

IMPACT OF THE UKRAINIAN FINANCIAL CRISIS ON LOCAL SELF-GOVERNMENT FUNCTIONS

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Abstract. Since 2014, Ukraine has undergone a major decentralisation reform with the aim of strengthening local self-government, through the transfer of powers, responsibilities and fiscal resources from the central to the local level. However, the full-scale Russian invasion in 2022 has significantly disrupted this process. The ongoing war has caused severe financial instability across all levels of government and led to a functional and fiscal transformation of local self-government bodies. The present article examines the impact of Ukraine's financial crisis on the legal framework, functions and practical operations of local self-government bodies, focusing in particular on three areas: the shift in local functions during wartime, the impact of the financial crisis on local budgets, and the suspension of participatory budgeting and citizen engagement. The study is based on a combined legal and economic analysis, including national legislation and financial data. It is evident that local self-government bodies were obliged to adopt emergency roles, including humanitarian support and civil protection, despite the absence of explicit legal functions in these domains and inadequate financial resources. The crisis has also resulted in a considerable decline in own-source revenues and substantial reductions in interbudgetary transfers. Whilst legal provisions under martial law did indeed allow for a certain degree of flexibility, they also created risks for transparency, democratic accountability, and institutional overload. Notwithstanding the challenges faced, the article emphasises the resilience and adaptability demonstrated by local self-government bodies in Ukraine. The text calls for improved integration of legal safeguards and fiscal stability during periods of crisis, and argues for the urgent need to restore participatory tools during the post-war recovery phase. The findings contribute to broader discussions on decentralisation under the martial law, and offer policy recommendations for strengthening local self-government within the framework of Ukraine's European integration. By examining this critical period, the article provides insight into how local democracy can be protected and rebuilt in times of war and uncertainty.

Keywords: public administration, municipal government, local self-government bodies, public finance, decentralisation, financial decentralisation, good governance, economic sustainability.

JEL Classification: K30, K38

1. Introduction

Since 2014, Ukraine has made significant progress towards decentralisation and the empowerment of local self-government bodies. The country has initiated a comprehensive decentralisation reform initiative with the objective of transferring a greater share of authority (powers and functions), resources, and responsibilities from the central government to local self-government bodies.

This reform is based on the provisions of the 1996 Constitution of Ukraine, which establishes the principle of local self-government. Article 7 recognises local self-government as one of the foundations of Ukraine's constitutional order. Chapter XI of the 1996 Constitution also outlines the legal framework for local self-government, defining the powers of territorial communities (hromadas) and the status of local councils, their executive bodies, and local self-

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government officials. These constitutional provisions formed the legal basis for the decentralisation reforms initiated after 2014, and continue to be fundamental to Ukraine's initiatives in establishing effective and accountable local government bodies. In 2015 and subsequent years, there were numerous attempts to amend the Constitution to more clearly reflect the principles of decentralisation, subsidiarity and good governance. Nevertheless, these proposals were not adopted. Notwithstanding, it is important to note that the reform was relatively successful, particularly when compared to earlier municipal reform efforts in Ukraine, even without constitutional amendments.

A significant development was the consolidation of smaller hromadas into larger ones, accompanied by the election of councils and the delineation of clearer budgetary powers. Local self-government bodies (both representative and executive) were granted greater autonomy in areas such as education, healthcare, local infrastructure and land management. The implementation of budgetary reforms resulted in hromadas acquiring a more substantial proportion of personal income tax and direct state transfers, consequently enhancing their financial autonomy. These changes were supported by legal amendments to the Budget and Tax Codes and the Law of Ukraine "On Local Self-Government in Ukraine" (The Law of Ukraine "On Local Self-Government in Ukraine", 1997). The objective of the decentralisation reform was twofold: firstly, to enhance efficiency and local accountability, and secondly, to align Ukraine with European principles of subsidiarity and multi-level governance. The reform aimed to improve service delivery, strengthen democracy at the local level, and bring public administration closer to European standards.

However, the full-scale war that began in 2022 has placed extreme pressure on Ukraine's public finances, with severe consequences for local self-government. This article explores the influence of the financial crisis linked to the war on the functions and responsibilities of local self-government bodies in Ukraine. The examination encompasses three primary domains: firstly, the transition in local self-government functions during periods of crisis; secondly, the repercussions of armed conflict and the global financial crisis on local public finance; and thirdly, the suspension or transformation of participatory budgeting practices. This study will focus on the manner in which local self-government bodies have adapted during this period of uncertainty, and the potential impact of these changes on post-war recovery and European integration.

