



KAPITEL 4 / CHAPTER 4⁴
INTERNATIONAL EXPERIENCE IN LOCAL GOVERNMENT FINANCING
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Introduction

The formation of local budget revenues and the identification of reserves for their increase are becoming especially relevant in the context of the market transformation of the Ukrainian economy. Despite ongoing changes and innovations in the Budget and Tax Codes concerning the decentralization of financial resources, the system for accumulating revenues in local budgets continues to be characterized by a low share of own revenues. As a result, the real financial capacity of local authorities is significantly limited. Meanwhile, in developed countries, local communities, relying on their own financial resources, serve as stabilizers of the socio-political and financial-economic situation in their respective administrative-territorial units. Therefore, the study of international experience in local government financing, particularly regarding the implementation of local government principles, becomes both theoretically and practically important.

The purpose of this study is to analyze the experience of local government reform in countries such as Poland, Kazakhstan, and Japan, and to consider the potential application of this experience in the reform of territorial governance in Ukraine.

Many domestic and foreign scholars have addressed the issues of local budgets and local government reform, including M. Pasichnyk, P. Vorona, V. Zhuravel, A. Tkachuk, N. Kaminska, L. Panasyuk, A. Skrypnyk, N. Stukalo, I. Tkachenko, M. Derkach, N. Chorna, and others.

4.1. Local government financing in Ukraine

In recent years, Ukraine has seen fundamental changes in its local government system, particularly regarding the formation of local budgets. A number of laws have

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been adopted to enhance the budgetary and financial autonomy of local budgets. These include the independent formation of local budgets based on stable revenue sources and expenditure powers, as defined by the main parameters set forth in the draft state budget (Article 75 of the Budget Code of Ukraine) [1]; expansion of the local revenue base; introduction of new types of transfers; decentralization of expenditure powers; and the establishment of a new system of budget equalization.

One important component of budgetary decentralization is the reform of state regional policy. In 2015, the Law of Ukraine "On the Principles of State Regional Policy" [3] was adopted, defining a system of strategic planning documents for regional development. The establishment of the State Regional Development Fund (SRDF) created opportunities to minimize corruption in the distribution of state budget funds to regional budgets, while introducing competitive selection for regional development projects. An online portal was created for direct registration of projects submitted for financing from the SRDF. As a result, Ukraine's state regional policy gained European characteristics and received competitive formula-based financing from the State Budget of Ukraine. Regions were given the ability to plan and finance their own development independently.

Local communities gained significant financial resources, with their budgets becoming comparable to those of cities of regional importance. State support for infrastructure development in such communities has also stimulated the creation of new opportunities in rural areas to provide citizens with comprehensive services from local government bodies, which they were previously deprived of [8, p. 32].

According to Article 64 of the Budget Code of Ukraine [1], the general fund revenues of city budgets of regional importance, district budgets, and budgets of local communities formed in accordance with the law and the prospective plan for community territory formation include: 60% of personal income tax (PIT); state duties, which are credited to local government budgets based on the place of action or document issuance; excise tax on retail trade of excisable goods; corporate income tax from communal enterprises; local taxes and fees; a unified tax; rent payments; fees for licenses for certain types of economic activities and certificates; fees for the placement



of temporarily free funds of the respective local budgets; proceeds from the sale of ownerless property; concession fees for objects of communal ownership; fees for providing administrative services; administrative fines and penalties; 80% of proceeds from the sale of scrap and waste of gold, platinum, platinum group metals, and precious stones; 25% of environmental tax; and other revenues to be credited to the respective local budgets [1].

For the effective use of SRDF funds, it is essential for both territorial communities and other local government bodies to understand where these funds should be directed. For communities, it is crucial that SRDF funds are used as efficiently as possible, creating new opportunities for increasing local budget revenues in the future [8, p. 33].

The lack of substantial experience in territorial community (TC) operations has led to improper distribution and functional use of funds. Therefore, it is necessary to consider the financial development practices of local governments in foreign countries.

