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# **Reforming Local Government in Ukraine**

A WHITE PAPER ON THE OUTCOME OF PUBLIC CONSULTATIONS

*kyiv 2008*

This White Paper was prepared under the “Public Consultations and Public Awareness Campaign on Local Government Reform in Ukraine—Phase 2” project undertaken jointly by the International Centre for Policy Studies (ICPS) and the Center for Ukrainian Reform Education (CURE) with funding from the Westminster Foundation for Democracy.

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# Introduction

This White Paper is the final product of a project called “Public consultations on reforming local government in Ukraine and public awareness campaign—Phase 2” being carried out by the Center for Ukrainian Reform Education (CURE) and the International Centre for Policy Studies (ICPS). This report outlines key problems in local government today, describes reform measures proposed to resolve them, and summarizes the positions of various interest groups regarding current problems and the suggested pathways to a solution.

In the first phase of this project, ICPS and CURE held public hearings in seven oblasts of Ukraine over November–December 2007, where a Green Paper on Local Government Reform was the basis for discussion. This analytical document discussed the current problems with the system of local government and how to handle them.

This report is based largely on the original Green Paper prepared during the first phase of this project. Other analytical materials prepared by ICPS were also used in preparing this report: a Green Paper on public administration reform in Ukraine, which was drafted in 2006 by the National Council on Public Administration and Local Government and the Center for Legal Reform with the support of ICPS under the “Public consultations on public administration reform” project, and the final report from the “Public consultations and awareness campaign on political reform in Ukraine,” which was also carried out by CURE and ICPS during 2007.

The overall structure of this report is similar to that of the original Green Paper, which underwent public discussion. Each chapter has been considerably expanded now, based on our analysis of the positions of various stakeholder groups and materials that they presented during the consultations.

The key difference between this Paper and the Green Paper is that it summarizes the reactions of stakeholders to the original contents. The current report makes it clear how changes to local administration need to be undertaken in order to succeed and indicates which of the proposed changes are a priority for regional stakeholders. Based on the information gathered at the hearings, many propositions from the Green Paper have been expanded and detailed.

This report can also be useful for international donor organizations that support the activities of community organizations in the regions. It provides an explanation for which problems in local polity are seen as core by regional representatives themselves and which ways of resolving them these individuals propose.

In addition to a discussion of the Green Paper, a report by Györgyi Nyikos, the Hungarian expert in local government, was presented during the second round of public consultations. With the help of this report, the participating Ukrainian stakeholders were able to look at issues of local government from a cross-national perspective. This report is presented here as a separate attachment.

The participants in this project express their thanks to the Westminster Foundation for Democracy for its financial support of the implementation of this project.

# 1. Key problems in local governing

The consultations we held generally confirmed the reality of the problems in the work of local governments that had been raised in the Green Paper. Still, stakeholders who participated in the discussions rated the importance of these problems quite differently. All regional representatives, without exception, paid the most attention during these discussions, not to the problem of inaccessible or low-quality public services provided at the local level, but to the enormous gap between what local governments did and what really mattered to local voters—and to the lack of accountability before the community. This last cluster of problems was where the most adjustments and additions came from stakeholders at the public hearings.

## 1.1. Inaccessible, poor quality public services

Local governments are supposed to provide basic social and administrative services: pre-school, primary, secondary and tech-voc education; preventive medicine and primary and secondary healthcare; keeping the public peace; the organization of residential service delivery, public transit, and so on. Today, only cities are capable of carrying out all these functions. Most rural communities and even many towns lack the financial and human resources to provide the entire range of public services of the necessary quality and quantity.

*Rural communities  
can't provide needed  
public services*

The result is that most people are deprived of the right to good quality public services and the human development gap among regions is considerable.

*This issue was raised least of all by stakeholders at the public hearings. Most likely this is because the consultations took place in oblast centers, where this problem is not as serious. Representatives of rural, county and small town governments were noticeably absent at these hearings.*

## 1.2. Government actions and voter concerns: Mind the gap

***Voter concerns  
do not drive local  
governments***

Being neither accountable to nor overseen by their constituencies, local governments, and especially local state administrations, yet dependent on the central government, local administrations are driven less by the concerns and needs of the local community than by their own interests or those of the central government. The Budget process itself and the top-down nature of budget planning and execution objectively make it impossible to take the interests of voters into account in the activities of local governments.

To this day, there are no workable mechanisms for voters to make clear their concerns and to ensure that these are taken into account in the work of the local government. Proportional elections to city, county and oblast councils have increased the “disconnect” between deputies and their constituents—and the interests of those constituents. As representatives of various parties in local councils, deputies are often less engaged in promoting the concerns of the residents of their communities than in the ideological struggle for power.

Priorities in funding local needs depend less on the will of local voters than on politicians and officials in Kyiv. As a consequence, there is little objective need for local representatives of local governments to be open about their work before the representatives of local communi-

ties or to consider voter interests in carrying out their activities.

Essentially, local governments and local executive bodies are unsupervised and unaccountable in the exercise of their powers. Neither the state nor communities have any working mechanisms for overseeing the work of local governments. This is especially obvious when it comes to handling land issues and planning the construction and development of infrastructure in cities, towns and villages.

***Voters have no means to oversee local governments***

*According to stakeholders at the consultations, this is one of the key issues at the local level. They considered the actions of both local governments and state bodies equally unaccountable and inappropriate in relation to the activity of local communities. As a rule, the biggest complaints in this direction were about the ineffective management of land, water, forest and mineral resources. At the basic level, and especially if the community was on the outskirts of a major city, local governments frequently abuse the right to transfer arable plots of land at no cost to private ownership. Governments also ineffectively manage mineral, forest and water resources that are under their control. These are often a means for public officials to take rents, which is neither in the state's interests nor in the local community's.*

*Participating stakeholders also noted the lack of workable mechanisms—or of any mechanisms at all—to ensure that local governments did not operate outside the control of the local community or appropriate bodies.*

### 1.3. Local economies—slow or no-go; regional development—uneven

State and local budget policy makes local development impossible today. Most communities do not even have development budgets, and all resources are directed at covering day-to-day needs.

The unitary model of government in Ukraine today expects public services to be delivered at the same level across all the country's territories. Yet, economic development varies greatly from region to region. As a result, there is a strong need for highly centralized public financing. To ensure the necessary level of public services to a given population, cashflow first has to be concentrated in the State Budget of Ukraine and then, based on a distribution formula, handed out to the regions through equalization transfers. In this kind of situation, local governments are effectively deprived of any means to strategically plan local development.

*Mechanisms for  
distributing resources  
are unbalanced*

The problem is that the existing distribution mechanisms do not actually provide the necessary leveling in public service delivery. Today, only a few regions—more accurately, a few major cities—more-or-less provide the full range of public services guaranteed by law. Most of the rest of the regions have trouble even providing those services needed to just survive.

In addition, the current mechanisms for forming and executing local budgets, where local revenues constitute an extremely tiny share, provide little incentive for local governments to develop their local economies. Low levels of local revenues mean that local governments cannot provide funding to support even the development of local infrastructure. Migration to faster-growing regions in search of a better standard of living causes business activity and jobs to decline, which leads to even less growth in the tax base and, in the final analysis, to an even lower share of local revenues in the local budget.

*Stakeholders were generally in agreement that this is a problem, providing specific examples in support of this.*

#### 1.4. State and local governments: Uncoordinated and even conflicting

A slew of conflicts between the state government and local governments are written into legislation. Up to 80% of the powers of local governments are duplicated by the powers of local state administrations. On one hand, local state administrations are formed at the top; on the other, they have been delegated by law to function as the executive bodies of the relevant councils.

Indeed, the political status of local state administrators makes it very difficult to be objective in their work and is yet another source of conflict with local councils, especially those formed on a proportional basis.

*Participating stakeholders generally agreed that this is an ongoing problem. In their opinion, this situation increases the level of corruption and dependence of the judiciary branch, which cannot be an independent arbitrator in cases involving local state bodies and local governments.*

***The powers of local government and state administrations overlap***

## 2. The roots of these problems

### 2.1. The lowest level of government cannot carry out the necessary functions

*The administrative structure does not ensure resources for communities to develop*

The administrative-territorial system inherited from the USSR in most cases ensures neither a proper resource base for territorial communities to govern themselves, especially rural ones, nor does it take into account impact of the population of these communities and their demographic profile on the type and quantity of public services that need to be provided to local residents.

