

SECTION 1. ACCOUNTING AND AUDIT

1.1 Role of political power on Ukrainian amalgamated municipalities (hromadas)

Abstract

The decentralization reform was started in Ukraine in April 1st 2014 with the implementation of Concept of Local Governance Reform and Territorial Organization of Power in Ukraine. Due to the centralized government (before implementation of decentralization reform), the development of local territory was slow or in some cases abandoned. Most people moved to big cities, which had brought financial losses to local government and due to these reasons, the quality of public services was poor, which harmed the local government's prestige among local people. The implementation of decentralization reform gave legal base for local communities to form municipalities and to collect local taxes and some of those taxes that were given to central government were transferred to local municipalities, so that local government could develop their own territory more efficiently and provide better quality of public services.

The main reason of implementation of decentralization reform is the external pressure. This component of institutional theory was mentioned by Tolbert & Zucker (1996) and according to their research, the external environment can force institutions (government entities) to bring changes inside organization. This external pressure was greatly increased in 2014 by Ukrainian society and the central government was forced to bring changes otherwise they (central government) would face the crisis of legitimacy.

Despite the implementation of the decentralization reform for almost 7 years, the financial dependance of Amalgamated Hromadas did not decrease from the central government. According to the website *Monitoryng*, more than 50% of their revenue come from central budget transfers and there is no trend in decreasing.

Purpose

The aim of the study is to develop recommendations to reduce the financial dependence of Ukrainian municipalities on the central government through a detailed analysis of the causes of such dependence.

Amalgamation and its motives

Jason (2020) defines amalgamation as an action in which two or more entities form a single entity. Amalgamation is a merger of two or more institutions (local government) into one institution.

There are different reasons for amalgamation among municipalities, such as: public service delivery motives, local democracy motive, political motives, structural motives and other motives (see table 1).

Public service delivery motives

Leland & Thurmaier (2014) mention in their work that one of the reasons of municipalities amalgamation is due to the sharing of service responsibilities. According to them, amalgamation of municipalities helps to create a foundation for creation of a platform through which members of amalgamated hromada (municipalities) can form a cooperation in sharing their responsibilities for providing public services and goods.

Table 1 Motives for Municipalities Amalgamation (based on Nanci et al., 2019)

Motives	Author/Year	Specific Motives
Public Service Delivery	Leland & Thurmaier (2014)	Sharing of service responsibilities
	Vojnovic (1998)	Effectiveness and efficiency of service delivery
	Swianiewicz (2018)	Improve public service provision
	Allers & Geertsema (2016)	Bring specialization to public labor market and improve division of labor
	Steiner & Kaiser (2017)	Decrease the cost of public services through different mechanism of provision (ex. Privatization)
	Dollery & Yamazaki (2018)	Decrease the cost of public services and improve their quality

Local Democracy	Tajbakhsh (2000)	Increased local political voice
	Suzuki & Sakuwa (2016)	Higher political trust among local people
		Increase participation rate of people in local elections
Political	Leland & Thurmaier (2014)	Policies of sustainable regional development
	Farid (2018)	Increased urbanization rate in amalgamated municipalities
		More logical land planning
	Miyazaki (2018)	Central government is more persistent in demanding provisions of public services from local government
	Strebel (2018)	Strong local council
		Better informed central government
Structural	Drew et al. (2017)	Larger Scale
		Improved infrastructure
		Better condition of economic and political structures
Other	King (2008)	Improved response to natural disasters

Vojnovic (1998) proved that when the sharing of responsibilities is happening in municipalities, effectiveness and efficiency of service delivery is improved greatly. Swianiewicz (2018) mentions in his work that some municipalities are too small and as the result they do not have enough financial resources and strength in managing waste, financing infrastructure, have enough capacity or providing services and finance some welfare services. Due to these reasons, amalgamation is the only way for municipalities to ensure their fulfillment of responsibilities. Allers & Geertsema (2016) mention that large municipalities have specialization and improved division of labor. With amalgamation, the local governments get bigger population and as the result local governments have more choices in hiring, which allow them to hire better educated workers or those who are already trained and have experience.