4.2. Features of local government financing in Poland

The first stage of decentralizing local government development in Poland began back in 1990. The country's 49 voivodeships were consolidated into 16, and local communities were given budgets with the right to independently determine the allocation of funds. Communities received not only real powers and money to exercise them but also ownership rights to land and most state assets. Poland introduced a system where each territorial community can attract funds to its budget from both its own revenues and state transfer payments [5]. This is one of the most important principles of Poland's reform. Mandatory revenues for Polish municipalities (gminas) include: tax revenues (from real estate, agriculture, forestry, vehicles, business activities of individuals taxed with a fixed tax card, inheritance, and donations); fees; a municipal surcharge on personal income tax; a municipal surcharge on corporate income tax; revenues of municipal budget units and contributions from off-budget economic units; property revenues; general grants; educational grants; road grants;



targeted subsidies from the state budget for tasks related to government administration entrusted to gminas; and interest on municipal funds held in bank accounts.

Non-mandatory revenues for gminas include: compensatory grants for lost revenues from benefits and exemptions established by law, such as agricultural tax; targeted subsidies to co-finance municipal tasks; targeted subsidies for tasks carried out by the gmina based on agreements with government administration bodies or other self-government units; targeted subsidies from the state budget to eliminate direct threats to public safety and order; subsidies from targeted funds; inheritance and donation contributions for gminas; dog owner taxes; interest on loans granted by the gmina; extension fees and interest for delayed financial obligations; interest and dividends on invested capital; and revenues from fines and enforcement payments. Gminas independently finance expenditures for territory maintenance, roads, streets, bridges, parks, environmental protection, water supply, sewerage and waste disposal, electricity and gas supply, primary healthcare, preschools, elementary schools, urban public transportation, libraries, cultural centers, sports grounds, and more.

Thus, gminas became independent legal entities with the right to defend their interests in court (including against the government), and they actively exercise this right. The list of gmina competences is open-ended, while voivodeships do not have such rights. In fact, most tasks are performed at the gmina level. For example, 40% of personal income tax remains in the gmina, while 1% goes to the county (powiat) and 1.5% to the voivodeship. Active gminas, in addition to their own funds, attract grants. For example, education for children in primary schools (grades 1-6) and gymnasiums (grades 7-9) is provided by gminas. Education in grades 10-12 (college, technical school) is funded by the county, while higher education institutions are funded by the state.

According to experts in this field, it will be more challenging to implement decentralization reform in Ukraine. They emphasize that Poland was prepared for reforms after its revolution and already had specific individuals ready to take on leadership roles in ministries and other government bodies [2; 4; 8].

Experts also note that Ukraine lacks the comprehensive approach Poland once



had. Moreover, they argue that Poland's decentralization experience cannot be directly compared to Ukraine's. In Poland, decentralization was not an isolated reform. Alongside it, many structural changes were implemented: reforms in the education and healthcare systems, and redistribution of funds through budgets. In Ukraine, each reform is separate, lacking the comprehensive approach to decentralization. In Poland, it was a systematic approach based on changes in the territorial-administrative division. Subsequent reforms were layered onto this and worked together [5; 10].

4.3. Features of local government financing in Kazakhstan and Japan

Reforming local government is undoubtedly a complex process. It is quite risky, but the benefits outweigh the risks. A modern state is a strong institution with vast capabilities, as exemplified by Kazakhstan, with its exceptional successes in development over the past twenty years, driven primarily by the state. However, no state can address all areas comprehensively, and central government bodies have their limitations. Some significant local issues can be best resolved at the local level. This is why many countries have established various forms of local government. Kazakhstan has three administrative-territorial units: national, regional, and district, each with its own budget. There is much debate about adding a fourth level, which could create new challenges in intergovernmental transfers and managing public funds, potentially causing more harm than good. Kazakhstan has made long-term efforts to enhance the competencies of rural akims (mayors), helping them become leaders ready to manage municipal budgets and communal property. However, there is still much debate and criticism that local governments, despite their level of autonomy, may prove unnecessary, and remote villages and districts may struggle to efficiently use the delegated powers, continuing to require substantial support from national and regional administrations [4].

Thus, Poland and Kazakhstan have nearly the same number of local administrative-territorial units. Poland has 2,479 gminas, while Kazakhstan has 2,445



auls (villages), districts, and cities of district significance, which are the only state level without independent budgets. There is no reason why a reform similar to Poland's could not work in Kazakhstan. Therefore, Kazakhstan has introduced several legislative changes stipulating that local budgets will be funded by tax revenues, non-tax revenues, income from the sale of communal property, and transfers from district budgets. From 2020 onwards, a self-sufficient budget is planned for all administrative-territorial units.

