



ЕКОНОМІЧНА ПРАВДА

Expert discussion on Prospects of Decentralisation

On 09 August 2022, CASE Ukraine think tank held a discussion on the topic of ***Prospects of Decentralisation***. The event featured MP, Chair of Subcommittee for Administrative and Territorial Set-Up Vitaliy Bezgin, Director of the Institute of Territory Development Yuriy Hanushchak and was moderated by CASE Ukraine Executive Director **Dmytro Boyarchuk**.

Keynote points of the discussion and abridged expositions of speaker reports are published below.

Keynote Points:

- Decentralisation is the basis for sectoral changes that have to happen in the country. Ukraine dealt with administrative and territorial division matters: territorial communities have been formed across the country, the number of Raions have changed, and community resources and powers have increased.
- The full-scale invasion and internally displaced persons have changed the demographics. A new approach envisions further modelling of service provision in the areas of public health protection, education and administrative services.
- The four directions to work in: separation of powers between the state and the local self-government; universal operation of the public service; selective correction of the administrative division; solving the situation with IDPs (matters of normal valid statistics and election law).
- It is necessary to introduce a legislation on administrative and territorial division, set straight the inner structure of local self-governance and solve issues of local state administrations.
- The budget for 2022 envisages 64% PIT left at its source in all the communities. The PIT has to be paid at the place where the production facilities are located, not where the employee has been registered.
- The influence of the body of local self-government in the filling of the budget with local taxes is insubstantial in Ukraine as it is not formalised in a normal body of law.
- According to the general rule, money follow the powers so where there are no powers there can be no money. Businesses should not be burdened with taxpayers' money and fiscal encumbrances that are more necessary for public needs.
- The current legislation on the capital city is not compliant with the European Charter of Local Self-Government.
- There additionally exist problems of political (unpopular) and corruption (it is easier for someone to take cash rather than bother with collect real taxes for the budget) nature. It is necessary to amend the administration law to eliminate misuse.

- Ensuring an effective control, separation between the state and the local self-government
+ law on the capital city= balanced formula for EU integration.

Transcript of discussion (for the full video of discussion please follow [the link](#))

- At which stage is the decentralisation reform now?

Vitaliy Bezgin

This is a rather philosophical question. Let me explain: the decentralisation per se is the basis for those sectoral changes that should be happening in the country. Ukraine in the period of decentralisation went through matters of administrative and territorial division, that is, territorial communities were created everywhere, the number of Raions changed, and community resources and powers were strengthened. This should serve the basis for sectoral changes and improvements happening in every industry.

Simply giving powers and money is not enough. It is necessary to comprehend and model how services in the domains of public health protection, education, public services will be delivered further on. Speaking of these indicators before the full-scale invasion of February 24th, they were down to the basic level practically in every domain. It was a success somewhere, not so successful elsewhere; still, nowadays the modelling requires a certain rethinking. There are challenges that should not be ignored and that will affect the national regional strategy. This specifically includes the issue of a great number of internally displaced persons that have changed the demographics.

Saying now a certain region that has hosted hundreds of thousands of IDPs has sufficient social infrastructure and satisfactory services would be against the reality. Therefore, the decentralisation that successfully passed the administrative and territorial reform and, to some extent, sectoral changes (which certainly are in need of improvements – particularly, the social welfare and support domains where huge gaps exist) requires a selective reconsideration with due regard to the martial law situation.

When the recovery plan was been designed, there was a subgroup on local self-government working on the public administration package within the National Reform Council. Some four problems have been identified that are the key ones now. Some of them were key already before the new phase in the war, others were laid bare by it. Actually, they are **the four directions** along which we have to work.

The first, and probably the most sweeping one is about Ukraine needing to separate the powers of the state and those of the local self-government, finally, at the legislative level. In my view and in the view of many European partners, the Ukrainian decentralisation has been among the most successful in Europe. The most basic thing is the delimitation of powers at the level of law, which will lead to corrections in the fiscal domain and the Budget Code. Actually, Ukraine should have done this 10, 15, 20, even 30 years ago.