Steiner & Kaiser (2017) talk about amalgamation as a chance for municipalities to rebuild current mechanism of delivering public services and even have a privatization to allow private enterprise to provide those services. It should increase the quality and decrease the price of providing those public services, so amalgamation will aid municipalities in decreasing the cost of delivering public services and increase their quality for local population (Dollery & Yamazaki, 2018). So, local authorities and residents are interested in amalgamation, because it improves provided public services.

After amalgamation, municipalities have more financial resources, which could be used to repair the existing infrastructure and build new infrastructure, to provide better quality and at the same time. The cost for municipalities will decrease, due to combination of existing infrastructure and newly build infrastructures.

Local democracy

Population size is one of the most important factors for amalgamation. Local representatives of municipalities want to have power to have a voice and power in changing national policies and to do so, according to Tajbakhsh (2000), local government merges with each other to get bigger voice in national politics. There are opponents to the idea of amalgamation and their main argument is that when municipalities merge, people tend to focus more on its functionality and neglect its local people demands. On the other hand, Suzuki & Sakuwa (2016) agree that the amalgamation make municipalities larger in size and population, which at the beginning makes local representatives focus on its functionality and ignore some demands of their voters, but at the same time large municipalities increase voters trust, makes them more motivated in participation of local politics and thus amalgamation brings more positive results to the local community than harm.

After the amalgamation, the number of residents will increase, which in turn will increase the political power of the municipality. The more people live there, the higher the voice of municipality in the eyes of central government. The second benefit for local democracy is that after amalgamation, more people will participate in local elections, because their trust is improved.

Political motives

The first benefit that amalgamation brings in category of political motives to municipalities is that the amalgamation makes it possible to have policies of sustainable regional development. Leland & Thurmaier (2014) in their work prove that larger municipalities are better equipped compared to their smaller counterparts and as the result their bigger size can make them sustain regional development. Farid (2018) has

the same opinion and his research prove that the larger the size of municipality can improve its urbanization. The increase of municipalities size makes local council face more responsibilities and larger pressure, which as the result force them to use their resources more efficient and thus plans of using land (land planning) are more professional and logical. So, amalgamation can bring to local council a sustainable regional development and urbanization.

The size of municipality does not only benefit local politicians and bureaucrats, but it brings some benefits to local people. The larger municipality the bigger responsibility of a municipality, but in some cases in bigger amalgamated municipalities if something goes wrong, local community can blame the central government instead of the local council or their representatives. Due to this reason, according to Miyazaki (2018), if local representatives cannot fulfill their obligations and responsibilities to local people, central government may interfere and put pressure on them and demand that they provide obligated services that local government is responsible, otherwise central government may even make such incompetent municipalities merge with a bigger one, which is more responsible and have better management, in other words, destroy incompetent municipality and fire incompetent local official through the amalgamation process.

The last political motive which promotes amalgamation is that the merger of municipalities can bring stronger and stable local councils. Strebel (2018) emphasized that in those territories that have population who speaks different languages it is common for municipalities to unite with other municipalities who have the same culture, common history and population that speaks the same language. It will bring more stability and efficiency to local area and at the same time central government will better understand the needs of different population in their country.

For the political motives, the main benefit after amalgamation, can be considered the sight of the central government. The central government will demand from the representatives of amalgamated municipality, to provide better quality of public services. Due to amalgamation, the number of residents will increase and if something

goes wrong, those residents will blame central government and because of that, central government will put more pressure on amalgamated municipality.

Structural motives

Economical structure, political structure infrastructural structure will greatly improve through amalgamation (Drew et al., 2017). The increase of municipalities territory and population will greatly improve municipality's resources. More people usually mean more collected taxes and better political structure in local area. With more resources, local government can better finance and upgrade local infrastructure as the result the urbanization process is smoother; amalgamation increase the scale, so more human resources are available, which can increase efficiency, because with the increase of population, there should be specialist or more well-educated employees who can improve the overall structure of municipalities.