The present article aims to demonstrate how financial and institutional stress have transformed the functions, resources and legal framework of local

self-government in Ukraine. Furthermore, the study considers the potential risks to democratic accountability and citizen participation under the conditions of martial law.

The analysis is grounded in a comprehensive review of Ukrainian legislation and public financial data, complemented by selected case studies from Ukrainian cities and towns. This methodological approach facilitates the identification of legal developments and budgetary shifts, whilst also providing practical examples of how local self-government bodies in Ukraine have responded to crisis conditions.

2. Functional Transformation of Local Governments During Crisis

The full-scale Russian invasion of 2022 subjected the Ukrainian system of local self-government to an extreme stress test. This phenomenon was especially pronounced in light of the ongoing decentralisation reform (Mishyna, 2025, 151). Prior to the war, local self-government bodies were already responsible for a wide range of functions; however, the crisis resulted in a significant expansion of their competence.

During the early days of full-scale war, local self-government bodies in Ukraine suddenly found themselves required to act far beyond their traditional legal and administrative functions. As well as their usual responsibilities, they played a vital role in meeting urgent wartime needs, such as local logistics, civil protection, organising emergency shelters, and providing basic humanitarian aid. This was done without the relevant legal basis during the first days of the invasion. They used local budget resources as well as an increasing number of donations.

This shift in functions, and therefore competence, occurred amid extraordinary legal and institutional circumstances. Following the Russian invasion in February 2022, the President of Ukraine declared martial law across the country. Under this legal regime, the powers of public authorities at national and local levels were significantly expanded in order to enable an effective response to the military threat. This included suspending or restricting several constitutional rights, such as freedom of movement, access to information and the right to peaceful assembly. Elections, referendums, strikes and constitutional amendments are also prohibited by law during this period. As mentioned previously, the decentralisation reform has also been put on hold. In order to manage emergency governance, Ukraine introduced a new type of temporary authority in the form of military administrations. These institutions were established at the oblast and rayon levels across the country, operating in conjunction with the prevailing vertical structure of state power. This also affected the traditional local state executive bodies, namely the

local state administrations, which are regulated by the Law of Ukraine "On Local State Administrations" of April 9, 1999.

This transformation resulted in a functional reorganisation. In periods of peacetime, the primary function of Ukrainian bodies of local self-government was to oversee infrastructure, education, housing and social support in the settlements. However, during wartime, these organisations began to operate in a manner more akin to "emergency response" agencies. Local self-government bodies assumed responsibility for the management of evacuation routes, the distribution of food and medical supplies, the establishment of emergency shelters, and the provision of support to internally displaced persons (IDPs), and subsequently, returnees. While these were not customary functions under the Law of Ukraine "On Local Self-Government in Ukraine", they were rendered necessary by the extraordinary situation.

The pressure exerted by these new roles has exposed both the institutional resilience and vulnerability of the system. In the context of Ukraine, the decentralisation reform enacted between 2014 and 2020 resulted in the establishment of robust and adaptable local self-government entities. It was demonstrated that these provisions enabled hromadas to respond swiftly and adapt their services. However, a significant number of local self-government bodies also experienced administrative overload, unclear mandates and a lack of guidance or resources from the central (national) authorities. This tension highlights the difficult balance between legal flexibility and bureaucratic limits. In the contemporary era, international organisations, foreign governments and NGOs are providing support in this area, particularly with regard to material resources.

It is imperative to underscore the long-standing and foundational role financial considerations have played in the evolution of municipal law within the Ukrainian legal framework. Professor Batanov underlines, that "[i]n Ukraine, as in most post-Soviet countries, there is a persistent tendency to view municipal law as a complex legal field with a rather broad and often vague scope. It usually includes not only the fundamental aspects of organising and structuring local self-government bodies – such as their creation, election, and procedural functioning – but also elements from other legal sectors. In recent years, this has extended to cover areas such as municipal service (including career progression within local self-government), as well as municipal finance, property, and land use." (Batanov, 2024, 13) Consequently, financial issues pertaining to local self-government in Ukraine have historically been examined within the ambit of municipal and constitutional law, as opposed to financial or budgetary law.

From an economic perspective, the expansion of non-financial functions resulted in increased fiscal pressure on local budgets. Local self-government bodies were compelled to reallocate resources to unanticipated and pressing needs, frequently without supplementary financial assistance from the state (and the majority of them have initiated, and persisted in, the practice of donating to the Ukrainian Armed Forces). The crisis resulted in a challenge to the concept of balanced decentralisation, with hromadas being compelled to operate with reduced funding or sustainability guarantees. Legally, emergency powers were enabled by martial law, but often lacked specific legislation. While this did indeed grant local self-government bodies greater autonomy in their decision-making, the absence of clearly defined limits or safeguards gave rise to long-term risks. In the absence of adequate legal clarity, local decision-making processes may become less transparent and more challenging to oversee, even in the post-war context.

