

Tetiana Devemy
PhD, Professor,
International Relations Department,
International Business Institute,
France
korneevat@yahoo.com

Tetiana Zatonatska
Doctor of Sc., Associate Professor,
Department of Economic Cybernetics,
Taras Shevchenko National University of Kyiv,
Ukraine
tzatonat@ukr.net

DECENTRALISATION: KEY CHALLENGES FOR UKRAINE

Decentralisation is a top priority in the extensive reform programme that the Government of Ukraine has been undertaking since spring 2014. Important legislation was adopted during 2014 and 2015, providing an enabling environment for reforms. However, in order to succeed, decentralisation reforms will require an unprecedented re-enforcement in administrative capacities at the local community (hromada), district (rayon) and regional (oblast) levels. It equally needs a significant change in political and administrative culture among elected officials and public servants, so that they are able to adapt to their new roles and responsibilities. Citizens' trust and involvement in policy making at the various levels of governance needs to be strengthened.

The Ukrainian Constitution defines the country as a unitary state and guarantees principles of local self-governments to be applied in the country. Yet, Ukrainian local self-governmental bodies have not been able to realize their potential due to years of overcentralized policies and an extremely limited financial autonomy. Mainly the central government decided what type of policies and services sub-national tiers had to provide, often with insufficient knowledge of the actual needs of the population. Consequently, many local authorities currently fail to provide quality services (e.g. administration, health, education, water) to their citizens and need to rely on private sponsors for any major investments.

After the change of the Government of Ukraine in spring 2014, local self-government, administrative-territorial and regional policy reforms became top priorities. Since that time, extensive work has been completed to enact these reforms. A concept on "Reformation of Local Self-Government and Territorial Organisation of Powers" was approved in April 2014 which sets the framework for an ambitious reform. Additional important legislation has been adopted during 2014 and 2015, including laws on state regional policy, fiscal decentralisation (Amendments to Budget and Tax Code) as well

as on cooperation and amalgamation of local communities. This created an enabling environment for the implementation of reforms. As local budgets are increased due to revenues from locally generated taxes, the reform has created new incentives for local leaders to deliver quality administrative services and foster economic development¹. A new philosophy of horizontal fiscal equalization was introduced². The reform steps taken have already produced positive results: Local budgets increased by UAH 44.6 billion (37.7%) in the first half year of 2015 in comparison to 2014.

The current version of the Association Agenda to prepare and facilitate the implementation of the Association Agreement was endorsed by the EU-Ukraine Association Council on 16 March 2015. The Agenda refers to the “(...) *strengthening of the functioning of local and regional self-government, and legal status of the service in local self-government bodies, including through a decentralisation reform devolving substantial competences and related financial allocations to them, in line with the relevant standards contained in the European Charter on Local Self -Government.*”³ “Chapter 27 “Cross-border cooperation and Regional Cooperation” in the EU-Ukraine Association Agreement promotes “*mutual understanding and bilateral cooperation in the field of regional policy, on methods of formulation and implementation of regional policies, including multi-level governance and partnership, with special emphasis on the development of disadvantaged areas and territorial cooperation (...)*”. A recent Communication from the European Commission emphasizes the crucial role of Local Authorities for enhanced governance and more effective development outcomes⁴. The EU has provided substantial financial support to regional policy reforms in Ukraine. One major obstacle to a successful Decentralisation process in Ukraine is the fragmentation of sub-national governments. Too many territorial units are too small to perform delivery of basic service functions effectively⁵. To overcome this fragmented structure and increase efficiency, the Government of Ukraine launched an ambitious territorial reform. The reform aims to reduce the number of territorial entities at community level, from more than 12,000 to approximately 1,200-1,500 hromadas (local communities). At the intermediate level, there are plans to reduce the 490 rayons (districts) to around 100-120. The number and territories of oblasts (regions) will not be changed.

The reform sets incentives for amalgamations of local communities using a “carrot and stick approach”: Amalgamations are voluntary but only bigger cities and newly amalgamated communities with a sufficient size immediately benefit from the reform having access to increased budgets and more autonomy. Smaller, less competitive

¹ From 1 January 2015, cities of *oblast* importance, *rayons* and voluntarily amalgamated communities receive 60% of locally generated personal income tax, 100% of so-called “single tax” (a lump-sum tax for small businesses). The Regional level additionally obtains 15% of personal income tax and 10% of the enterprise profit tax.

² Local communities with fiscal capacity above Ukrainian average by at least 10% are allowed to keep half of the revenue surplus. Poorer local governments, with fiscal capacity below 90% of the national average, receive a base grant which amounts to 80% of what this budget requires to catch up with the average.

³ http://eeas.europa.eu/ukraine/docs/st06978_15_en.pdf

⁴ https://ec.europa.eu/europeaid/sites/devco/files/communication-local-authorities-in-partner-countries-com2013280-20130515_en_4.pdf

⁵ OECD Territorial Reviews: Ukraine 2013.

communities will receive fewer subsidies and benefit only in case of amalgamation with others. As of September 2015, 793 communities voluntarily decided to amalgamate and 159 new hromadas were formed.

In the area of regional development, the Government of Ukraine has displayed qualitatively and quantitatively new approaches. The State Strategy for Regional Development was adopted on 6 August 2014. With guidance and expert support from the EU funded Support to Ukraine's Regional Development Policy Project, the Ministry of Regional Development, Construction, Housing and Communal Services approximated to principles of EU Regional Policy and established a transparent funding mechanism for regional development: the State Fund for Regional Development. The fund is an innovation in the Ukrainian budgetary system: it provides stable and predictable funding, uses a fixed formula to calculate the distribution among regions¹⁰ and allows multi-annual development projects. In 2015, the Government of Ukraine allocated UAH 2.9 billion to the fund. To ease the application process and projects' independent evaluation, ensure transparency and visibility, the fund is administered through a web-based system.

In 2015, for the first time since its inception, the fund has been providing financing for all types of investment programmes and regional development projects. In earlier years, the fund focused solely on the construction or reconstruction of social infrastructure. Important changes have been made regarding the basic selection criteria for investment programmes and regional development projects: namely, compliance with the priorities identified in the State Strategy of Regional Development, regional development strategies and in regional action plans to implement them. To support amalgamations of local communities according to the newly adopted legislation, the fund also provides funding for investment programmes and regional development projects that are implemented as cooperation projects of local communities and projects for voluntarily amalgamated local communities. The quality of projects submitted to the fund remains a major bottleneck. The success of the mechanism for stimulating regional development through the State Fund for Regional Development is largely dependent on the ability of the authorities and non-state actors to properly apply new approaches in utilizing the fund's financing.