After amalgamation, the combined financial and human resources should improve the overall structure of municipality. The increase of population of amalgamated municipality will bring higher experience workers and more financial resources due to the increase of local government's territory.

Other motives

For the other motive category, natural disasters are mentioned by King (2008). In areas where natural disasters often happen, small municipalities are simply incapable to deal with them, so small municipalities have to merge with other municipalities to better deal with future natural disaster and in some countries, central government even encourage those small municipalities to merge, so better efficiency and less casualties will happen in those municipalities after natural disasters.

So, in areas where the rate of natural disasters are high, small municipalities cannot survive, due to insignificant financial resources and the lack of personnel. Amalgamation is the only way for that territory to develop and in case of natural disaster happen, the rate of survivors will be higher in the amalgamated municipality, because of above reasons.

Decentralization process

The key point of implementing decentralization reform is to improve the wellbeing of local people. To make sure that the wellbeing of local people can be improved, decentralization brings local government some autonomy and power to manage its own territory. The second benefit, is that after decentralization, villages, towns and cities get the legal rights to form voluntary municipalities with other entities (villages, towns and cities), which as the result should improve the quality of public services, decrease the price for local people on this public services and due to combination of public infrastructure (after municipality is formed), the cost to manage those infrastructure should decrease and the efficiency of management is increased, because of higher human resources (municipalities have more experienced workers compared to villages or towns). Finally, local democracy is improved and people have more trust in local and central government.

Figure 1 illustrates the process of decentralization. Due to external environment, in most cases the overall demand of population, using local and central elections, people can demand from government to implement decentralization reform. Moreover, local central governments can also have Public Service Delivery Motives, Local Democratic Motives, Political Motives and Structural Motives that will make the government agree in implementing decentralization reform.

Villages, small towns and even cities may not have enough financial resources for providing public services. The implementation of the decentralization reform allows villages, towns and cities to form municipality, new governmental entity that combines all of its members financial resources. After municipality is formed, it has more financial resources than its separate member and this resource can be used by municipality to build new infrastructure (for example, build new water pipelines), which can improve the quality of the service and decrease the price of provision for municipalities (Swianiewicz, 2018; Drew et al., 2017).

Also, after municipality is formed, the local community become larger in size and its population. According to Suzuki & Sakuwa (2016), due to the increase of the

size of the community, local people have a higher motivation in attending local elections, which increase participation and as the result more people trust local government.