This situation lends further support to academic theories of "decentralisation under duress", which propose that local self-government bodies are empowered during national emergencies, but face increased risks of burnout, budget gaps, and democratic erosion. In the context of Ukraine, it is evident that this model evolved during a period of armed conflict, necessitating further examination to elucidate its intricacies.

3. Local Public Finance under Conditions of Decline

The financial crisis triggered by the full-scale war in Ukraine has had a substantial impact on the financial capacity of local self-government bodies.

In 2024, the OECD experts observed that in Ukraine, the composition of local budget revenues was as follows: more than 90% of the total revenue was derived from taxes and transfers. Consequently, when assessing the revenues of territorial communities, creditors should direct their attention to these communities. The largest share (67%) of tax revenues is personal income tax (PIT). Subsequently, the single tax (13%) and property tax (10%) are levied. The tax rates for residential and/or non-residential real estate are determined by the decision of the local council, depending on the area of the object, location (zoning) and types of such real estate objects, regardless of the cost of the object (OECD, 2022, 23).

This structural dependency on a limited set of revenue sources rendered local budgets in Ukraine especially susceptible to external shocks. As emphasised by the OECD in 2024 (see the aforementioned citation), over 90% of local revenues are derived from tax income and intergovernmental

transfers. The preeminence of the PIT, in conjunction with the single tax and property tax, signifies that any alteration in employment, business activity, or property use has a direct impact on local fiscal stability. Furthermore, the capacity of local councils to establish tax rates, particularly for property, had formerly been a catalyst for local fiscal autonomy. However, during wartime, this mechanism proved insufficient to compensate for widespread economic losses.

The OECD's analysis further emphasises the necessity of comprehending hromadas not merely as administrative entities, but as financial actors contingent on particular economic indicators. The decline in local revenues was precipitous, resulting from a combination of military actions, population movement, and structural damage. This situation necessitated an immediate realignment of financial planning and strategic support.

A significant challenge has been a considerable decrease in own-source revenues. The PIT, which had previously constituted a significant proportion of local budgets, decreased due to mass displacement, unemployment, and business closures. The large-scale internal displacement of millions of Ukrainians resulted in a significant alteration to the demographic and economic map of the country. Some hromadas, particularly those in frontline or temporarily occupied regions, lost a significant proportion of their working-age population. Consequently, their tax base shrank almost overnight as fewer residents were generating taxable income and local businesses were closing or relocating.

At the same time, "other hromadas, particularly in western and central Ukraine, experienced a sudden population increase as they became host communities for IDPs. While this led to greater pressure on local services and infrastructure, it did not immediately translate into higher revenues. IDPs are often unemployed or underemployed, and may not contribute to PIT in their host communities, especially if their place of official registration remains unchanged." (Makarets, Kavylin, 2024, 215) This discrepancy between legal and practical obligations has resulted in a misalignment between service responsibilities and available financial resources in numerous communities.

The result is a highly uneven fiscal landscape, where some hromadas face financial collapse due to population loss, while others struggle to meet rising costs with insufficient budget support. The confluence of these demographic shifts, in conjunction with the overarching economic downturn, persists in constituting a grave threat to the financial sustainability of local self-government bodies. Addressing this imbalance necessitates not only additional intergovernmental transfers but also legal reforms

to account for displaced populations in local budget planning.

In a similar fashion, collections of land tax declined, especially in regions where occupation or active military action was being undertaken. Concurrently, the prevailing economic downturn had a deleterious effect on other local taxes and fees, thereby weakening the financial autonomy that had been achieved during the decentralisation reform.

In response, local budgets were restructured. Funds were reallocated to support the military and humanitarian efforts, repair damaged infrastructure and provide essential services such as emergency housing, heating and medicine. Many hromadas also redirected their spending to support displaced persons and essential workers. However, these adjustments often entailed reducing investment in long-term development, education, and cultural programmes. The shift in budget priorities, while necessary, has increased fiscal stress at the subnational level even more (it was already high since 2000th, see Yakymchuk, 2012, 299) and raised concerns about the future capacity of local self-government bodies to resume regular service delivery after the war.