Ukraine's current administrative system is typified by a high level of centralization of functions and concentration of resources at the county and oblast levels. The relative size of local budgets in the Consolidated State Budget is 40%, while that of oblast budgets in total local budgets is 38%; the relative size of oblast-level municipal budgets is 47%, while that of county budgets is 15%. The relative size of the budgets of villages, towns and county-level towns in the consolidated county budget is 15-20%. This means that three times more funds are deliberately allocated to the budgets of oblast-level towns than to county budgets, although more than 60% of the population of Ukraine lives in villages, towns and small cities.

In addition, there is an enormous gap in the economic and demographic profiles of communities and counties, with populations ranging from as little as 15,000 inhabitants—some counties of Chernihiv Oblast—up to 130,000—Derhachivskiy County in Kharkiv Oblast. This results in objective reasons for the unequal provision of public services to the local population.

*The type and population of communities and counties varies excessively*

The current situation actually hampers the development of proper local government in villages, towns and county-level cities.

In many medium-sized and large cities, local governments are quite capable of providing their residents with the whole range of necessary services without involving local governments at the oblast level or local state administrations. But due to the way legislation has been drawn up, they do not actually have the authority to do so. Indeed, the residents of large cities have to apply for certain services to oblast administrations and, even worse, to state bodies that are neither accountable to nor supervised by the community.

Still, the majority of communities cannot provide the full range of public services, not due to legal restrictions, but for lack of resources—financial, human and so on.

The actual extent of community government remains unclear to this day. Flaws in the legislation dealing with this limit the jurisdiction of community government bodies to the limits of their populated areas, leaving the status of lands adjacent to each community to be decided at the county level by state administrations.

*Local government is not universal*

*Typically, participating stakeholders agreed only partly with the supposed roots of local government problems. Most of them agreed with such points as the centralized allocation of financial resources, the violation of the jurisdiction of local government, and ineffective legislative restrictions.*

*On the other hand, participating stakeholders did not generally consider major differences in the sizes of counties or overly small populations in territorial units as something that seriously hinders the work of local governments or reduces the likelihood that the local population will receive quality public services.*

*Firstly, stakeholders tended to appeal to the historical, cultural, religious and ethnic aspects of various regions as determining the difference in the populations of oblasts, counties and territorial units. Secondly, most stakeholders were convinced that in the majority of cases the lowest level of local government would be quite capable of performing its functions if all the other problems in the system of local government system were solved: ensuring financial independence, more effective property and land management, and so on.*

*On the other hand, the idea was sometimes voiced at these consultations that, should territorial reform be undertaken in Ukraine, it would be necessary to harmonize the domestic system with European standards. This would make it possible to use EU structural funds effectively in the future. Participating stakeholders also raised clear examples of how unable many local governments were to function, at the lowest level. For example, some 15% of village councils lack their own premises in Dnipropetrovsk oblast, while 25% of those who do have no heating.*

## **2.2. The division of power at all levels is unclear and irrational**

According to the Constitution, there are two centers of power at oblast and county levels: an appointed state administration and an elected council. This immediately establishes a kind of competition between the two bodies and is frequently the cause of conflicts in the process of making decisions regarding territorial development.

Fully 80% of the powers vested in local governments by the Law “On local government in Ukraine” are also vested in local state administrations by the Law “On the local state administrations.” That is, there is no clear division of powers between local governments and local state administrations. The practice of village, town and city councils delegating powers to their oblast and county councils, which means to council executive bodies in the form of local state administrations, should clearly be the exception rather than the rule. Because this practice is widespread, it offers opportunities for the abuse of public funds and the evasion of accountability on the part of local state administrations. It also makes local governments dependent on state institutions at all levels.

*Similar powers are vested in both local governments and state administrations*

Local government legislation also fails to clearly divide powers, duties and responsibilities among different levels of local government—communities, counties and oblasts. Some aspects in this area are regulated by the Budget Code. However, the Code only designates spending powers and establishes the right to determine the volume of transfers from the State Budget to oblasts, counties and oblast-level cities. As a result, the regulation of relations between oblast and county levels or oblast-level cities depends very much on the actions of specific officials and varies from region to region. This is particularly true of the division of power between oblasts and oblast capitals.

*Different levels of local government also overlap as to powers*

This issue is particularly important for specific municipal administrative territorial units (ATUs) that “contain” other ATUs, that is, on whose territories other ATUs operate without forming a single community with the city. Indeed, they operate as independent local governments. This is true of 64 oblast-level cities, on whose territories 202 other ATUs function—villages, towns and so on. This muddled power structure leads to chaos in the distribution of resources to exercise powers, which offers fertile ground for permanent conflict.

*Sometimes several administrative units operate within a single territory*

*Participating stakeholders agreed that the confused division of powers is a major cause of problems in Ukraine's system of local government. Some were also of the opinion that the consequences of this problem are much more serious. The domination of state authorities in local affairs tends to discredit the institution of local government: local deputies are often helpless to resolve problems in their communities and the result is that voter confidence in them is low. The average person sees few benefits from this kind of local government.*

## 2.3. Local governments are fiscally hobbled

### 2.3.1. *Insufficient sources of revenue for local governments*

The need to centralize public funding in order to provide public services of equal quality results in an insufficient financial base among local governments and their consequent dependence on State Budget transfers.

In general, local government revenues constitute a very small part of local budgets—less than 10% of total income. In addition, some local taxes and fees are difficult to administrate, so local offices of the State Tax Administration are actually not interested in collecting these taxes and fees. This reduces the enforcement of tax payments.

***Local revenues constitute less than 10% of local budgets***

***There is no property tax***

Ukraine still has no property tax, which is a major source of revenue for local budgets in many countries and can guarantee their fiscal viability. In addition, the current procedure for distributing revenues from state taxes and fees that are in excess of the fiscal norms set by the State Budget Law does not encourage the local governments even in cities with solid fiscal capacity to do something to increase such revenues. Current legislation provides no incentives for local governments to promote local business development that might, in turn, generate new jobs. Possibly the only exception is small and micro en-

terprises that operate under a simplified taxation system.

### *2.3.2. Public funds do not cover the state's fiscal obligations*

The scope of local governments powers is defined by law. Money to fund the exercise of the powers delegated to local governments are allocated by the Verkhovna Rada every year during the planning and adoption of the State Budget for the following year. However, in deciding the ultimate volume of transfers to local budgets, VR deputies do not take into account either the financial state of local governments or the range of powers delegated to them. Consequently, the transfers are not always enough to fully finance the delegated powers.

Spending on the exercise of delegated powers amounts to 90% or more of local budget expenditures. A major part of this spending, in turn, is to cover the payrolls of public institutions. However, funds allocated as transfers from the State Budget are sometimes insufficient to even pay these salaries in full.

Cities that have substantial revenues of their own can pay for their own capital and current spending, although they could use these funds to develop local infrastructure, such as improvements and social and economic development, instead.

The central government establishes breaks and holidays related to local taxes and fees without paying the necessary compensation to local governments. In addition, new laws often add new public duties to local government plates without matching financial support.

### *2.3.3. Lack public service standards and costing methodology*

To a large extent, this underfunding of real needs at the local level is caused by problems with costing these needs. The basis of any cost evaluation should be the state social standards and norms that came into force

***The volume of transfers is inadequate to fund delegated powers***

***Local government services have not been costed***

with the Law “On state social standards and social guarantees.” Still, despite numerous calls for enforcement on the part of the Verkhovna Rada, many social standards and norms still have not been developed by the Cabinet of Ministers, although the Law itself came into force more than five years ago. The old social standards and norms are fragmented into small elements whose sum does not cover the whole range of public services and whose indicators are often outdated. These factors make the old standards and norms unacceptable for calculation, which makes it impossible to come up with a correct assessment of expenditures for real service needs.

#### *2.3.4. The mechanism for distributing subsidies to local governments is ineffective*

*State subsidies at the county level are handled by local administrations*

According to the Budget Code and the Law “On the regulation of budget transfers between county budgets and the budgets of county seats, villages, towns and their associations,” equalization transfers from the State Budget are planned only to the county budget level. Further distribution among county, village, town and county seat budgets is actually handled by local state administrations and approved by county councils.

This often leads to abuse on the part of county officials in terms of how fairly equalization transfers are distributed among the communities in the county. In effect, this is the traditional soviet “nested doll” budget system and it keeps local governments from becoming bodies that can make independent decision in support of local development.

*Only cities designated as state or oblast level are fiscally independent*

Only state- or oblast-level cities, which have direct ties to the State Budget and the Ministry of Finance, have the real rights associated with fiscal independence. The rest of the country’s basic self-governing ATUs—villages, towns and cities—do not have the necessary financial resources to provide the full range of public services, from public, state, housing and utilities, to social and cultural services.

