

TRANSFORMATION OF THE LOCAL BUDGETS' ROLE: THE EXPERIENCE OF UKRAINE IN THE CONTEXT OF GLOBALIZATION

Olena Zelenko¹, Liudmyla Denyshchenko²

Abstract. *The purpose* of this study is to determine the peculiarities of the development of local budgets in Ukraine in the frame of decentralization reform in the context of established trends in local budgeting in other countries. *The research methodology* is based on the theory of financial globalization and involves methods of dialectics, methods and principles of scientific knowledge, tools of analysis and synthesis, expert evaluation, generalization and analogy. *As a result* of the research, the foreign experience of forming local budgets is highlighted and the peculiarities of this process in different countries of the world are determined; a review of existing publications and an analysis of the dynamics of the structure of local budgets and Ukraine are done; qualitative characteristic of the current situation and recommendations for further development of the local budgeting process in Ukraine in the current conditions of globalization are provided. Among the main recommendations for increasing the revenue part of local budgets there are the following: creation of additional conditions by the state and local governments to improve the business climate in communities; inventory and arrangement of community land funds; creation and arrangement of the real estate register; audit of the communal enterprises activities of the community in order to find additional opportunities to increase the efficiency of their activities; support and motivation of local business for further activity and development; intensification of the centers of administrative services and search for opportunities which will improve the provision of paid services of any complexity in the short term; promoting the development of domestic tourism. *The practical value* of the results of this research is that the proposed recommendations are general, relevant and can be used for all territorial communities of Ukraine with no exception. The analysis of trends in the context of local budgeting development processes in other countries and the current situation regarding decentralization reform allowed us to conclude that Ukraine has chosen the right direction, which has a positive impact on the financial capacity of local communities. Ukraine's path towards transforming the role of local budgets, despite the similarity of the general features of local budget restructuring, should be unique. The implementation of the presented proposals will contribute to the successful completion of the decentralization reform and the full implementation of the role of local budgets – ensuring sustainable financial capacity and meeting all the needs of the inhabitants of a particular area.

Key words: local budget, financial capacity, structure, source of income, international experience.

JEL Classification: E62, F01, H61

1. Introduction

Every inhabitant of an urban or rural community has the right to modern medicine and education, accessible and high-quality administrative, communal, social services, good roads, clean and lighted streets. Everyone will be able to influence the quality of these benefits only when it is possible to establish direct contact with those responsible for providing all benefits. The closest

government representatives to the community are local governments: village, settlement, city councils and their executive committees. Therefore, they must have broad powers and sufficient financial resources to be able to solve all the necessary local issues, problems and be responsible for it.

That is why Ukraine has begun the process of decentralization, which involves the transfer of powers

Corresponding author:

¹ Volodymyr Dahl East Ukrainian National University, Ukraine.

E-mail: zelenko.olena@gmail.com

ORCID: <https://orcid.org/0000-0003-4880-246X>

ResearcherID: V-9966-2017

² Volodymyr Dahl East Ukrainian National University, Ukraine.

E-mail: ludadenishenko@gmail.com

ORCID: <https://orcid.org/0000-0002-8160-7343>

and financial resources from state to local authorities. A key aspect in this process is the financial resources that are mobilized in the local budget and spent in the relevant area. Today, among scholars, the concept of “local budget” is defined as a system of formation, distribution and use of financial resources to provide local authorities with the functions and tasks assigned to them, both their own and delegated (Denyshchenko, 2018). The problem of the adequacy of the process of filling the revenue side in local budgets to meet the needs of the community and its compliance with modern world trends in the context of globalization is relevant today, this is about it and will be discussed in this paper. Thus, the purpose of the research is to determine the peculiarities of the local budgets’ development of Ukraine in the decentralization reform frame in the context of established local budgeting trends for other countries. The tasks of this research are: highlighting the foreign experience of local budgets and identifying the features of this process in different countries; review of available publications and analysis of the dynamics of the local budgets’ structure in Ukraine; qualitative description of the current situation and providing recommendations for further development of the local budgeting process in Ukraine in the current conditions of globalization.

2. World experience in local budgets’ forming

The formation of the budget system is in accordance with economic and legal regulations and the state system. The three-tier system is formed in countries with a federal system (USA, Germany, Canada, Switzerland). In such countries, the peculiarities of the formation of local budgets are determined by both legislative documents at the state level and the legislation of the federation. The two-tier budget system is formed in unitary countries (Italy, France, Japan) and there all the norms of formation are determined only at the national level.