The second aspect that is now becoming prominent in Ukraine is about a normal public service that has to operate everywhere. That is, there is the legislation on civil service but the one on the service in bodies of local self-government, on its professionalisation is now increasingly topical. A relevant draft legislation has already been registered and we are going to move in this direction.

The third aspect is about the need to selectively correct the administrative division. It may not be possible to resolve the challenges that emerged without changing the configuration of communities and Raions – here is the issue of enclaves due to active hostilities in the northern part of the country. These things have to be sorted out because they are about the system of governance.

The fourth one is about IDPs: should they be really deemed the internally displaced ones. It is about the matters of real effective statistics, the election legislation that concerns local elections for these citizens to receive their right and become fully integrated into the social and political life in a new land that hosted them and gave them the roof over their heads.

These are the aspects that will turn challenges in the coming years; I hope we will be able to sort them out. An interim phase is about cementing the administrative and territorial division and the sectoral changes that had already happened but, sadly, had to be frozen because of the military conflict.

- What are the challenges the reform is facing and where, in your view, are the critical points?

Yuriy Hanushchak

It is worth mentioning that this reform has been on for quite a long time. The active phase kicked off in 2014 but the first Law on Local Self-Government had been adopted back in 1991, then the first budget reform arrived in 2001. The Budget Code effectively started the separation of powers in the local self-government. The separation is not about formalising something in law but rather to identify conceptual tenets of how to do it. In my view, this is also much more serious because a new generation of lawmakers will not revise previously made decisions. The decision is a difficult one because it will mean a conflict not just between the two branches of the public government – the central government proper and the local self-government – but rather inside the philosophy of governance as such.

We have to acknowledge there is a branch of power that is not institutionalised – the Office of the President that is making decisions without being constitutionally authorised to do so. This is also an issue within the decentralisation realm. We must make a rather important step, namely, by looping the self-government with feedback – a responsibility that can be either formal (incompliance with the law) or informal (civic society). Who has to do this? Under the Constitution, it is only the business of local state administrations – therefore, they have to be granted these powers, they have to be solely within the structure of the Executive rather than have double subordination because in this case they become weak and politicised. The question of the Law on Local State Administrations is not about the state but rather about the system of balances between the local self-government and the state.

As regards the administrative and territorial division, we have been able to make only puzzles so far. We need to adopt a law on territorial division to show philosophical positions of what makes a good administrative division and how this is changing. The work over such draft law is currently underway.

Another point: it is necessary to develop a clear view of the structure of the local self-government itself. E. g., such notion as ‘the executive committee’ is rather fogey. It is necessary to clearly separate, on the one hand, all things administrative, which is what the executive body is dealing with, and, on the other hand, the political ones where there is discretion, where decision of certain

nature can be made, where the law provides for framework approaches towards solving this or that matter. Such things can be decided solely by the Rada as a representative body.

We are witnessing a certain superimposition of powers today: the city mayor thinks he/she must dictate the policy; the Rada says it is its prerogative. Proposal mechanisms and tools need to be made separate. It is absolutely beyond normal when city mayor deputies are approved by the council, they should be mayoral nominees. Nor is it normal when legal regulations are approved by the city mayor. In this regard, the recent law (that was logically adopted) has become a litmus test of sorts to see if city mayors abuse the level of authoritarianism they have been currently granted. The coming signals show they are not doing it.

The decentralisation has really started to work from inside the society. Even city mayors have begun to understand they need to consult the Rada rather than unilaterally work and make decisions. Still, the boomerang will hit back, either from the government (if it materially breaches the law) or from the Rada (if a political decision is made).

There are, at least, four things that must be done: **first**, introduction of a legislation on administrative and territorial division; **second**, separation of powers; **third**, the inner structure of local self-government; **fourth**, local state administrations. After that the sectoral legislation will develop (it will not work without those things). The changes will fit into the environment created via the administrative and territorial division and the governance system.

- The reform plan has no dedicated section on decentralisation; however, there are many things linked to it, one of them being the proposal to change the personal income tax payment regime. There is a serious proposal to pay the PIT at place of registration. What is your position regarding this? Are there real prospects of switching to it?