By encouraging a “handout” mentality towards the State Budget, the equalization transfer mechanism established by Ukraine’s Budget Code provides little incentive for communities, especially smaller cities, towns and villages, to generate their own revenues. On the other hand, taking those revenues that exceed “fiscal capacity norms” for expenditures away from the municipal budgets of large and medium-sized cities offsets any efforts on the part of “donor” communities to promote business, employment and increased personal incomes. Ukraine’s donor communities are mostly those cities with a population of over 500,000, cities with ports, railway hubs, major export-oriented enterprises, or atomic energy stations, that is, those cities whose strong economic base was established under the Soviet Union.

***Local communities have little incentive to establish their own revenue base***

*The question of fiscal independence for local governments was one of the most burning issues raised at these consultations. Participating stakeholders largely agreed that local governments needed to have their own revenue bases. However, they proposed quite a range of different approaches to expanding these sources.*

*Some stakeholders expressed doubts that property and land taxes could become a major, stable revenue source for local budgets in the first years after they were introduced. Still, there needs to be some movement in the direction of collecting such taxes. Other issues also need to be dealt with: expanding the jurisdiction of local governments to the areas adjacent to communities, finding qualified potential owners for farmland, and so on. Otherwise, property and land taxes are unlikely to become a significant source of local budget revenues.*

***A property tax should be instituted along with other measures***

*Some participating stakeholders suggested controversial proposals, such as increasing local government revenues by better managing community resources for profit, if state management of resources such as minerals (granite, sand, mineral water), forests and water is ineffective.*

*The issue of standardizing public services caused considerable controversy as well. While recognizing the urgency of the problem, participating stakeholders expressed many reservations as to what mechanisms and methods should be used in calculating these standards.*

## 2.4. Use of money, property and resources is inefficient and inappropriate

***There is no system for evaluating the impact of expenditures***

A system for determining the effectiveness and productivity of public spending has not been worked out, whether at the State Budget level or at the local budget level. A combination of the fact that it is impossible currently to finance all the commitments taken on by the central and local governments and the fact that communities have no leverage over local state administrations results in a free-wheeling approach to forming local budgets. Other than secured items, such as payroll for public employees, the financing of specific expenditures depends largely on what officials in local state administrations feel like doing.

The existing procedure for preparing budget request based on the previous year's spending figures does not reflect the impact of these expenditures on the volume and quality of services provided to the local population. This leads to ineffective planning and inefficient use of public funds.

***There's no effective internal or external budget oversight***

The absence of "management by objectives" planning and scheduled audits that make it possible to monitor the effective use of funds, and the effective absence of external controls including public fiscal oversight of the use of local budget monies are further reasons for the ineffective use of already limited financial resources.

The existing network of public entities does not reflect the needs of Ukrainian society today. On one hand, some bodies and institutions that receive the public and provide with specific services do not even have proper premises. On the other, other budget institutions rent out their

premises to commercial entities or hang on to premises they have no use for, thus placing extra strain on local or State Budgets.

Currently, there are also no working mechanisms for communities to join forces on a contractual basis in order to undertake and finance specific functions together. This prevents any optimization of the network of public institutions and organizations. For example, when the law fails to provide a simple mechanism for funding a single institution, say, a school or clinic, out of several local budgets, the network of these institutions cannot be improved by increasing the efficiency of the local government's use of available resources. There are other legal barriers to optimizing public institutions, as well. According to Part 3 of Art. 49 of the Constitution of Ukraine, for instance, the current network of healthcare facilities can not be reduced.

Laws regulating the status of community property and the exercise of delegated powers need improving. The distribution of municipal and state lands has not been completed. Consequently, the material resources available to local governments are being used extremely ineffectively. This is particularly true of land belonging to underdeveloped communities that border on major economic and industrial centers, as well as municipal land and property in urban areas.

*The main problem, according to most participating stakeholders, is the inefficient use of resources due to corruption in government and state authorities. As a result, local governments often fritter away their most valuable resource—land. Similarly, state bodies are very ineffective at managing forest, water and mineral resources, squandering them without any benefit to the state or local communities.*

*Ultimately, the most likely solution to the problem of inefficient budget management, in the view of community organizations that attended the hearings, would be to introduce external public oversight over its use. They made it clear they had little faith in the*

***The network of public institutions is inefficient***

***Local governments make poor use of available resources***

*possibility of proper internal mechanisms for controlling budget spending and increasing its effectiveness, such as budget management by objectives, scheduled audits, and so on.*

## 2.5. Voters have no input into legislation to support local development

***Local governments have no impact on decisions made in Kyiv***

Effective procedures and mechanisms for coordinating between central and local governments are lacking when it comes to policy decisions that affect the interests of local governments. According to the Constitution, local governments, unlike the executive and legislative branch, are not empowered to legislate. Moreover, local government representatives may not appeal to the Constitutional Court of Ukraine, even on matters within their competence.

At the state level, there is no institution that might represent the interests of local governments and have veto powers over the drafting and adoption of bills that violate its rights and eliminate state guarantees. The Secretariat of the President, the Secretariat of the Cabinet of Ministers, the Ministry of Economy, the Ministry of Justice, the Ministry of Finance, and so on, all have departments at the level of administrative sections—at MinFin it is an actual department—, that handle local government issues.

Because of this, local government interests are poorly represented and not heard when legislation regulating local government activities is being drafted.

*Participating stakeholders considered this problem in the broader context of a lack of proper contact between voters and their elected representatives and the resulting tendency to ignore the regions and the opinions of regional leaders in the legislative process. Indeed, the main political forces in the Rada show little interest in taking local government problems seriously.*

*According to participating stakeholders, the central government is not interested in large-scale reform of local government or in the re-distribution of powers and resources in favor of the regions and communities. This means that mechanisms must be established that would allow local reform activists to lobby such changes in Kyiv.*

## 2.6. There are not enough professionals at the local level

One major factor underlying current problems in local government in Ukraine is also the lack of professionals, especially in local governments. According to the Main Administration of the Civil Service, only 61.5% of the country's 92,000 local government officials have completed a Master's degree, which is considered a proper post-secondary education in Ukraine. In 2005, only 11.6% of municipal officials undertook professional development courses, while nearly 240,000 local council deputies for all intents and purposes received no targeted courses in local government. This means that local officials sometimes not only do not know how to resolve specific problems, but are often not entirely aware of the scope of rights and powers that the state and the law assign to different levels of local government.

***Local governments lack professional staff***

This problem has become even more pressing since the 2006 elections, when nearly 80% of elected deputies at all council levels were newcomers. Of 172 elected oblast-level municipal mayors, only 75 were incumbents. This means that in about 59% of Ukraine's cities, where more than 50% of the population live, mayors were elected for the first time. Needless to say, these positions were occupied by people for whom municipal government was a completely new sphere.

***Mayors and deputies need professional development***

Another unresolved problem is depoliticizing the civil service at the local level. When bureaucratic positions are politicized, enormous turnover of staff results at the local level after any election. The newly-elected head of

a city, town or village often fires many qualified workers in the executive, who were forced to campaign on behalf of the predecessor, and then hires new, less qualified workers.

***The system for training municipal public servants needs to be modernized***

In addition, there is an urgent need to overhaul the system for training state and especially municipal officials because it does not satisfy needs of the country or the regions. The current system is oriented mostly towards academic teaching and its curriculum is not aimed at the professional development of individuals who are in mid-career. It is also quite limited in terms of “throughput.” According to the Main Administration of the Civil Service, at the current rate, it will take the current system 240 years to train highly qualified public servants and local government officials, as there are some 92,000 officials working in local government in Ukraine today.

***There is no system for training local deputies***

As to training for local council deputies, there is no such system at the state level. In this situation, it makes sense that the primary training should be organized by political parties when they begin to form their election lists.