In countries where there is a large difference in budget support, there is usually a high level of centralization of the budget system. Conversely, where the difference in the budget support of individual territorial units is small, a decentralized system is usually formed. According to it, local budgets are a separate component of the budget system that is not included in the state or regional budgets of the highest level.

The experience of functioning of budget systems in different countries of the world demonstrates greater efficiency of the decentralized type, because the financial resources accumulated on this principle are more mobile, more quickly distributed according to the available needs of the community.

The main forms of building budget systems in the world were qualitatively analyzed by Buryachenko A.,

who identified four groups of countries (Buryachenko, 2014):

1. Countries with a high level of independence of regional and local government, based on broad tax powers (Australia, Canada, the USA, the UK, Japan).
2. Countries with a significant share of funding for social spending at the regional and local levels (Denmark, Norway, Sweden, Finland).
3. Countries with significant independence of budgets of different levels that actively interact with each other (Austria, Germany, Switzerland).
4. Countries with a high level of dependence on the central budget (Belgium, France, Greece, Italy, the Netherlands, Portugal, Spain).

The process of formation and use of local budgets also has its own specifics in different countries (Chorna, 2013), for example: 1) in Germany, local budgets for next year are planned at the rate of 2-3% more than last year; the main expenses are education, social work with various vulnerable groups of the population; 2) in the UK, the main source of replenishment of local budgets is the municipal tax (its size is calculated depending on the value of property and the number of adult family members); main areas of expenditure: housing, education, judiciary, police, ecology; 3) in France, the share of taxes in the local budget – 40%, subsidies – 30%, own revenues and loans – 30%; moreover, most local budgets in this country are in deficit; the main expenditures are directed to the police, civil and fire protection, education, culture and infrastructure.

Following the general principles of local budgeting, each country chooses its own path of development, and so far there is no single recipe for creating a balanced and efficient structure of local budgets; each of the available is unique in its own way, adapted to the needs of the population of a particular country and territory.

3. Actualization of the local budgets’ role in Ukraine

Most scientists consider the budget system of Ukraine to be two-tier and centralized (the level of centralization until 2014 was approximately 65-70%) (Denyshchenko, 2018; Chorna, 2013). However, it should be noted that the structure of local budgets had three levels: regional; district; budgets of individual cities, towns and villages. During the 24 years of operation, the current budget system did not pay off, and the results of inefficient redistribution of funds prompted its reform.

Since April 2014, local self-government reform has been implemented in Ukraine, which has several areas, including: territorial-administrative, which aims to optimize the number and size of administrative territories (oblasts, districts, amalgamated territorial communities), and financial and capacity of local budgets). For six full years now, local budgets have been planned and implemented in accordance with

the Concept of Reforming Local Self-Government and Territorial Organization of Power in Ukraine (On approval..., 2014), which provides an opportunity to conduct first reviews and evaluate the effectiveness of the reform of local finances. their use.

A significant number of scientists pay attention to the optimization of local budget processes in Ukraine, including Lutsenko I. (Lutsenko, 2020), Bogatyreva E. (Bogatyreva, 2018), Maistrenko O. (Maistrenko, 2009), Baranovska N. (Baranovska, 2018), Duma V. (Duma, 2017) and others. Most scholars provide the results of their own research on certain specific issues of the local budgeting segment, which help to feel and understand its progress, problems and successes. Some authors pay more attention to the theoretical basis of local budgeting, others research foreign experience in order to determine the possibility of implementing best practices in Ukrainian self-government. But the financial activity of local self-government in Ukraine is constantly moving in time, new circumstances and conditions of functioning appear, the coverage of which gives an opportunity to consider and analyze the results of activities to fill local budgets in recent years.

4. Analysis of local budgets in Ukraine

The revenue part of the local budget, according to the law, consists of general and special funds, as well as the development budget, each of which has features of filling and use. The general fund contains funds intended for the implementation of general or priority functions of local governments, namely: salaries with accruals, payment of utilities and other services, purchase of necessary equipment, materials, items and more. That is, it is the part of the local budget that provides a financial opportunity for local governments to perform their direct functions in the interests of the community.