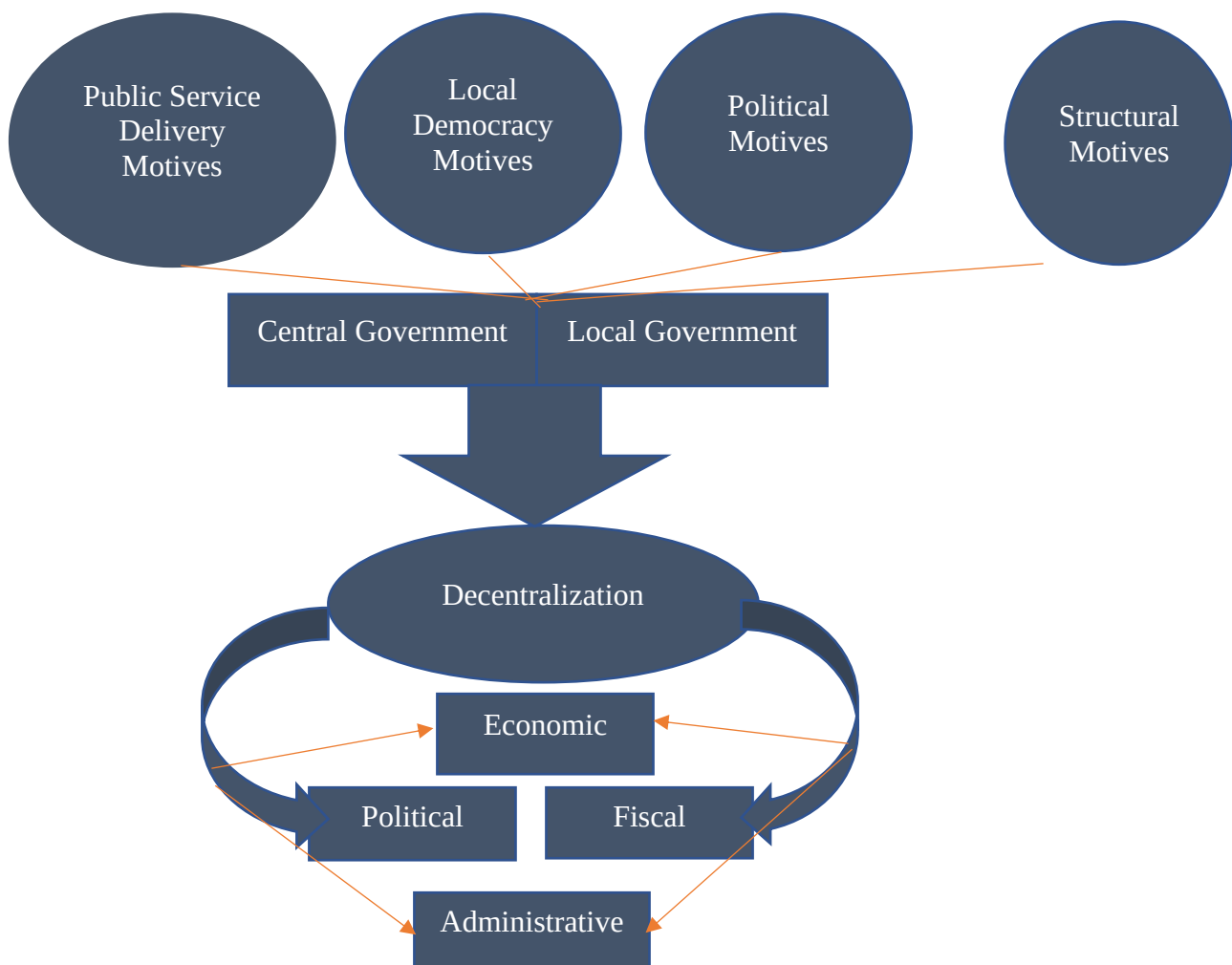


Figure 1 Decentralization Process

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Miyazaki (2018) also proved in his work, that the central government check more local government in providing public services, if the local community has higher population. For example, compare to an ordinary village, central government will pay more attention to municipality, because it has higher number of residents and if

something goes wrong, the local people will blame central government than the local government. So, central government has high interest in ensuring that municipalities have fulfilled their responsibilities in providing public services to local residence due to large number of local people.

Due to the above reasons, both central and local government have enough motives in implementation decentralization reform and after government chose in implementing this reform, it has to choose, which type of decentralization reform it will implement.

Using local and central deputies each political party can put pressure to implement the decentralization reform, that they think is better. For example, one of the party has a majority in central government, opposition parties can use local elections and governments as a platform to promote the vision of their reform. So, both sides will be heard and a compromise will be reached.

Clash of Central and Local governments in Ukraine

The main idea of the old institutionalism is to bring new ideas and new people to the institution, who can reform and bring changes, so their functionality and purpose is up to date with current demand. In works of Weber, it is shown that he believed that the only way for the institution survived and be stable, the new people and ideas are essential. On the other hand, starting from DiMaggio & Powell (1991), whose work brought foundation for new institutionalism, mention that “homogeneity of organizations” is the key factor to the stability of the whole institution. Instead of having different voices inside organization, that cause sabotage inside institution, it is better to keep the unity inside institution.