*The topic of the lack of professionals among deputies and local government officials led to the most heated debate at these consultations. Stakeholders were quick to point out the lack of professionalism among deputies on local councils, which are elected on a proportional basis.*

***Deputies show little interest in becoming more professional***

*Deputies not only lack knowledge of the local government system but they are also reluctant to bridge any gaps in their knowledge. They do not deem this necessary because many of them run for local council only to lobby their own business interests. Even with training, teaching materials and opportunities to attend related courses, deputies often ignore any resources. For example, according to a survey of deputies at different levels published by one of the NGOs at the hearings in Dnipropetrovsk, of 127 deputies polled in the oblast, only two knew what was in the Law “On local government.”*

*Needless to say, local councils cannot even effectively exercise the powers they have, let alone lobby for further local government reform.*

*Clearly, the main “gatekeepers” in the selection of more professional deputies to local councils should be the political parties that form election lists. Still, without public pressure and changes to the electoral system, the process of improving the quality of elected representatives will be far too slow and ineffective.*

*Another aspect discussed by participating stakeholders was fact that state bodies are unprepared to support or fund local initiatives to provide training for local officials or deputies. For instance, participants from Dnipropetrovsk Oblast commented on certain restrictions on public funding for training local deputies: to run a course, attendees have to be included in the civil service reserve list. Still, there are some positive examples of state officials supporting such training programs, such as in Zhytomyr Oblast.*

**The state does not support a system for training local officials and deputies**

## 2.7. The system for local elections is flawed

Often local governments do not represent voter interests based on their composition. With county and oblast councils elected on a proportional basis, many communities are not represented at all while oblast or county centers are over-represented, sometimes controlling as much as 80% of an oblast council.

**Territorial communities are not proportionally represented on local councils**

Proportional elections to municipal and oblast councils has led to a situation where these bodies often represent party interests, but not the interests of their electorates. This leads to hyper-politicization on these councils.

*The majority of participating stakeholders agreed that this was a problem. They considered the flawed election system the main factor that had reduced the professionalism of elected officials and led to unconstructive confrontations on local councils. However,*

**Unprofessional councils are the result of a poor electoral system**

*the discussion of how to resolve this problem provided no consensus at the local level as to the direction the local council election system should evolve in.*

## 2.8. Locals have no means to participate in and monitor their governments

Voter involvement in the making of key decisions depends largely on subjective factors and is not regulated by law. There is no legislation on local referenda that reflects modern conditions.

***There is currently no real link between local governments and their constituencies***

At the root of the low quality of administrative services is the fact most such services are the responsibility of executive bodies whose officials do not feel accountable to or overseen by the local community and who are not subject to the oversight of local governments. The centralization of power, the lack of proper feedback between local governments and their constituencies, insufficient state attention to the needs and interests of local governments have all led to a situation where local governments exercise their powers in a legal vacuum and without any oversight.

***Mechanisms to hold deputies accountable or remove them are ineffective***

*According to participating stakeholders, the components of this problem include the inefficiency of mechanisms like removing a deputy, voting non-confidence in a local state administration head by the relevant council, assigning deputies to specific territories, activity reporting by deputies, and holding public consultations.*

***Local officials actually impede public access to necessary information***

*Another component of the problem is the fact that local governments and local state administrations actually hinder public access to necessary information, such as regulations, resolutions, statutes and so on. The failure to reform the judiciary branch is another part of this problem, as it prevents ordinary people from effectively challenging specific actions by local governments or local state administrations. The problem of rule of law in Ukraine keeps Ukrainians from effectively controlling their governments.*

*Stakeholders pointed out that local councils were not always in a position to control executive committees. Current norms restrict such opportunities, that is, elected representatives cannot be members of an executive committee and committee members are nominated by the mayor and rubber-stamped by the council.*

*Some stakeholders saw this lack of control over politicians by voters as the result of the passivity of voters themselves, who do not understand nature of local government and are not interested in playing an active role in local affairs.*

## 2.9. Mechanisms to ensure consistent nationwide policy are ineffective

Local state administrations are supposed to ensure consistent state policy across the country. Because of the different ways they are formed and overlapping powers, city, county and oblast councils are often in conflict with both the heads of local state administrations and the central government. On one hand, the quasi-political status of the head of a local state administration encourages confrontation with the local council if the latter has a majority made of parties in opposition to the central government or the President. On the other, the grounds for calling a vote of non-confidence in the head of a local state administration are not specified anywhere, which leads to free-wheeling decisions by local councils or to excessive “flexibility” on the part of local state administrators.

Then again, the central government does not have any leverage over local councils even if they are in violation of the Constitution and the laws of Ukraine. The mechanism for calling pre-term elections to local councils by Verkhovna Rada that is currently on the books is not very effective—something that is confirmed by the fact that this provision has not once been applied in nine years. The only mechanism for settling such conflicts remains

***The central government does not ensure consistent policy across the country***

***The central government has no influence over local councils***

the court system. But even in this case, the personal liability of individual local deputies for illegal decisions made by their councils is unclear.

*Participating stakeholders did not pay much attention to this problem, possibly because it concerns the central government more than local ones.*

### 3. Suggested steps for reform

The stakeholders participating in these public hearings offered the most comments, reservations and proposals on the priority of changes and on specific proposals presented in the Green Paper on local government reform.”

In general, regional stakeholders shifted the main emphasis from large-scale changes like administrative-territorial reform, budget reform and so on, to specific smaller-scale changes that make a small but specific contribution to ameliorating the situation.

According to participating stakeholders, it is possible for local government to evolve on the basis of the existing Constitution by adopting appropriate legislation. They said that the potential for local government development afforded by the Constitution and current laws, despite their many flaws, was not being fully exploited by local governments for a number of objective and subjective reasons. Their proposals were mostly limited to concrete recommendations as to what requirements should be changed to eliminate these factors.

The idea of administrative-territorial reform did not find support at these public hearings. Reaction to the idea of changing the territorial system and setting up administrative-territorial units (ATUs) with a “scientifically viable minimal population” was especially negative. Participating stakeholders opposed this proposition on the basis of historical, religious and ethnic regional charac-

teristics, which they felt should be taken into account when planning such reform.

Most of the other proposals in the Green Paper were generally approved. Some of them were concretized, added to and clarified.

### 3.1. Options for local government and ATU systems

**Option 1.** Leave current administrative-territorial system and division of powers among levels of government (status quo)

*Option 1: Leave things as they are—including problems*

This option keeps the current public administration system at the local level and the existing division of powers, responsibilities and resources.

Pros	Cons
The service infrastructure will remain familiar to the public. Local officials will carry out their customary duties at their posts.	All the noted disadvantages of the existing system will remain, which will hinder serious improvement in public service quality.

**Option 2.** Re-distribution of powers and responsibilities without enlarging or consolidating communities.

This option presupposes that:

- those functions that the lowest level of government—primarily this concerns rural areas—cannot undertake to a level that can ensure effective performance will be transferred;
- communities that have the capacity will be ceded more public responsibilities, powers and financial opportunities.

Thus, for example, in villages where the councils cannot effectively run the school system, this function will be transferred to the county level. County education de-

partments, which are accountable to the county administration head—or county council once executive committees are established—will run the entire school system in that county.

Under this option, services will not be remote from consumers because they will be provided through the existing network of budget institutions, such as through the existing school system. However, administrative functions such as financial, HR, property, and school bus administration, will be centralized at the county level. The powers of large village councils will include only those that such councils can actually carry out, such as land management, garbage treatment and landscaping.

***Option 2: Concentrate administration at the county level***

<b>Pros</b>	<b>Cons</b>
<p>County-level administration will offer economies of scale for social networks (schools, medical facilities). A certain quality of public services will be guaranteeable. Cities, especially big ones, will be able to independently provide a greater range of public services on their own judgment.</p>	<p>Public services in rural counties will be predominantly administered centrally. The location of specific services will tend to be remote from the residences and businesses of those needing the services. Opposition from village councils because of loss of influence and resources to the county level. Disputes will continue between existing county seats and county-level cities. Duplication of powers: similar public services will be provided in cities by government bodies and in rural areas apparently by local state authorities. This will also need more complicated Budget procedures and more complicated laws.</p>

**Option 3. Enlargement through voluntary mergers of communities and a redistribution of functions on a contractual basis**

***Option 3: Communities merge voluntarily***

This option avoids some of the disadvantages of the previous option and takes care of an important political issue that can arise in implementing Option 2: the transfer of functions to the county level can potentially provoke conflict between the existing county seat and county-level cities that have a well-developed local government and strong financial base. Such cities consider themselves self-sufficient, prefer to be independent of county seats, and have a direct link to the State Budget.

Pros	Cons
<p>Strengthening the government of certain village councils would enable them to provide more public services at a level closer to their residents—that part provided on the county level today or not provided at all—and to improve overall service quality.</p> <p>The conditions can be established to strengthen participation of community members in solving local issues through public discussion of voluntarily joining forces on a contractual basis.</p>	<p>The passivity of current rural communities, lack of qualified workers in small communities that need to be enlarged could result in an overly slow process of mergers on a contractual basis. Poor legislation regulating voluntary contractual relations among public bodies could lead to conflicts that even the courts will not be able to settle effectively.</p>

The drawbacks of this option can be largely reduced by introducing proper fiscal incentives for voluntary mergers, such as through the allocation of state funds for infrastructure development.