The structure of revenues of the general fund includes revenues from personal income tax (60% of the total amount), rent for special use of forest and water resources (50%), rent for subsoil use in the community (25%), state duty at the place of action (100%), excise tax on the sale of excisable goods and the community (100%), income tax of state (10%) and utilities, property tax (100%), single tax (100%), fees for parking spaces, tourist tax (100%), rent and license fees (100%), administrative fees, fines (100%), etc. (Budget Code..., 2010).

During the seven years since the beginning of the financial decentralization reform, according to the Ministry of Finance of Ukraine, there has been a steady increase in general fund revenues approved by local councils and from 2014 to 2020 these figures increased almost 3.4 times. The dynamics of growth of revenues to the general fund is presented in Figure 1.

The indicators of the general fund for recent years presented in Figure 1 show that the redistribution of funds from state to local budgets towards the latter has significantly increased the financial capacity of local governments, which is a motivating factor for further revenue growth and use in community needs. In addition, it should be noted that during this period, the revenues of the general fund each year exceeded the planned.

In terms of the most budget-generating taxes for 6 years of financial decentralization reform, the general picture of revenues to the general fund of local budgets is presented in Table 1.

According to the data in Table 1, the largest part, which forms more than half of the general fund of local budgets, is the personal income tax (18% of accrued income). During the research period, its size increased from 53.6 to 177.8 billion UAH, i.e., 3.3 times, and the share increased from 53.71% to 61.33%. The main

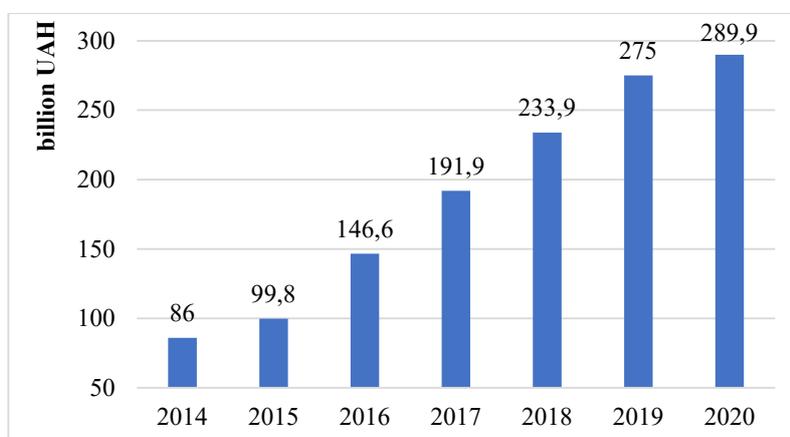


Figure 1. Revenues of general funds of local budgets of Ukraine 2014-2020, billion UAH

Source: based on data (Execution of local budget..., 2021)

Table 1

Structure of tax revenues to the general fund of local budgets during 2015-2020, billion UAH

Years	Total	Personal income tax	Land fee	Real estate tax	Excise tax	Flat tax	Other revenues
2015	99.8	53.6	14.5	0.53	7.7	6	17.47
		53.71%	14.53%	0.53%	7.72%	6.01%	17.51%
2016	146.6	79	23.3	1.4	11.6	10	21.3
		53.89%	15.89%	0.95%	7.91%	6.82%	14.53%
2017	191.9	110	26.4	2.4	11.3	15.4	26.4
		57.32%	13.76%	1.25%	5.089%	8.03%	13.76%
2018	233.9	138.1	27.3	3.1	18	29.8	17.6
		59.04%	11.67%	1.33%	7.70%	12.74%	7.52%
2019	275	165.4	32.8	4.9	21	35.2	15.7
		60.15%	11.93%	1.78%	7.64%	12.80%	5.71%
2020	289.9	177.8	31.5	5.8	22.4	37.9	14.5
		61.33%	10.87%	2.00%	7.73%	13.07%	5.00%

Source: based on data (*Execution of local budget..., 2021*)

factors that influenced the significant increase in the value of personal income tax are the growth of the minimum wage and the average wage, which, according to the Pension Fund of Ukraine, increased by the same indicator – 3.3 times (*Official site of the Pension Fund..., 2021*). Based on this, we can conclude that in Ukraine as a whole the number of jobs has not changed, and the increase in personal income tax was facilitated only by an increase in wages.