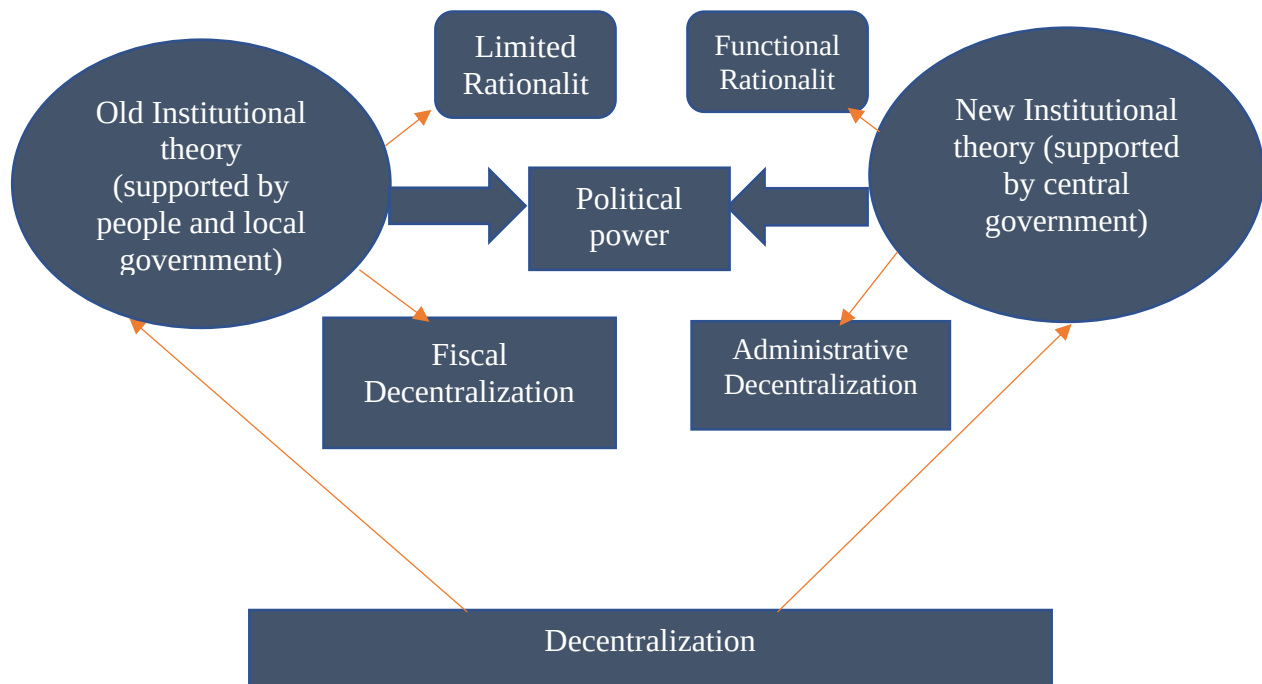


Figure 2 Clash of Central and Local governments

Figure 2 illustrates my analytical model and how my assumptions influenced the way of choosing the theory. In my research I am using the abductive approach and as a result after analyzing lots of official governmental statistics and reports, I made an assumption that the central government from the very beginning was not planning on giving real power to local municipalities.

The main crux of figure 2, is the way different parties understand and wish to have decentralization. The majority of Ukrainian people and local government view decentralization as the main tool to bring changes to the whole governmental system (limited rationality - change everything) and become equal or partners with the central government. To do so, Ukrainian municipalities need to be self-financed and thus the idea of fiscal decentralization is promoted by local government and residents.

On the other hand, as the empirical findings show, central government does not want to lose its power, but due to external environment, it had to implement decentralization reform. To keep political power and have less changes inside the system, central government wants to implement administrative decentralization, so people would be satisfied, and local government will have de jure political power (symbolism of decentralization). At the same time, by giving political power and less

financial means and central government wants to have financial power over amalgamated hromadas, so that central government can have power over local community and be in a relationship as the boss and local government is its subordinate.

Both sides, central and local governments want to have real power and thus political fights are happening over decentralization reform in both parliament and local communities about ways of its implementation.