Vitaliy Bezgin

It is only natural there is no separate section on decentralisation. EC Head Ursula von der Leyen said at the conference in Lugano Ukraine has two success stories of transformation, those of decentralisation and digitalisation. As both are cross-sectoral phenomena there is no current need to separate them.

Now it is necessary to capture things at the level of government authority – matters of local state administrations, prefectures. I hope a normal version of the bill will be motioned for the second reading and voted for to usher this grand transformation.

The matter of PIT within sectoral changes is of utter importance. There currently exists a great disproportion in rural areas. The issue is the PIT grows on a yearly basis. If we look at the 2022 budget, 64% PIT should be left locally for all the communities. There are many companies registered in Kyiv despite doing actual business, e. g, in a rural community in the Mykolaiv Oblast and their employee receiving services there. That is, the community takes an extra load on itself and its infrastructure without getting any benefits for companies placed on its territory. This is, to some extent, also a demotivating factor: why attracting investors in the area when all the taxes will go to Kyiv?

The proposal to collect payments at place of employee registration is another aspect. The debate between the current approach and the one based on production capacity location has been going on for a year. It is a rather philosophical question, quite similar to that of 'chicken and egg': what we will call a priority, the attracting of investors now or providing services to citizens in order to motivate residents of a given territory. Personally, I am not a supporter of the proposal on service delivery to citizens based on the place of their registration. I am of idea it should be based on production capacity location because now territories, particularly during their restoration, have to fight for money, for attracting manufacturing facilities to them and for filling their drying budgets with tax revenues.

If I am not mistaken, there have been 14 bills on the topic suggesting various models registered with the Tax Committee in the past years. Ultimately, it would be a challenge to predict which of these will be adopted by the majority. Still, speaking immediately about the lobby and the interest of the local self-government, the Association of Cities of Ukraine supports the option based on production facilities location. Frankly speaking, mayors of some biggest cities would be probably interested in keeping their currently existing status quo. I hope with consensus and compromises we will be able to design a right model. I am convinced the PIT has to be paid at place of production facility location.

- What is your opinion about PIT? It has been clearly declared we are going to integrate in the EU and we have been granted the candidate status. What other commitment does it impose on us in the context of decentralisation?

Yuriy Hanushchak

I am a supporter of 50/50 PIT distribution per place of employee registration and production facility location. If, from the standpoint of document processing, there is a position that Vitaliy supports, then, as a first step, this will make a right approach because people tend to live and work in their community. The administrative and territorial division reform was carried in such a way as for the economic activity centre to extend to cover the surrounding villages from where people commute to work. Because of that it will be a better option than the one that exists today. Anyway, the current existing system cannot stand as it is.

As regards the extent to which we need to integrate in this part, the Bible of the Council of Europe includes the European Charter of Local Self-Government. When they write laws, they, first of all, check their correctness against this Bible. For the majority of bills, we request opinion from the Council of Europe and its body, the Venice Commission where human rights are enshrined. Generally, they give position opinions on bills so we actually follow the course of those EU rules.

A huge problem has emerged now with non-voting the law on Kyiv where it says about the separation between a government agent, the state administration, and the local self-government and where there should be a mayor at the helm of the executive body of the Kyiv Council. Unfortunately, everything is mixed up now and there is a nail driven quite ago by the Council of Europe that says the capital city should be a mirror for compliance with EU rules.

After the issue is solved, plus the Law on Local State Administrations, it will be easier to resolve the inner things determining the specifics of Ukraine. For example, the core tax in the structure of finances in France is the real estate tax, and the notion of delegated powers is practically non-

existent. Here is the difference between us and them. Ensuring an effective control and separation of the State and the local self-government, plus the capital city – this is what needs to be done with EU integration in mind.

- The reform plan pays a lot of attention to the real estate and land tax, which are still a matter of future for us. Why we have not had successes in this yet?

Vitaliy Bezgin

The key issue is hidden in the administration of the tax. Generally, the matter of local tax administration is wider. Unfortunately, the little influence a local self-government body has on the filling of the budget with local taxes is explained by it being not formalised in a normal legislative way.

Another problem: we cannot find, also despite the help from the Local Self-Governance Association, a balanced model to implement it. This topic is not very popular with the public and not every government official at whichever level is ready to accept that much negative.