The second level of income and share of the tax that fills the general fund of local budgets is the land fee. This is a mandatory payment made by legal entities and individuals in the form of land tax or rent for the use of land of state and communal property (*Tax Code..., 2010*). The actual amounts received by local budgets during the research period increased from 14.5 to 31.5 billion UAH, and their share in local budgets, on the contrary, decreased from 15.89% to 10.87% (*Execution of local budget..., 2021*). Similar conclusions are made by I. Lutsenko, explaining the increase in payments by increasing the inventory and land provided for use, and the decrease in the share of land tax in the structure of local budget revenues is explained by regulatory problems regarding the tax base (Lutsenko, 2020). Bogatyreva E. explains the reduction of the share of land fee by the unsatisfactory condition of the lands provided for use, the introduction of inefficient tax benefits for the local budget, as well as the unsatisfactory level of tax payment by land users (Bogatyreva, 2018).

Excise tax is a tax on the consumption of excisable goods (products), which is included in the price of such goods. The list of such goods is provided in Article 215 of the TCU (*Tax Code..., 2010*). Revenues from excise tax are also a significant component of the revenue side of the general fund of local budgets, namely, in their structure from 2015 to 2020 occupies an almost constant share – from 5.89% to 7.91%, and the amount of revenues from it for this period increased

2.9 times (*Execution of local budget..., 2021*). Taking into account the growth of the general level of prices for consumer goods, we can assume that the filling of local budgets from it is a constant value.

The flat tax is the next important component that significantly fills local budgets. It is a business tax paid by businesses when they choose a simplified taxation system and those who run their business in the community. The number of payers of such a tax reflects both the number of entrepreneurs in a given area and the amount of their contribution to local budgets. That is, the level of revenues from the flat tax can be concluded about the favorable business climate in the community or region. This tax also helps to fill the community development budget, and this increases its budget-generating role. In the period from 2015 to 2020, the amount of payment of the flat tax in Ukraine increased from 6 to 37.9 billion UAH (6.1 times), and its share in the total fund of local budgets increased almost 2.2 times (*Execution of local budget..., 2021*). Both indicators show an overall increase in entrepreneurial activity operating on a simplified taxation system (mainly small business) and an increase in the share and role of small business in Ukraine and its impact on enriching local budgets and the well-being and quality of life in communities. According to analytical data (*How did the number of..., 2020*) in the period from 2015 to 2020, the number of “simplified entrepreneurs” decreased from 2268 to 1886 thousand people or by 20%. At the same time, the number of small business legal entities conducting business on the simplified taxation system increased by 5.5% (from 1,278 to 1,351 thousand people). Thus, we can recognize a threatening fact – a general decrease in the level of small business in Ukraine.

Revenues from real estate tax occupy a small share in local budget revenues, namely from 0.53% to 2% (*Execution of local budget..., 2021*). This indicates

a small amount of state-owned real estate, which remained at the disposal of communities after years of privatization. In addition, a significant proportion of real estate is unsuitable for rent. It is also worth listening to the opinion of Maistrenko O. (Maistrenko, 2009), who explains the small level of such revenues by the lack of a single real estate register and clear standards that should provide criteria for assessing the condition and determining the rental price of buildings. In such conditions, the use of available premises is almost impossible.

Other revenues to the general fund of local budgets are a set of a number of local taxes and fees in monetary terms for the specified period vary from 17.47 to 14.5 billion UAH (Execution of local budget..., 2021), and their share in the structure of the general fund has a steady downward trend. This indicates a general decrease in the total share of the remaining local taxes and fees listed in the article, including income from profits of state and municipal enterprises, administrative services, fines, tourist tax, rent, etc.

Thus, a review of the structure and dynamics of revenues to the general fund of local budgets, comments of scholars, analysis of current legislation allows us to conclude that Ukraine today is still in a state of reforming the public financial system, consisting of public and local finances. At this time, 6 full years have passed, during which local finances were planned, formed and used under the new rules. During this period, the share of local budgets in the general indicators of the state budget has significantly

increased. According to the official website of local government reform, it is possible to determine a steady increase in the share of own revenues in the total fund of local budgets, but the growth rate is declining from year to year (Figure 2).

Despite the constant increase in the amount of own tax revenues, their size is insufficient for local budgets to reach full financial capacity. This is a problem that Ukraine still has to solve during the current reform.

