

LOCAL BUDGETS UNDER MARTIAL LAW CONDITIONS

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The full-scale Russian invasion of Ukraine, which began in February 2022, has significantly impacted the economic situation in the country. Large-scale infrastructure destruction, constant shelling, occupation of certain territories, mass population migration, decline in production and business activity, as well as the government's anti-crisis measures to reduce the tax burden, have considerably weakened the financial capacity of local budgets, especially in communities located in active combat zones. In this regard, the analysis of the state of local budgets and the peculiarities of forming their revenues under war conditions becomes particularly relevant and is of vital importance for overcoming socio-economic challenges during martial law.

As of 2023, there are 1,952 local budgets in Ukraine, including 25 regional budgets, 13 budgets of cities of regional significance, 35 budgets of districts in cities of regional significance, 136 district budgets, 6 budgets of towns of district significance, 1,469 budgets of territorial communities, 39 budgets of urban-type settlements, and 229 budgets of village councils (villages) [2].

Local budget revenues play a key role in maintaining financial stability and the development of territorial communities. They are formed from multiple sources and directed towards financing various spheres of vital activity such as infrastructure, education, healthcare, culture, and social protection. Under martial law, the role of local revenues increases, as they become an important tool for strengthening the country's defense capacity by providing resources for implementing defense measures at the community level.

During 2019–2023, significant fluctuations were observed in the revenues of Ukraine's local budgets, caused by economic and political factors as well as martial law conditions. Thus, in 2019, local budget revenues amounted to UAH 560,528 million. In 2020, under the influence of various factors, including the COVID-19 pandemic, their volume decreased by 15.9% to UAH 471,480 million. As a result of economic recovery after the pandemic and reforms aimed at increasing local budget revenues, 2021 was characterized by an increase in local budget revenues to UAH 580,699 million, or by 23.2% compared to the previous year. Russia's war against Ukraine, which began in 2022, led to a worsening economic situation, a decline in investments, and a decrease in entrepreneurial activity, resulting in local budget revenues falling to UAH 555,097 million, or by 4.4%. Gradual economic recovery and government efforts to support local budgets during martial law caused a significant increase in their revenues in 2023 by 17.6% to UAH 652,608 million. Similar trends during this period were characteristic of the expenditure side of local budgets in Ukraine as well [2].

In 2022, a decrease in local budget revenues was typical across revenue sources (tax, non-tax, income from capital operations, funds of targeted budgets, etc.), except for funds from the EU, foreign governments, and international organizations, whose volume increased sixfold compared to 2021 to UAH 223 million. The greatest decrease in budget revenues, as expected, occurred in regions of active hostilities: Kherson (-33.3%), Luhansk (-21.9%), Donetsk (-19.9%), Zaporizhzhia (-15.1%), and Kharkiv (-11.6%) oblasts [4]. This was mainly due to population decline caused by migration to safer regions within Ukraine and abroad, reduced business activity of large and small enterprises, and a fall in citizens' purchasing power.

Regarding own-source revenues, since the beginning of hostilities, 85% of communities have received less than their budgeted funds, and every fourth community located in invasion zones collected at least 50% less revenue than pre-war plans. Significant shortfalls are observed in land tax payments (UAH 5.7 billion compared to 2021). In March, potential losses were at 38%, with budgets missing UAH 1.1 billion for that month. Growth was only observed at the end of 2022, by 1.4% [5].

Due to tax privileges, including setting the excise tax on fuel imports at 0 euros per 1,000 liters,

the excise tax experienced the largest relative decline, with its volume in 2022 falling by UAH 6.8 billion, or by 70.2%, compared to 2021 [6, 7].

The dynamics of local taxes and fees collection illustrate a similar trend. Thus, due to tax privileges caused by the war's outbreak, during 2022 a decrease in their volume by 6.2% was observed (from UAH 89.9 billion in January to UAH 84.3 billion in December), although with the reform introduction, local budgets collected 122% more of these taxes than before the consolidation. This indicator varies by region: where the population has increased due to internally displaced persons (IDPs) and business relocation, there has been a significant increase in these taxes (on average by 18.0%), while in other regions there has been only a decline [1].

Despite the overall decline in tax activity, the personal income tax shows growth, accounting for 68.4% of revenues for the period January–December 2022. December recorded a record level of revenues since the budget reform began — UAH 33.3 billion for the month, which is UAH 8.5 billion (34.4%) more than the same month in 2021. This growth is mainly explained by increased monetary support for servicemen (UAH 11.1 billion), whose numbers significantly increased, as well as an increase in the share of PIT credited to local budgets — from 60% to 64% since early 2022.