Another factor is the body of local self-government, being left without direct influence on local tax collection, is actually demotivated. The reality is the chair of a small community knows in detail where each tax is paid (or not paid) – particularly, when it comes to land. Local representatives better handle information than central government representatives who are focussed solely on VAT. This is the key cornerstone.

The remainder of issues contain political and corruption aspects. The political aspect is about it being unpopular; the corruption one is because sometimes it is easier for someone to accept cash rather than bother with really using these tax revenues to fill the budget. Not an easy discussion but at each meeting with local self-government bodies we speak about how necessary it is to enshrine respective administrative changes in law. In reality, we cannot find a balanced formula that would weed out misuse.

In the context of eurointegration processes, Verkhovna Rada's decisions envisage a eurointegration subcommittee set up with each committee to look, jointly with the general committee, into the compliance of everything with EU legislation because it will be problematic to progress towards fully-fledged EU membership without it.

Concerning our domain, Yuriy Ivanovich was absolutely right when he said the European Charter is the foundation for everything. We really obtain opinions on a regular basis but we will surely have remarks regarding local self-governance in the capital city, which is utterly limited and undoubtedly in breach of European principles. Beyond that, I think, the situation is currently balanced.

- Is it true there was a complete amalgamation of territorial communities? Would it not stand to logic to transfer 20% PIT to Raions like Oblasts have?

Vitaliy Bezgin

It depends on philosophy and politics the state produces in this or that domain. The amendments to the Budget Code were adopted just in time, on the eve of 2020 local elections. I am convinced those elected to Raion councils understood they would be a merely political body with the budget powers trimmed to its thinnest.

When someone says 'let us transfer 20% PIT to the subregional level', that is, to the Raion level, I immediately have a logical question: who we are going to take the money from: from the communities or from the national budget? And will anyone of them be ready to give it away? Therefore, I see no chance of transformation of PIT redistribution within the context of what we have now, what the government and Oblasts give. **For 64% communities it is possible.**

Taking into account the EU integration that we are talking about, the EC opinion published a week before Ukraine was granted its candidate status had a rather positive part on decentralisation. Among the key successes are: the administrative and territorial reform of the component and the issue of budget decentralisation where 64% of communities have been mentioned as the correct solution. So, one should not expect or observe any rollback here.

As for the percentage of amalgamated communities, the entire country is covered with communities; this was recorded by the government in June 2020 at the level of the zoning resolution adopted by the Verkhovna Rada. As of July 17 2020, it has been two years since the country became 100% covered by territorial communities.

Yuriy Hanushchak

Here is a play on words, that is, the process will end with the law on territorial division. Essentially, a concept of community as an administrative-territorial unit that is the territory of a territorial community will be introduced, after which the very concept of amalgamated community will cease to exist because one word – communities – is easier to say.

There is a general rule: the money follows the powers. Where there is zero power, there will be zero money. This is the taxpayers' money; because of this, it is not possible to burden businesses with fiscal encumbrances that are greater than what is necessary for public needs – this is one of the public finance rules. When it is about 64% - probably, it can even be 70% - to correctly calculate the cost of powers. This is the task Vitaliy mentioned at the beginning: to correctly calculate each power being deregulated or transferred to local self-government and to give the money in the form of local taxes and duties to match such powers. These are the social powers, the state is responsible for them, and they should be supported by national funds from PIT revenues.

This is how the system should work. Raions are out of luck now because we cannot really see now how powers can be taken from the Oblast or the basic levels when they cannot be executed at the basic level or are unfeasible at the Oblast one.

- What are the chances of legislatively solving the problems of managing the capital city in the coming years? Of particular interest is the question of how realistic is the reshaping of metropolitan districts.

Vitaliy Bezgin

The matter of limited self-governance in the capital city from which other issues emerge, that is, separation of powers per districts in the city of Kyiv, even municipal district limits that have been suggested to be changed – everything boils down to the one and only issue of finally adopting an adequate law about the capital city. The existing law, first of all, does not comply with the European Charter and secondly, it was written a long time ago and has long lost its relevance.