**Option 4. Enlarging communities through centralized mergers, including compulsory ones**

The main threat facing this option is opposition from both voters and local governments in rural areas in instances of compulsory reform.

*Option 4: Forced consolidation will raise hackles*

The advantage of this option over the previous one is the establishment of conditions for equal service standards throughout the country, across all communities and territories.

Because the lowest level becomes self-sufficient, it should be able to provide a full range of better quality public services.

Pros	Cons
<p>The basis is set for making community governments better capable of providing more public services closer to their residents (that part provided on the county level or not provided at all) and improving overall service quality.</p> <p>The material and financial bases of local governments are reinforced.</p> <p>The ability of local governments to provide public services becomes consistent across the country.</p>	<p>Rural communities and governments will oppose forced mergers.</p> <p>Conflicts could arise in some centralized communities.</p>

This fourth option can also be implemented in tandem with Option 3 as the final stage of local government reform.

Along with community enlargement, the issue of county enlargement can be tackled.

**Stakeholders are wary of administrative reform**

*The most heated debates with representatives of local community were around administrative-territorial reform as one of main elements of local government reform. The regions remember the failed efforts headed by Vice Premier for Territorial Reform Roman Bezsmertniy in 2005 and are quite cautious about new ideas along those lines.*

**Such reform needs to reflect regional differences**

*Stakeholders appeared convinced that in changing the borders of administrative-territorial units it was important to be guided not by “scientifically viable minimal population” numbers for each level of ATU—the basic principle espoused by the NU–NS and BYT coalition—but by specific regional socio-political and economic characteristics.*

*A good example is Chernivtsi Oblast, which has many tiny communities. Those from Bukovyna believe that it is unlikely that neighboring villages differing as to language, religion and ethnicity will want to merge into a single community, because such mergers could make the situation worse and lead to open conflicts.*

**Stakeholders were against county- or oblast-level mergers**

*Participating stakeholders supported only the idea of greater consolidation of the weakest communities at the lowest level—villages—into larger ATUs. Other proposed enlargements, at the county or oblast level, received very negative reactions. The main argument against was the increased distance between the public and their service providers.*

*It becomes obvious that administrative-territorial reform needs to offer positive incentives. Currently, stakeholders think that undeveloped road and transport infrastructure and the low penetration of cars make distances to oblast centers or county seats where administrative or social services are provided a very important factor. Enlarging counties or oblasts seems little more than an ill-thought out project by Kyiv politicians rather than an urgent need.*

*The main conclusion of project experts was that large-scale administrative–territorial reform is impossible in Ukraine for a number of objective and subjective reasons. Still, a move to merge feeble ATUs at the lowest level—villages and small towns—that is not done in a mechanistic way but takes into account regional peculiarities is probably realistic.*

***Broad-based administrative reform is impossible***

### 3.2. A clear distribution of powers among all levels of government

The overlap and duplication of powers among local governments and local state administrations needs to be eliminated.

By setting up executive bodies for county and oblast councils that will focus solely on governing functions, it will be possible to depoliticize the councils themselves and task them with handling the development of their communities, a typical local government job. It will also improve the quality of public services, as county governments will be more dependent on county residents.

***Executive organs are needed at the county and oblast level***

The nature of local state administrations needs to change. By being relieved of their economic functions, they will be in a position to monitor the compliance of local governments with the law and public service standards. In this case, the existence of state administrations at the county level seems pointless.

***Local administrations should oversee the enforcement of legislation***

There also needs to be a fixed set of public tasks that each level of government will be responsible for by law, that is, through a new law “On local government” or two new laws: “On community government” and “On county government”. At each level, the delegated powers must be exclusive.

### *Proposed list of community powers*

*If the communities are enlarged to capacity level, the idea is to delegate these tasks to them:*

- *pre-school education and upbringing;*
- *secondary education and extracurricular activities;*
- *care of the elderly and disabled;*
- *preventive and primary medicine;*
- *land management;*
- *environment protection;*
- *housing construction planning;*
- *municipal and residential utilities (water supply network, sewage, heating, power and energy conservation);*
- *landscaping, maintenance of local roads, streets, parks, cemeteries, and so on;*
- *local transportation;*
- *organization of recreation and cultural activities (clubs, libraries);*
- *health and sanitation;*
- *veterinary control and prevention.*

*Those powers that can not be exercised by communities should be delegated to the county level and those that can not be exercised at the county level should be delegated to the oblast.*

***The powers of local governments at all levels should be specified in law***

*Participating stakeholders mostly agreed that it was necessary to eliminate the duplication of powers between the state authorities and local governments and between different levels of local government. One proposition was that there be a comprehensive list of the powers delegated to local governments of each level and to state authorities written into law.*

*No effective solution was proposed for legislating the limits of local government powers within a single administrative-territorial unit. It may be that this will be impossible to do without introducing changes to the administrative-territorial system.*

### 3.3. Fiscal independence for local government

#### 3.3.1. *Providing a sufficient fiscal base for local government*

First, the local tax system needs reforming, namely by introducing a property or real estate tax and reforming the existing land tax. There is the risk that such a step will be unpopular, so any move will need an effective information and promotion campaign. Property tax could be mitigated during the introductory phase by establishing a simplified mechanism for calculating it and modestly low rates.

***A property tax and a reformed land tax are needed***

Second, the majority of state taxes need to be earmarked for local government use. This should spur local governments to expand their tax bases. One negative consequence of such a decision could be even greater regional discrepancies as to the quality and accessibility of public services. Financially independent regions will be able to provide better quality services, while underdeveloped regions will not be able to match them. This calls for effective mechanisms to ensure financial leveling and leveling transfers are likely to be larger.

***Most state taxes should be designated for local budgets***

Third, mechanisms are needed that will motivate the state tax service to collect local taxes and duties, possibly by instituting of dual accountability on the part of the heads of local tax offices.

*In discussing the prospects for a real estate tax and an improved land tax, participating stakeholders agreed that both were needed. They did express some reservations as to the timeframes involved and were*

**Impact analysis  
is needed before  
instituting new taxes**

*not all certain whether these taxes could fill local budgets.*

*In the first place, as Dnipropetrovsk Oblast administration representatives stated, before even introducing a property tax it would be necessary to carry out a feasibility study, to determine what kind of revenue volumes it might bring and it would match the eventual cost of administering it. This could be vital for certain disadvantaged territories, given the need to reduce the tax rate for property providing less than the norm of space per resident and property belonging to poor people.*

*Spacious properties that would be subject to the highest tax rate tend to be distributed unevenly, mostly in communities in close to large cities. This is why introducing a property tax in more remote communities will not have the necessary impact on their budgets.*

**Without a land  
market, a land tax  
won't work**

*The question of reforming the land tax was also hotly debated. According to some of the ideas voiced, this reform needs to be combined with a more active institution of an agricultural land market. Currently, land offers few serious revenues. In more remote residential areas, arable farmland is often left uncultivated. Having a land tax when land is not being worked or is being poorly used is pointless.*

*One factor that might make the land tax more beneficial according to some participating stakeholders would be to transfer land adjacent to residential areas to the local community's jurisdiction and to extend the principle of universal local government throughout Ukraine. In addition, there were proposals to provide local governments with the power to monitor whether farmland locate on their territory is bringing its owners any income.*

### 3.3.2. *Enforcing state and local government fiscal obligations*

To solve this problem, a workable mechanism needs to be developed and enshrined in law to allow local governments to refuse to take on functions that are not funded fully by the State Budget and one that would allow them to forcibly draw on funds from the State Budgets in situations where tax breaks introduced in Kyiv result in lower revenues at the local level.

Gradually, certain delegated powers should become local and be funded from local sources of local budget revenues.

At the same time, the central government and the Verkhovna Rada should refrain from impinging on areas of local government authority, especially by offering breaks on local taxes and fees.

One solution of this problem could be to settle disputes between local governments and local state administrations through the courts. Participating stakeholders repeatedly emphasized the need for closer ties between local government reform and judiciary reform.

### 3.3.3 *Establishing public service standards and means to assess their cost*

The standards for administrative and public services need to be updated and brought into line with modern requirements. These upgraded standards should be accessible both to service beneficiaries and service providers, and become the basis for:

- forming a budget for the entity that is the service provider;
- calculating interbudgetary transfers;
- effectively controlling expenditures and assessing service quality.