The largest part of tax revenues for the research period were: personal income tax, land fee, excise, flat and property taxes. The share of these taxes in the general fund was determined from 82.5 to 95% (Execution of local budget..., 2021), so the research of the amount of revenues from them and finding ways to further increase their own tax revenues is extremely important for any community in Ukraine.

Personal income tax revenues to the community budget are growing mainly due to the increase in the minimum and average wages over the 6 years of reform, rather than due to an increase in the number of enterprises and an increase in the number of jobs.

Land is a powerful source of community revenue from its use. A quality land fund is a guarantee of such profits that are still insufficiently understood by local leaders.

In search of sources to increase the revenue side of local budgets, it is impossible to ignore even small ones in terms of revenue. One of them is community real estate tax revenues.

A significant part of the revenues of the general fund should be revenues from the profits of state and municipal

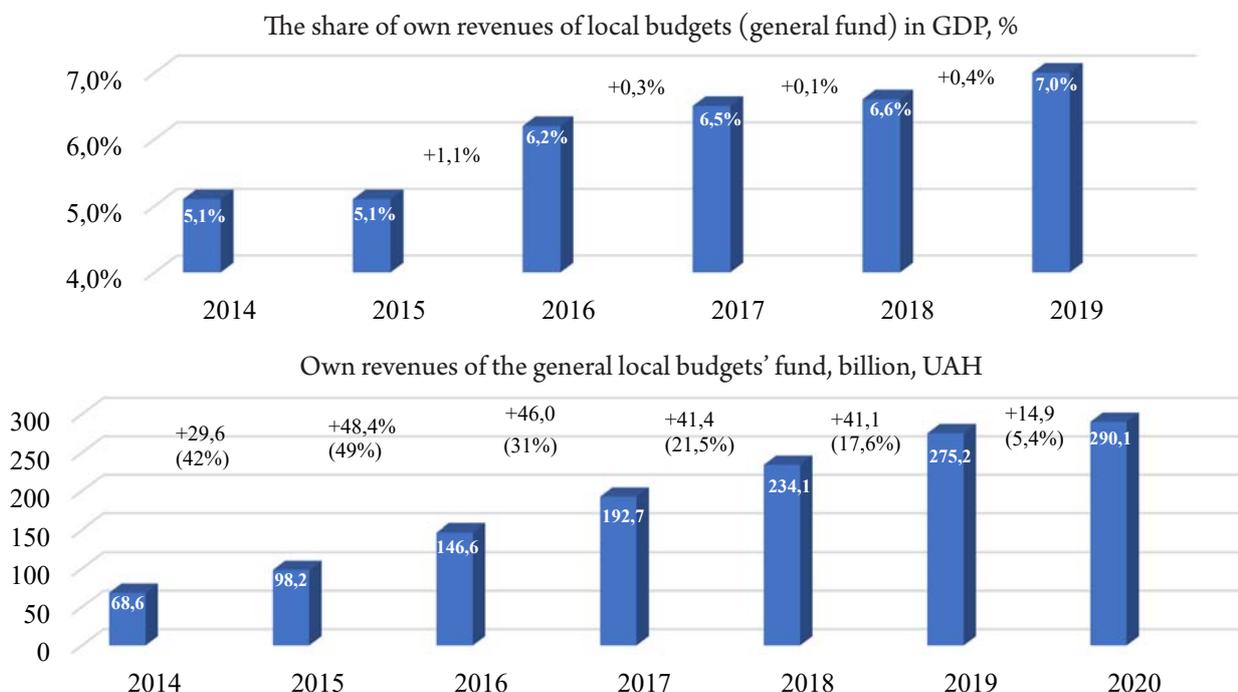


Figure 2. Dynamics of the own revenues' share in the general fund of local finances for the period from 2014 to 2020.

Source: (Official site of local government..., 2021)

enterprises of the community, funds from administrative services, fines, advertising and tourist fees, and so on. Their presence, size and share in the structure shows the community's own ability to use its resources, earn and create a development budget. Unfortunately, during this period, in Ukraine as a whole, there was a negative trend both in the amount of funds and in its share in the structure of the general fund (more than three times). This indicates a general crisis of entrepreneurial and administrative activity of local self-government, inefficiency of utilities, inability or unwillingness to earn independently for the benefit of the community.