A similar dynamic is observed regarding single tax revenues. In 2022, its volume increased by UAH 0.9 billion, or 2.0%, compared to 2021. Month-to-month fluctuations during May–December 2022 were significant: from growth of 50.3% to a decline of 25.7%, with further growth up to 40.0% [8]. This instability is explained by changes in tax legislation allowing business entities with large incomes to switch from paying profit tax (18%) to a simplified taxation system with a single tax rate of 2% (instead of 5%) [6, 7]. By region, revenue unevenness is observed: Lviv oblast recorded growth of 20.3%, while Odessa, Sumy, Kharkiv, Mykolaiv, Chernihiv, Zaporizhzhia, Donetsk, Kherson, and Luhansk oblasts saw significant declines [5]. The main reason is active hostilities in these regions, which led to partial suspension or complete cessation of local enterprise activities.

As for interbudgetary transfers, according to the Ministry of Finance of Ukraine, in 2023 their structure was supplemented with funding directions related to overcoming the consequences of massive armed attacks and eliminating damage to local infrastructure, with the following breakdown: 49% constituted the educational subvention; 16% — the basic subsidy, which is higher than in pre-war years; 15% — other transfers; 9% — additional subsidies to local self-government bodies negatively affected by Russia; 9% — subvention for road repair and maintenance; 2% — other additional transfers [3].

With the start of the full-scale war, the expenditure burden on local budgets has increased, consisting of:

- costs related to integration of IDPs (education, social services, housing);
- the need to restore destroyed infrastructure: roads, schools, hospitals, water and heat supply facilities;
- increased funding of humanitarian needs: support for IDPs, evacuation activities, support of medical institutions, schools, etc.;
- additional expenditures on defense and security (territorial defense, shelters, assistance to the military).

An equally important problem in the functioning of local budgets is the uncertainty and instability of budget planning, which consists in frequent changes in legislation in response to the challenges of wartime; problematic forecasting of revenues and expenditures, especially in border and de-occupied territories; insufficient support from the state budget in some cases or delays in financing subsidies.

Despite the positive dynamics of local budget revenues in 2023, the need to implement measures and create alternative financing mechanisms to ensure the financial stability of territorial communities remains relevant. In this context, several directions of action can be distinguished:

- It is necessary to strengthen measures aimed at employing internally displaced persons (IDPs) and creating new jobs for them, which implies the implementation of programs to assist in job search, stimulate entrepreneurship among IDPs, and relocate enterprises to safer regions. Special attention should be paid to providing opportunities for professional training and retraining for IDPs to increase

their competitiveness in the labor market;

- Local communities should be encouraged to make decisions regarding the placement of temporarily free budget funds in government debt securities and/or deposit accounts. Such financial steps will contribute to creating a financial reserve for the future and will partially reduce risks through diversification;

- Reforming the management of municipal enterprises is important to bring them out of the crisis state. This can be achieved by optimizing expenses, more efficient use of resources, and introducing modern management practices. It is also necessary to implement transparent systems for monitoring the financial activities of municipal enterprises, attract professional managers, and create a competitive environment in the provision of communal services, which will contribute to improving their quality and efficiency;

- The efficiency of land resource management should be significantly increased, which implies reviewing the terms of existing lease agreements, conducting a full inventory of lands, systematizing records, and updating rent amounts. Such measures will significantly increase tax revenues. At the same time, it is important to ensure transparency in land distribution procedures, which will contribute to rational land use and minimize abuses in this area. The development of modern information and analytical systems will make it possible to effectively control the use of land resources and increase local budget revenues from land fees;

- Since internal and external investments can become a significant source of local budget revenues, communities need to assess their economic potential and present it to investors through appropriate platforms, programs, projects, and initiatives;

- In the process of planning local budget revenues, it is important to clearly define priority expenditure directions for the next year, and draft local budgets should be realistic and correspond to the current economic situation, avoiding inflated expectations. Budget planning itself should be carried out on a medium-term basis taking into account the national strategy for Ukraine's reconstruction.

Therefore, continuing the course towards decentralization of local self-government and stimulating local communities to maximize budget revenues is extremely important. Implementing the above-mentioned measures will strengthen the financial stability of local budgets during wartime, increase the efficiency of resource management, and activate economic development at the community level.

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