The formation of local finances in Japan is also noteworthy. Local governance in Japan is two-tiered. Local authorities play a significant role in ensuring the country's sustainable development. The development of regional and state programs is based on the principle that the residents of a country are the owners of its natural resources. Thanks to a well-developed economic model, the central government maintains a close relationship with local governments, which positively affects their development and support for the population. The revenue side of local budgets consists of taxes and non-tax revenues such as bonds and loans. The expenditure side is primarily directed towards social insurance, servicing public debt, and grants to local governments [6].

The revenue side of the budget includes both tax and non-tax revenues. Among the tax revenues: 40% comes from personal income tax, 30% from corporate income tax, and 30% from indirect taxes. Compared to other countries, Japan has a relatively high share of non-tax revenues, including income from rent, sales, fines, lottery revenues, and loans. A distinctive feature of Japan's budget system is that all budgets are balanced without deficits. To redistribute financial resources and equalize the financial potential of prefectures, a special institution—the Financial Equalization Fund—was created. It is formed as part of the central government's budget. To determine which areas are entitled to receive funds from the Equalization Fund, standard territory budgets are calculated. The fund is formed through deductions of 32% from personal income tax, corporate income tax, and alcohol excise tax; 24% from VAT; 5% from tobacco excise tax; and 19% from other revenues [9].



Table 1 - Features of Local Budget Formation in Foreign Countries

Experience of Poland	Experience of Kazakhstan	Experience of Japan
<p>Polish communities received not only real powers and funds to implement them but also ownership of land and most state assets. Poland introduced a system where each territorial community can attract funds to its budget from both its own revenues and state transfer payments. This is one of the most important principles of the Polish reform.</p>	<p>Local budgets are funded by tax revenues, non-tax revenues, income from the sale of communal property, and transfers from district budgets. From 2020 onwards, independent budgets are planned for all administrative-territorial units. Ensuring local authorities' autonomy in managing local matters (budget, taxes, economic issues, etc.), while maintaining strict oversight from the Center regarding nationwide matters</p>	<p>A distinctive feature of Japan's budget system is that all budgets are balanced without deficits. To redistribute financial resources and equalize the financial potential of prefectures, the Financial Equalization Fund was created. Tax rates are differentiated, and local authorities have the ability to set local taxes freely.</p>

Conclusions

Based on the analysis, it can be stated that, in general, local budget revenues in the countries examined have a similar structure, consisting of both tax and non-tax revenues. Tax revenues, which include income from taxes, fees, and other mandatory payments, form the basis of budget income. Non-tax revenues play a much smaller role in the composition of local budget revenues. A distinctive feature of Japan's budget system is the relatively high share of non-tax revenues—15% in the national budget and 25% in local budgets. Japan is characterized by high centralization of tax revenues, two-thirds of which are state taxes, with the remaining taxes going to local budgets, providing 40% of their income [6].

When looking at the implementation of decentralization reform in Poland and the proposals being discussed in Ukraine, the commonality lies mainly in the goal and final management structure. However, there are significant differences: in Poland, the reform was preceded by several stages of reform and a desire to make irreversible



changes; Poland did not require the enlargement of territorial communities, and the size of counties proved to be non-essential—thus, the main issue was providing authority and resources, not the number or area. Only the voivodeship level required enlargement, which does not need significant changes in Ukraine.

Based on this, we can note that the general strategic direction for Ukraine should be to increase local authorities' interest in boosting their own budgetary potential when filling local budgets. The disadvantages of Poland's local government reform system are that Polish communities are too small, and larger communities are needed to tackle more complex issues. In Ukraine, people should be convinced that creating strong communities with populations of 15-20 thousand is necessary. Then, there will be enough funds to finance larger projects and programs.

Japan's experience could serve as an example to follow, particularly the reduction in the total number of taxes, which would improve their administration and expand the list of local taxes. Local taxes should include those that would provide substantial and permanent revenues, such as personal income tax. It is essential to recognize the link between the services provided at the local level and the funds required to deliver those services.

Necessary steps must be taken immediately for Ukraine to achieve greater autonomy in generating local revenues in the future. While local revenue sources remain unstable and insignificant, the role of state grants and subsidies should not be diminished, as only in this way can the state actively influence the development of local self-government.