It is also necessary to point out the objective circumstances that in some way affected the amount of tax revenues, namely the land fee and the flat tax in 2020. In March of that year, due to the quarantine that took place in Ukraine due to the COVID-19 pandemic, the Government of Ukraine decided to allow certain categories of taxpayers not to pay the above taxes for this month. Thus, local budgets underreceived at least 1/12 of tax revenues, which affected the overall reduced result (On Amendments to Certain Legislative Acts..., 2020).

According to the structure of expenditures, local budgets of Ukraine have a social orientation (Figure 3).

According to the data presented in Figure 3, the largest share of expenditures in 2020 was labor costs (and, compared to 2019, this figure increased by 15.5% (Official site of local government reform in Ukraine)), the second largest were capital expenditures, the third – subsidies and current transfers.

5. Ways to increase the revenue side of local budgets

Therefore, based on the conclusions made about the sources and efficiency of filling the general fund

of local budgets, we can determine the following recommendations to local governments to increase the amount of filling this fund:

1. The need to create additional conditions by the state and local governments to improve the business climate in communities. The same recommendations can be applied to the possibility of increasing revenues from the flat tax. Local businesses, especially small ones, are the foundation of a community's well-being and the key to its future prosperity.
2. Carrying out an inventory and arrangement of land funds of communities, bringing the land fund to a level sufficient for its profitable use, will certainly contribute to the receipt of permanent income from land lease and their growth.
3. Creating and organizing a register of real estate owned by the community, bringing it, if necessary, to a proper condition for use or lease, return to the community of abandoned premises, will provide opportunities to increase income from their own real estate communities.
4. Conducting an audit of the activities of communal enterprises of the community in order to find additional opportunities to improve the efficiency of their activities, modernize and improve the quality of their work to provide additional services.
5. Support and motivation of local business for further activities and development, involvement of business structures and the public in public dialogue will contribute to further strategic economic and social development.
6. Intensification of the administrative services' centers and search for opportunities will improve the provision of paid services of any complexity in the short term.
7. Promoting domestic tourism in the community will increase revenues from tourism tax, increase

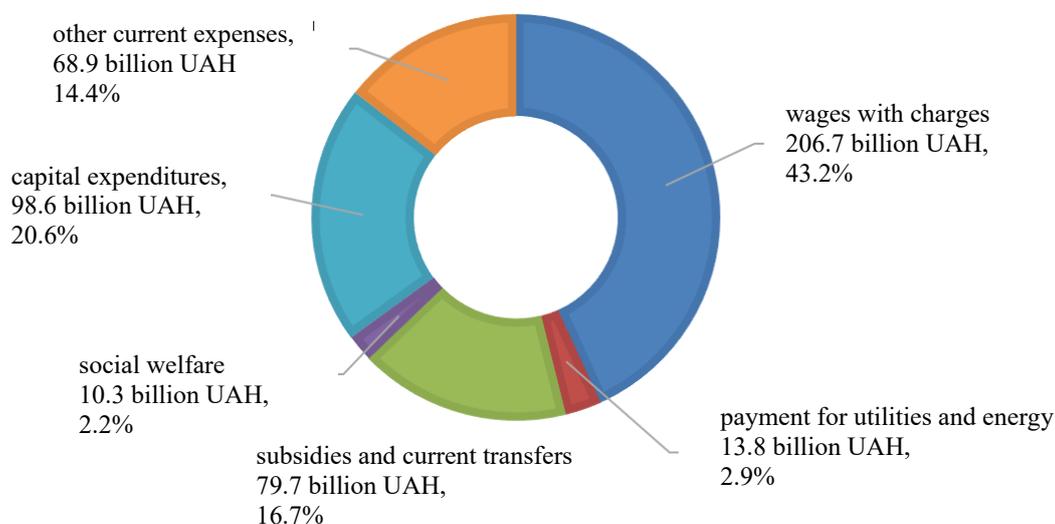


Figure 3. The structure of expenditures of local budgets of Ukraine in 2020

Source: (Official site of local government..., 2021)

the profitability of enterprises in other sectors of the community: transport, hotel and restaurant business, entertainment centers, trade, etc., as well as have educational and patriotic social effects, return youth and will help attract investment.

6. Conclusions

The state and peculiarities of filling the general budget in each community can differ significantly. Local governments have all the opportunities and information to analyze and identify both strengths and weaknesses of the budget, draw conclusions and determine their own priorities for further activities to find and attract reserves to increase the own profitability of local communities. The proposed recommendations are general and relevant for all regions of Ukraine without exception.

