introduce complexity.

Considering these findings, as a starting point, the Georgian legal framework should be updated to ensure the alignment of the ComLaw and the Methodology and, additionally the Methodology needs to undergo further review and updates to align the Methodology with EU and UK guidelines.



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