As soon as stories about the law on the capital city emerge, this gives rise to media activity, wars and constant politicisations of the process – everything but providing the capital with normal local self-government. It will be a challenge in the future because it would not be logical to launch in the middle of the war a political discussion instead of nation-building.

I am confident the only agent in the country with no interest in Kyiv having its local self-government back is the team of Kyiv City Mayor Vitaliy Klitschko with its destructive attitude towards the matter. If it is not ready to de-politicise the process then, to my greatest regret, the law on the capital is either doomed or will have to be adopted only after vicious political fight.

- Coming back to the process of EU integration: will it compel towards greater self-governance of the capital city or the overall EU integration movement will be completely unrelated to the matter?

Vitaliy Bezgin

I think this will affect eurointegration; it will press on it because the current legislation on the capital city is clearly at odds with the European Charter of Local Self-Government and European principles and approaches. Actually, the executive branch in Kyiv is not independent and self-governing. The Chair of the Kyiv City State Administration is nominated rather than elected as a mayor; it is a person appointed to, and dismissed from, the office.

The model suggested by Europeans is an adequate one: to separate matters pertinent to the executive committee as an independent executive body of Kyiv that is immediately chaired by the elected city mayor and assumes responsibility for the managing of the city and matters of government control that have to be referred to the function of local state administrations, that is, Oblast and Raion state administrations across the country. Unfortunately, we still see an unhealthy symbiosis going for decades, an ongoing game around who can be at the helm of the KCSA besides the mayor. I hope the activation of eurointegration processes will lead to a situation when a normal, European legislation in the area will have to be adopted.

Yuriy Hanushchak

I must add that, while there is no self-government or central power in Kyiv, there is a lot of money - 60 billion - there. Position overlapping - who manages funds and who controls him himself over the spending of the funds – this is not normal; this is against all the rules of public funds management. However, someone likes it because there is always some added value in the chaos that can be consumed. We do not have a fully-fledged local self-government in the capital, such as, for example, in Kharkiv or Dnipro. It is advisable to adopt the law on the capital city as soon as possible.

Indeed, it is necessary to provide Raion councils with maximum powers because in this case it will make an anti-corruption factor: the more we provide, the less it will be likely for them to steal. In order to tell whether they steal or not in ten districts, money movements in different district budgets are analysed. When there is a single budget of 65 billion, any misuse can be hidden there. This will be a huge nail in the sole that will be preventing us from going to Europe because we will be constantly pushed. They pretend to turn a blind eye as long as the war is going on, then they say 'Hold on. If you want to join the European Union, you have to show what do you want'.

- How Raion councils will further exercise their powers with due regard to amendments to the local self-government legislation?

Vitaliy Bezgin

The matter of Raion councils is actually not in the local self-government laws. It can be solved only through amendments to the Basic Law – the Constitution – by completely removing such an entity as Raion councils.

As regards Raion state administrations, these, like Oblast state administrations, after the Constitution is amended, will have to be transformed into prefectures that will coordinate operation of bodies of local self-government as well as supervise at the level of local self-government the compliance with laws and the Constitution in respect of delegated powers.

We have a huge problem: after the prosecution office was released of its general supervision function, no one no longer supervises local self-government while our civil society is still in the process of development. Therefore, changes are only possible through the law on local state administrations.

Yuriy Hanushchak

The political role of state administrations is zero because it is a government body that should not have a policy of its own. The policy of state administrations should be defined by law – more than that, separately for Raion and Oblast administrations. One of the objectives of the law is the separation of powers between Oblast and Raion state administrations: the Oblast level cannot be a mailbox for transfers to the Raion level. We ended up with far fewer Raions than there were so direct communication between the centre and the Raions is possible.

- Are relationships between councils and executive bodies possible when a council sets targets using business-like metrics, e. g., by quality-of-life indicators?

Yuriy Hanushchak

When a council sets goals as they do it in business, this is called a program-based budgeting where certain targets, respective qualitative and quantitative indicators to be achieved are outlined. However, there must be a relevant council decision – a local program where everything is described.

The legislation for this has already been designed and good councils use these things. Some do it purely formally but this is already a matter of development of the local self-government – and of the civil society that should monitor these processes.