Using Provincial government to control amalgamated hromadas, case of Beta AH

Deputy of Beta AH: “Everything started with L in 2018. L is a city of regional subordination and around the city – L-ke district. The authorities of the city and district belong to different political forces and, to put it mildly, are not friendly with each other. But in the subordination of the district there is the Central District Hospital, which served patients both from the city and from the district. But as a legal entity, the hospital was located in the city. Understand? So, 60% of the personal income tax from the salaries of doctors fell into the city budget (L) and the district didn't get anything. After opposition won in L city and started to lead and promote protests against central government, surprise, district leadership, screwed up by their party bosses, transferred the hospital actually to the paramedic station of the neighboring village.

60% share from personal income tax began to go to the budget of the village council. And from there – a reverse subvention to the central budget. So, the city budget immediately lost several million hryvnias”.

In Ukraine, if the local budget income (includes cities, towns, villages and amalgamated hromadas) index is higher than 3.000 hryvna on one person. If the index is higher than 3.000 hryvna on one living resident, than the sum of the current local income minus 3.000 hryvnva multiply by the number of residents = Difference and this difference is transferred to central budget. In L case, central government transferred legal residence of the city's hospital to the village, then the money that are used to financed hospital were transferred to the village and later those money was transferred

to central government's budget. So, as the result, L. city lost millions of hryvna and they (City L) still had to pay for the hospitals electricity, water, and its repairs cost, because village council did not use transferred money for those purposes because de facto hospital is located in L city.

Head of Beta AH: "Can you imagine? I was greatly surprised when I found that even our main theater was transferred to some Batsamethika village? Legally, of course... Pandora's box was opened in Beta's amalgamated hromada. In such a simple way, our hromada lost about 70 million in 2019 year and 83 million hryvnia in 2020".

According to deputy of Beta's amalgamated hromada, they (local government in Beta's AH) enormous pressure, because central government use provincial government as a tool to punish those amalgamated hromadas who "do not behave" or when the opposition party is a majority and to harm their reputation, president's party may use legal transfers of local property to other villages, towns or cities, so that those amalgamated hromadas will have less financial resources and later president's party will tell residents that it is the fault of local government.

Beta AH case shows that if opposition party dominates local community, Ukrainian central government (represented by presidential party) will use provincial government as a mean to decrease states budget transfers, so that local leaders would not have enough money to function normally and provide necessary public services. Later, central government (presidential party) will promote that it is the fault of local leaders and local resident should choose central government (presidential) party in next elections, to fix their problems. The case of Beta amalgamated hromada shows that the central government is ready to use its power in provincial government to keep their political power in local areas by making amalgamated hromada incapable, so that local people would blame local leaders and change them.

Conclusion

Using official governmental statistics from the website Decentralization, it was found that after the implementation of decentralization reform, the central government

added delegated responsibilities to local communities. After interviewing the Head of municipality, it was confirmed that those added delegated responsibilities are the main reason of Ukrainian municipalities financial dependance.

Local officials confirmed that if they were responsible for their own responsibilities that they had before decentralization reform, their amalgamated hromadas could fulfill them and be self-financed. Due to delegated responsibilities, which include the repair of public facilities, paying for their water, gas and electricity use and repairing infrastructure, most Ukrainian municipalities are unable to fulfill their responsibilities without state budget transfers and grants despite decentralization reform. It is especially hard to municipalities who are located on a periphery (more than 50 kilometers from cities with one million population), because entrepreneur, businesses and manufactures invest in those municipalities that are located near big cities.

We cannot claim that this dependance of municipalities was prearranged by the central government, but there is evidence that the central government uses its financial power to keep local municipalities ‘in check’ – keeping down local political opposition to central government’s decisions and actions (no criticism of central government, otherwise central budget transfers will be decreased) and increase political power of central government in municipalities by decreasing central budget transfers, so they would not be able to fulfill their responsibilities and in next local elections central government political party (presidential party) will be elected.