The analysis of trends in local budgeting processes in other countries and the current situation regarding decentralization reform allows us to conclude that Ukraine has chosen the right direction, which has a positive impact on the financial capacity of local communities. Ukraine's path towards transforming the role of local budgets, despite the similarity of the general features of local budget restructuring, should be unique. It is impossible to implement the experience of other countries without taking into account the specific properties of the national financial and economic system. Awareness and adherence to these two aspects will contribute to the successful completion of decentralization reform and the full implementation of the role of local budgets – ensuring sustainable financial capacity and meeting all the needs of the inhabitants of a particular area.

References:

- Denyshchenko, L. V. (2018). Local budgets: origin, concepts, structure, directions of development and their role in regional development. *Global economic problems*. Issue 22. Retrieved 20 June, 2021 from: <http://global-national.in.ua/archive/22-2018/146.pdf>
- Buryachenko, A. (2014). Functional decentralization and improvement of the system of budgetary relations. *Finance of Ukraine*, vol. 2, pp. 19–29.
- Chorna, N. (2013). Foreign experience in the formation of local budgets and the possibility of its application in Ukraine. *Scientific conferences*. Retrieved 20 June, 2021 from: <http://oldconf.neasmo.org.ua/node/734>
- On approval about the Concept of reforming local self-government and territorial organization of authorities in Ukraine. Cabinet of Ministers' Order. April 1, 2014 № 333-r. Retrieved 20 June, 2021 from: <https://zakon.rada.gov.ua/laws/show/333-2014-%D1%80#Text>
- Lutsenko, I. S. (2020). Monitoring the fiscal role of property taxation in Ukraine. *Effective Economy*, vol. 11. Retrieved 20 June, 2021 from: http://www.economy.nayka.com.ua/pdf/11_2020/75.pdf
- Bogatyreva, E. M. (2018). Payment for land as a source of filling local budgets in Ukraine. *Effective Economy*, vol. 6. Retrieved 20 June, 2021 from: http://www.economy.nayka.com.ua/pdf/6_2018.49.pdf
- Maistrenko, O. V. (2009). Real estate tax as an additional source of filling local budgets. *Right Ukraine*, vol. 10 (46). Retrieved 20 June, 2021 from: <http://dspace.nbuv.gov.ua/handle/123456789/28687>
- Baranovska, N. I. (2018). Foreign experience in the formation of tax revenues of local budgets. *Economics and customs relations*, vol. 8, pp. 32–39.
- Duma, V. L. (2017). International experience in forming the budget potential of local finance. *Economy and society*, vol. 13, pp. 1093–1099.
- Budget Code of Ukraine (2010). *Law of Ukraine*. № 2456-VI. July, 8. Retrieved 20 June, 2021 from: <https://zakon.rada.gov.ua/laws/show/2456-17#Text>
- Execution of local budget revenues (2021). *Official website of the Ministry of Finance in Ukraine, section Local budgets*. Retrieved 20 June, 2021 from: <https://www.mof.gov.ua/uk/vykonannia-dokhodiv-mistsevykh-biudzhetyv>
- Official site of the pension fund in Ukraine. Retrieved 20 June, 2021 from: https://www.pfu.gov.ua/2121350-pokaznyk-serednoyi-zarobitnoyi-platy-za-20__-rik/
- Tax Code of Ukraine (2010). *Law of Ukraine*. № 2755-VI of December 2. Retrieved 20 June, 2021 from: <https://zakon.rada.gov.ua/laws/show/2755-17#Text>
- How did the number of sole proprietors and legal entities in Ukraine change in 2013-2020? (2020). *Word and deed. Analytical portal*. Retrieved 20 June, 2021 from: <https://www.slovoidilo.ua/2021/01/27/infografika/biznes/yak-zminyvalasya-killist-fopiv-ta-yurydychnyx-osib-ukrayini-2013-2020-rokax>
- Official site of local government reform in Ukraine. Retrieved 20 June, 2021 from: <https://decentralization.gov.ua/finance/gallery>
- On Amendments to Certain Legislative Acts of Ukraine Aimed at Providing Additional Social and Economic Guarantees in Connection with the Spread of Coronavirus Disease (COVID-19). *Law of Ukraine*. № 540-IX. 2020. March, 3. Retrieved 20 June, 2021 from: <https://zakon.rada.gov.ua/laws/show/540-20#Text>