***Local governments should not take on functions that are not funded***

*Developing service standards goes hand-in-hand with training in instituting them*

*There were varying proposals to introduce public service standards from stakeholders. First of all, they said that developing such standards and, even more so, instituting them at the regional level would require considerable resources to be earmarked in the State Budget. To ensure a successful introduction, it would also be necessary to train local officials to apply these standards. Otherwise, they would remain on paper only.*

*These standards should be developed in partnership with local representatives*

*Stakeholders were also concerned about the possibility that the positions of local governments in different regions might be ignored while the central government developed the standards and the methods for calculating their cost. Participants emphasized repeatedly that, if local governments were not involved in the process, the ultimate standards and the assessment of their cost would either be largely ignored or would cause many regional distortions. Overly high and idealistic standards devised by the central government could lead to a situation where few communities could actually meet those standards. The calculation methodology also needs to be flexible to reflect the difference in the cost of goods and services in different regions.*

### 3.4. Effective use of funds, assets and other resources

#### 3.4.1. Effective use of funds

*Budget reform is needed*

The ineffective and inappropriate use of public funds can be resolved through budget reform whose key component is decentralizing public finance. Four main steps are necessary to achieve this:

- standing legislation should be reviewed and obligations that can be funded neither by the state nor by local governments need to be tossed;
- workable procedures are needed for merging communities and co-financing certain public service

functions, especially the possibility of financing of a single institution from different budgets on contractual basis;

- a system of overseeing and monitoring the effectiveness and efficiency of budget expenditures is needed, including planned audits. In particular, some way of introducing management by objectives needs to be considered for budget planning and establishing independent public institutions that can monitor the legitimacy and effectiveness of local budget use and conduct regular audits.
- the network of publicly-funded institutions needs to be optimized if public money is to be spent more effectively.

*Participating stakeholders focused most on the need to monitor public spending. They said that the main emphasis must shift to getting community, media and local activists more involved in this process. NGOs, which view independent public monitoring as one of the main ways to make the use of public funds effective, were especially vocal during the discussion of this issue.*

*The project experts were given information about a number of pilot projects taking place in this sphere, including efforts to monitor public funds launched by a coalition of NGOs in Dnipropetrovsk. To increase the effectiveness of their local government, this coalition is working to introduce public policy mechanisms: open debates of important local decisions with all stakeholders and a search for consensual solutions. This kind of work needs to be extended to other regions.*

**Public monitoring of public spending is the key to effective use of resources**

### 3.4.2. *Effective management and intended use of community property*

The status of community property needs to be regulated by law. In addition, the allocation and registration of municipal and state lands needs to be completed. Finally, there has to be effective, independent public control over how legitimately and appropriately community assets and property are managed and land issues are handled.

***Mineral, forest and water management are all ineffective***

*Participating stakeholders considered it necessary to restrict the opportunities local government officials have to bargain away community property. One particular idea voiced was to legislate a ban on the free transfer of subsistence plots to individuals by local governments, as this provision offered many opportunities for corruption.*

*In addition, stakeholders proposed involving local communities in overseeing state management of resources and property in a variety of ways. Their priority was forest, water and land resources. The majority of speakers stressed that public management of these resources was very poor because they mostly function as cash cows for those officials who manage them and for private business. One original idea brought up was that natural resources should be divided into two categories: strategic resources, whose management should be left with the central government, and local resources, such as granite, sand and so on, whose development should profit local communities.*

### 3.5. Local government participation in making state policy

Any drafts of legislation that affects local interests need to be coordinated or debated, at the central level, with national associations of local governments and, at the local level, with the government of the relevant level. This coordination and consultation should be made mandatory by law.

According to a statement by the Association of Cities of Ukraine, mechanisms for cooperation between the Association and the Verkhovna Rada have already been developed and implemented. However, cooperation between the Association and the Cabinet of Ministers needs improvement.

*Proposals from stakeholders on how to resolve this problem were diverse. Some stakeholders insisted that, to reflect the interests of local government more fully, a bicameral legislature is needed to form state policy, with the upper chamber being formed of representatives of local government and would be able to control and restrict the legislative initiatives of the lower chamber.*

*In addition, some said that, to solve this problem, local governments and their associations needed to lobby more. Only pressure from below was likely to put local government reform on the central government's agenda and make it pay attention to local communities. Another option was to get local party activists to unite to lobby necessary changes in their parties' policies towards local government.*

*It became clear during the consultations that such lobbying groups would not be equally active in all regions of Ukraine. For example, in Lutsk and Chervivtsi political party representatives expressed readiness to take on more power and more responsibility. Local politicians saw local government as the place for their professional activity and thus viewed its re-*

***There's no mechanism for local governments to interact with the Government***

***An upper chamber of parliament could represent local government interests***

*form as an opportunity to expand their sphere of influence.*

*On the other hand, stakeholders from other regions, such as Dnipropetrovsk, expressed strong doubts that local deputies would welcome reforms that would increase their powers and responsibilities. In their opinion, political parties in these regions were immature and the interests of local deputies were limited to land allotment, which they tended lobby for their own benefit under the current system. Needless to say, these deputies care little about reform. Even if their powers were increased, they would be at a loss as what to do with them and the quality of local services in such regions would not improve as a result of reform.*

### 3.6. Stronger human resources for the local public sector

Like the civil service, service in local governments needs to be professional and apolitical.

***Administrative and political positions must be distinguished at the local level***

In particular, there needs to be real competition for jobs and career promotions and it must become impossible to dismiss municipal officials for political reasons and other subjective factors. Most importantly, political and administrative positions in local governments need to be clearly distinguished. Salaries for municipal officials need to be in sync with salaries in the private sector, in addition to being transparent.

Once county state administrations are eliminated, it will make sense to encourage those officials to switch over to local governments, especially, to the executive committees of county councils.

It is especially important for local governments to institute mandatory continuing professional development for officials.

The enlargement of communities is likely to have positive impact on the quality of human resources for the

local public sector, as it will increase competition for jobs in this sector and will provide more opportunities for competent people to develop careers.

*Participating stakeholders thought that this problem was one the most essential. It was mentioned in almost every region where consultations took place. Stakeholders were adamant that there needed to be a system of continuing professional development for local government representatives and professional training for local council deputies.*

*In discussing the need for municipal officials to continue to develop professionally, stakeholders noted that professionalism needed to become one criterion in performance appraisals and career promotions for officials. Only under such conditions would these individuals be motivated to continue their professional development. If professional development fails to become one of the criteria against which a municipal official's performance is measured, the municipal officials will have little incentive to attend professional development programs.*

*Although the professional development of deputies should, logically, be a matter of concern to the leadership of local parties, the latter lack the capacity to undertake it. So, this issue needs to be the focus of attention for international donors who are working on local government development, and possibly state government.*

*Stakeholders discussed mechanisms for resolving this problem, such as training local deputies at State Budget cost in return for registering them in the Civil Service reserve.*

*Also, Zhytomyr Oblast representatives reported on the status of a pilot project for training local government officials. This is being conducted by the Main Civil Service Administration and the oblast council. Unfortunately, this project remains a pilot at this time.*

**Both the state and donors need to focus on training local deputies**

**Educational requirements for local deputies could be set in law**

*One radical proposal was to include specific education requirements for those running for local councils and the mayor's office in electoral legislation.*

### 3.7. A different system of council elections

Local governments need to represent the interests of their electorate, that is, the residents of their community, county or oblast. This means that Ukraine probably needs to go back to the majority electoral system in cities and switch to a proportional system with open lists at all other levels.

With a majoritarian system of elections, elections to county and oblast councils could take place at polling districts whose borders coincide with the boundaries of territories to be represented on the given council. In counties, this means community boundaries; in oblasts, it means counties and oblast-level cities. This should ensure proper representation of the common interests of county and oblast communities.

Moreover, local and national elections should be held at different times, which would enable voters to devote more time and attention to local elections.

For councils to be able to represent the interests of local communities, a provision could be introduced according to which only residents of the relevant city, county or oblast would be eligible to run for office at that level.

**The closed proportional system is ineffective**

*The lack of professionalism among local deputies, as participating stakeholders saw it, was a direct result of the change in the electoral system. The closed proportional system was much criticized by participants. They said that, although the new election system had some positive effects in terms of the development of political parties at the local level, local representative bodies also worked less effectively as a result.*

**Stakeholders did not agree about the best electoral system**

*However, stakeholders were unable to find a reasonable and consistent answer to how the system should be changed. Some proposed going back to the majoritarian system.*

*rity system and shifting to a proportional model with some type of open lists. The discussion also led to the conclusion that analytical and consultative work was needed with stakeholders at the local level so that they could make up their own mind about which electoral system was better for them and start lobbying for it in Kyiv.*

### 3.8. Public participation in decision-making and overseeing government

Mechanisms are needed that will make it possible for the public to participate in the making of important local decisions. A law on local referenda needs to be adopted. To improve the quality of administrative services, such services need to be decentralized and delegated to the local government.

***A law on local referenda is needed***

*Participating stakeholders actively proposed other changes that might allow for more effective community oversight of local government. Among these was improving the mechanism for removing local deputies from office, giving this right to voters, rather than a party's executive. Another suggestion was to establish a stricter approach to the responsibility of state administrators if local councils voted non-confidence in them and stricter accountability on the part of elected representatives under law.*

***The mechanism for recalling deputies needs improvement***

*Stakeholders placed considerable hope on such instruments as public councils and hearings as a way to oversee government. However, to make these more effective, provisions on public hearings need to be both more simple and more mandatory for local governments in clearly specified instances. At the moment, most community statutes simply state that such hearings "can be held." Also, the level of representation of stakeholders needs to be clearer, because such hearings are currently not very representative. Both these instruments can be written into the statutes of all local communities.*

***Provisions on public hearings also need improvement***

***The capacity of local CSOs to monitor and oversee government must be raised***

*Another problem with public oversight is lack of capacity among community organizations to represent their own interests at council meetings or hearings, even when local governments are open to the idea. A good example is Mykolayiv: stakeholders from the local government reported that community representatives on the permanent advisory committee attached to the deputy commission on local government were quite inactive. Capacity-building among such local organizations should be the focus of efforts among both officials and international donors.*

### 3.9. More consistent state policy countrywide

***The post of head of state administration must be depoliticized***

Local state administrations need to be depoliticized. The posts of local state administrators should be included in the list of civil service postings and politically neutral professionals should be appointed to those positions. As these individuals will not perform any governing functions, they should not be answerable to the local councils.

The law also has to establish personal responsibility for local government officials, including locally elected deputies, for decisions that are in violation of the law.

***Judiciary reform is imperative***

*According to participating stakeholders, this problem could be partly resolved through judiciary reform. In addition, they agreed that local administrations could be more effective at ensuring consolidated state policy if they were relieved of all local government functions and left with only such functions as overseeing local government compliance with the law and with standards of public services.*

### 3.10. Local government reform that is clear, reasonable and consistent

Regional government, that is, executive bodies for oblast councils and the transformation of local state administrations into coordinating and supervisory bodies overseeing the legitimacy of the work of local governments, needs to be instituted in Ukraine. However, if it is introduced before there is proper local government, it could lead to a certain imbalance in the political structure if reform is implemented simultaneously at all levels. Moreover, there is a risk that political power will then concentrate at the oblast level, hindering full decentralization and the development of meaningful local government.

Moreover, to avoid conflict between oblasts and their centers, one proposal is to assign the status of “urban region” to some of the country’s largest cities and providing them with the functions and powers at both local and oblast levels.

# Annex 1. Decentralization and transparency: local government reform in Hungary

The relationship between central and local government is changing. The idea of decentralization is now accepted as the way forward in many countries worldwide. Moreover, there are many different reasons for introducing a decentralized system.

The introduction of pluralistic democratic government at the national level led in almost all CEE countries to an immediate demand for parallel reform in local administration. What varied greatly, however, was the speed with which these elected bodies were vested with the powers and resources that determined their real weight in local affairs.

Three sets of issues typically posed challenges:

- territorial structure;
- assignment of competencies;
- funding.

*The size of administrative units and options for reforming local government*

The European Union introduced a common classification of territorial units, called the NUTS system. Why is this NUTS system important for decentralization and Member States? For one thing, NUTS levels are used for allocating structural funds as the classification system is hierarchical. Member States may decide to go further still in terms of hierarchical levels by subdividing to NUTS Level 3. The NUTS level to which an administrative unit belongs is determined on the basis of population thresholds shown in the Table 1.

***The NUTS system is used to distribute EU structural funds***

*Table 1. Territorial Structure: Territorial Units in the EU*

Level	Minimum population	Maximum population
NUTS 1	3,000,000	7,000,000
NUTS 2	800,000	3,000,000
NUTS 3	150,000	800,000

It is interesting to compare the administrative figures and the NUTS II figures of the new member states. Here, we can see that, of the 10 countries shown, only three have adopted the regional decentralization model.

*Table 2. Territorial Structure: Higher Levels*

Country	Number of NUTS II Units	Number of Intermediate or Upper Levels of Government	Type of Regionalization
Bulgaria	6	28	Administrative Regionalization
Czech Republic	8	14	Regional Decentralization
Estonia	1	15	Administrative Regionalization
Hungary	7	19 counties + 22 cities with county status + Budapest	Administrative Regionalization + Regionalization by Existing Local Government
Latvia	1	26 districts with rights + local governments 7 cities with district rights	Regionalization by Existing Local Governments
Lithuania	1	10	Administrative Regionalization
Poland	16	16	Regional Decentralization
Romania	8	41 + Bucharest	Regionalization by Existing Local Governments
Slovenia	1	58	Administrative Regionalization
Slovakia	4	8	Regional Decentralization

The question is: Would it be relevant to base a new government tier on the NUTS II level? In the countries without a decentralization model, the NUTS II level could be considered a possible framework for regional development planning. In Hungary, the Regional Development Act provided for the formation of regional councils called macro-region development councils in each NUTS II unit, with decision-making powers for the implementation of regional policy. However, these regional councils are not a new tier of government, but rather an assembly of representatives of institutions involved in regional development.

*The NUTS-2 level is for planning regional development*

Table 2 shows that there is generally a clear-cut divide between the approach to regional development and the approach to territorial administrative division of the country. Poland is the only country among 10 in which the country's regional divisions and the NUTS II level coincide. This reflects the fact observed in EU member states that territorial reform is not only a response to new problems, but also a result of history, of existing legal systems and patterns of institutions, and, last but not least, of party politics.

*The administrative territorial structure of EU countries does not match the NUTS system*

In the majority of CEE countries, local government legislation has allowed human settlements of any size to claim the status of an autonomous municipality. The result is that the basic level of local government has a highly fragmented territorial structure, as illustrated in Table 3.

*Local government is very fragmented in CEE countries*

*Table 3. Number of municipalities and their population in CEE countries*

Country	Number of Municipalities	Mean Population of Municipalities	% of Municipalities with Less Than 1,000 Inhabitants	% of Population Living in Municipalities with Less than 1,000 Inhabitants
Estonia	254	5,713	9.4	1.2
Latvia	563	4,400	32.1	5.6
Lithuania	56	66,300	1.8	0
Poland	2,483	15,561	0	0
Czech Republic	6,230	1,659	79.8	16.7
Slovakia	2,875	1,874	68.4	16.2
Hungary	3,152	3,242	54.7	7.7
Slovenia	192	10,344	3.1	0.2

***Municipalities must have at least 5,000 residents***

The target minimum in Western European reorganization at the basic levels of local government has average population sizes well over 5,000, which has been and is viewed empirically as adequate for most municipal services. However, most CEE countries have thousands of communities claiming municipal status with populations below 1,000—and a substantial proportion of these fewer than 200. Reform programs are challenged by the inability of such communities to provide administrative and fiscal capacity.

***Efforts to consolidate communities run into political opposition***

There is a range of solutions to territorial fragmentation, including amalgamation of smaller units, performance of tasks through inter-municipal bodies, and assignment of selected tasks to either central municipalities or to higher tiers of government. Local government associations resist the compulsory frameworks that usually accompany inter-municipal cooperation on any significant scale. Assigning tasks to central towns is unpopular with villages, and assigning them to higher tiers is unpopular with the larger towns.

### *The system for managing development at the regional level*

Similarly to the practice of other countries, the spatial and settlement structure of Hungary is laid down in its Constitution. Accordingly, the total national area is divided into the capital, counties, towns and villages. In Hungary after the change, the Constitution and the Act on Local Governments recognized those rights of local communities, including the smallest of settlements to govern their own local affairs. As a consequence, the number of local units jumped from 1,500 to 3,152.

The passing or amendment of acts concerning the local government requires a two-thirds majority in the Parliament. This qualified majority requirement is intended as a safeguard, but it can occasionally generate tensions and even hold back opportunities to introduce change. This is particularly the case in Hungary at present where, following the recent local elections, the opposition has a majority in most local governments.

Local government in Hungary exists at two levels: the municipality and the county. There is no hierarchical relationship between the two levels. County governments are neither superior organs to municipal governments, nor do they have any supervisory authority over them. The difference between these two lies in the administrative tasks delegated to them. Municipalities provide local public services to their settlements; counties have a subsidiary role in that they provide public services that settlements cannot undertake, as well as those that have a territorial character.

In the European Union, regional level units have a dual function: to develop underdeveloped regions; and to mediate between central and local public administrative responsibilities, organize regional services, and reduce differences among local geographical units.

In Hungary, seven 7 planning and statistical regions have been set up, corresponding to the NUTS system. In each region, a council will be formed of representatives of micro-regions, mayors of big towns, representatives of eco-

***Hungary's options for changing its territorial administration are complicated***

***At the NUTS-2 level, Hungary has established 7 development regions***

conomic and social partners, and representatives of relevant ministries. The Council's main tasks include the formulation and adoption of a regional development concept and programs, the coordination of territorial economic development, the preparation financial plans, and policy on decentralized development sources.

***Administrative bodies at this level do not have the status of local governments***

Hungary will not necessarily have to establish self-governing assemblies in the regions either, but this can be one objective in the process of constitutional amendment, and the present regional development institutional system may provide the regional basis for the programming and the allocation of government funds.

### *Hungary's micro-regions and local taxes*

***Micro-regions are municipal unions that provide public services***

The reason for the establishing the micro-region system in 2004 was firstly to develop more structured joint provision in key areas of public spending, including development projects. The central government is encouraging municipalities to use the micro-regions as a basis for such joint provision. Several incentive mechanisms have been introduced, such as progressively larger grants, threshold requirements in investment grants, and one-off and formula-based compensations. As of 2007, some penalties have also been introduced. For example, the "deficit grant" will no longer be available to those municipalities that are not in an association for the joint provision of educational services.

***Almost all micro-regions provide common educational services***

Virtually all the micro-regions are now being used for joint provision and are running at least three services. The most common joint provision as Table 4 shows is in education. Though the micro-region system seems to be running well, there is some scope for improving governance. The micro-regions are typically run by the association councils comprising only the mayors from participating municipalities. Reportedly, in some instances this is leading to excessive marginalization of municipal assemblies.

*Table 4. System of Micro-Regions in Hungary\**

Purposes	Number of Micro-Regions with Joint Provisions	In %
Education	162	98
Social Institutions	21	13
Basic Social Services	113	68
Children-Protections Services	2	1
Basic Children-Welfare Services	136	82
Mobile Libraries	77	46
Internal Audit	152	92
Total Number of Micro-Regions with Joint Provisions	165	99

The total fiscal capacity of municipalities is basically determined by

- exclusive revenues from local taxes, local fees and user charges,
- municipal surcharge on shared taxes, mostly on personal and corporate income,
- revenues from the sale or rental of municipal property,
- bond fees, bank credits and other interest income,
- income from municipal companies, and
- general and special subsidies and grants of the central government, and so on.

The ability of municipalities to mobilize their own fiscal resources is generally judged quite limited, partly because relevant decisions on local tax bases and rates as well as tax sharing schedules have been made by the central government and/or are subject to serious restrictions in the national tax law. Although the intergovernmental

\* As of February 2007.

*The largest local tax  
in Hungary  
is the business tax*

transfer system is constructed differently from one country to another, the dominance of a purpose- and project-oriented grant system is apparent.

In Hungary, under the current legal framework, local authorities have a relatively wide margin of discretion about how to from their local taxes. The heaviest local tax is the business tax. But there are problems with it:

- It erodes the local tax base and increases pressure on tax competition.
- To the extent that regional disparity in the local business tax base broadly matches that of wealth, strong reliance on local business taxes aggravates regional income disparities.

At present Budapest and surrounding municipalities collect the most local business tax and, indeed, four districts within Budapest alone account for 30% of total business tax revenues.

*Table 5. Local Taxes in Hungary As of 2005*

Type of Tax	Number of Municipalities Levyig the Tax	Number of Municipalities Levying The Tax as a % of Total Number of Municipalities Levying at Least One Tax	Amount of Revenues Raised As a % of Total Local Revenues
Building tax	734	23,6	11,2
Land tax	402	12,9	1,3
Communal tax for individuals	2190	70,5	2
Communal tax for business	702	22,6	0,3
Tourism tax	519	16,7	1,3
Local business tax	2639	85	84
Total number of municipalities having at least one tax	3106	100	100

Acknowledging these problems, the government announced in 2005 that firms would be able to fully deduct local business taxes paid in calculating their corporate income tax in 2006 and that the local business tax would be completely eliminated in 2008. However, only the first step has been implemented so far, while the abolition of the local business tax has been suspended as part of the government's measures to rein in its deficit.

### *The structure of municipal local government bodies*

The basic rights and powers of local government are exercised by the **body of representatives**, which may delegate authority to the mayor, and its committees. Delegated powers may not be transferred further.

The decision to establish **committees** is determined by the representative body, which elects members to such committees. More than half a committee's membership must be elected from among representatives, but the remaining members may be citizens or representatives of citizens' organizations. Committees draft decisions and the representative body may grant committees decision-making power, too.

The **mayor** is the political and administrative head of the local government and is responsible for local policy implementation. The **chief executive**, also called the notary, is a public administration professional, while the mayor represents its political side. Thus, the chief executive is appointed, not elected, by the representative body for an undetermined period and on the basis of open competition. The law establishes the qualifications of chief executives.

The chief executive manages the **office**, is responsible for its day-to-day activities and is expected to ensure the lawful activities of the local government.

*The main powers of local government belong to the representative body*

*The head of local government is the mayor*

### *Transparency in local government and community oversight*

Effective and efficient local government requires not only incentives from the central government but also strong oversight by local citizens. This can be helped by regulations ensuring transparency in the actions and outcomes of local government and by participation in decision-making.

*Public hearings  
are not an effective  
instrument in Hungary*

Unfortunately, these are arguably inadequate in Hungary. For example, regulations stipulate that at least one public hearing per year must be held. While virtually all municipalities comply, only a small fraction of them exceed this obligation. There are no strict rules for the organizing such public hearings, either, meaning that agendas can be set up in such a way as to avoid sensitive issues. Moreover, public hearings are often poorly advertised and, as a result, poorly attended.

Local governments carry out a significant share of public procurement. Hungary scores fairly well in OECD indicators for procurement policy and the latest report concludes that most local public procurements follow the rules of open tendering procedures. However, it also points out that half of these local governments have yet to comply with the obligation to establish an internal code of conduct. Public procurement practices also feature among the complaints of foreign investors, along with other aspects of red tape and administrative procedures.

### *Local government and the system of state power in Hungary*

The creation of new local governments in 1990 required the transformation of the entire system of public administration. Before 1990, the state administered local affairs in accordance with the principles of centralization and hierarchy through a system of councils at the local level. Since 1990, Hungarian **public administration** consists of two main components: bureaucracy and democratic institutions.

The first includes central government bodies and their organs at the local and territorial level (de-concentrated institutions), which are subordinate to the state administration. The second type of structure is the system of **local governments** (decentralized institutions), based on principles of autonomy and subsidiarity. The functions of public administration are shared by these two components.

Wage-setting and employment conditions for public sector employees are strongly centralized. The central government imposes a limit on increases in the number of permanent employees and sets salary scales and wage adjustments. Local governments should be given more leeway in designing work contracts with their employees and in setting wage levels to reflect local conditions better. The central government is moving ahead with reforms to remuneration and management for civil servants and similar systems are supposed to be adopted by local governments.

New European Union member states face significant challenges that require a strong public management system:

- the continuing challenges of fiscal management with many of the new member states not meeting the entry criteria for the euro zone on fiscal parameters, including deficit levels;
- new challenges of effective absorption and utilization of EU funding, which will amount to up to 3.5% of GDP in the next funding period;
- the future challenge of remaining competitive inside and outside the EU.

A strongly performing public management system is an essential ingredient of sound fiscal management and effective development planning, both of which require well developed strategic planning and policy management capacity and a stable and qualified human resource base.

Decentralization is a complex and contentious process. It involves choices that are either politically or technically difficult—or both. It requires the reconciliation of conflicting interests. It demands tenacious spadework and, to drive the process through, determination and positive enthusiasm.

In the course of its systemic changes, Hungary faced historic challenges to establish a new type of local and central public administration and to form a government based on the results of democratic elections. Since 1996, Hungary has been addressing longer-term difficult issues, such as policy implementation, as well as problems arising from the transition itself, such as overly rapid decentralization in the early days of the reform process. By the end of 1999, the transitional challenges of building up basic legal and policy frameworks consistent with market democracy had been largely met. After 10 years of determined reform, Hungary has entered the mainstream of the EU countries with respect to the challenges it faces in establishing quality public administrative regimes supporting good governance and long-term economic growth.