In this context, international donors have become a vital source of financial support. Many hromadas have received targeted aid in the form of donor-funded grants, humanitarian subsidies and recovery programmes. Thanks to the activity of the associations of local self-government bodies (as supported by the Law of Ukraine "On Associations of Local Self-Government Bodies"), and the co-operation of the hromada (as supported by the Law of Ukraine "On Co-operation of Hromadas"), a lot of help was distributed.

Furthermore, vertical fiscal relations with the central government have played a significant role. The legal framework governing interbudgetary transfers is still regulated by the Budget Code of Ukraine. However, in emergency situations, there is a necessity for more flexible mechanisms. While some local self-government bodies have successfully applied for state subventions, others have launched international partnerships or received assistance from sister cities abroad. While these financial survival strategies have helped to avoid collapse, they remain unsustainable without long-term planning and legal certainty. The volatility of local budgets during wartime highlights the need for clearer legal provisions on municipal borrowing and fiscal risk management after the war ends.

4. Participatory Budgeting and Public Involvement: From Practice to Pause

Prior to the outbreak of the full-scale war, Ukraine had made notable progress in promoting participatory democracy at the local level. One of the most visible

instruments of public participation was participatory budgeting, which was introduced in numerous hromadas as part of the decentralisation reform. These initiatives enabled residents to propose and vote on local projects, thereby providing citizens with a direct voice in the allocation of public funds. The practice of participatory budgeting was endorsed by both national guidelines and international donors, thus becoming a symbol of the country's efforts to build transparent, responsive, and inclusive local self-government.

Nevertheless, the war has resulted in the suspension of these processes in numerous hromadas. As financial and human resources were reallocated to emergency services, defence needs, and humanitarian aid, participatory budgeting initiatives were suspended or deprioritised. In certain instances, the infrastructure designed to facilitate public participation (for example, local council engagement units) has been either damaged or repurposed. In other cases, the legal and political environment under martial law restricted public assemblies and consultations, thereby making it difficult to maintain previous levels of civic engagement. While the suspensions were comprehensible in the given context, there is a risk that they could potentially erode the long-term culture of democratic participation.

This disruption has wider implications in the context of Ukraine's constitutional and legal development. As Baimuratov and Kofman (2022) have observed, the experience of municipal reform in EU Member States demonstrates that ensuring the capacity of hromadas is essential for facilitating meaningful interaction in the legal space of local self-government. In conditions of legal globalisation, this space is shaped not only by national law but also by international standards (Baimuratov, Kofman, 2022, 117). The success of Ukraine in aligning with European norms on local democracy is contingent not only on the resumption of participatory practices but also on the integration of public involvement into post-war recovery plans. A renewed focus on participatory budgeting has the potential to strengthen democratic resilience and support more inclusive local self-government in the reconstruction phase.

Notwithstanding the cessation of activity in numerous domains, certain settlements have endeavoured to sustain a modicum of civic discourse. In relatively safer regions, simplified or thematic participatory budgeting rounds were organised to address war-related needs, such as public shelters, emergency lighting, or youth engagement projects. Despite their limited scope, these local adaptations were instrumental in preserving a participatory culture and exemplified the adaptability of the model in crisis situations. It is important to note that civil society organisations have persisted in promoting the values of transparency and inclusion,

even in a digital or remote format. This demonstrates the resilience of democratic innovation.

The recovery planning process in Ukraine can benefit from the best practices observed in other European countries. For instance, in Poland, local self-government bodies have utilised participatory budgeting not solely as a financial instrument, but also as a means to integrate migrants and displaced persons into community life. In Portugal, certain municipalities have adopted a strategy of incorporating youth and marginalised groups into separate participatory tracks with the aim of enhancing equity. The findings of this study demonstrate that participatory budgeting can be reconceptualised in post-war "settings" to support social cohesion, rebuild trust, and foster inclusive reconstruction. It is submitted that Ukraine stands to benefit from such models, especially in hromadas receiving large numbers of IDPs and returnees, or planning large-scale redevelopment projects.

In the post-war context, the re-establishment of participatory budgeting will necessitate both legal support and political will. It is imperative that subsequent iterations of the Law of Ukraine "On Local Self-Government in Ukraine" and the Budget Code unequivocally advocate for citizen participation, not merely as a symbolic gesture but as an intrinsic element of local democracy. As suggested by N. Mishyna, "[t]he involvement of international donors and European institutions could also incentivise hromadas to reintroduce and expand participatory processes as part of broader reconstruction efforts" (Mishyna, 2025, 149). The integration of participatory budgeting into post-war governance structures in Ukraine has the potential to serve as a catalyst for the reaffirmation of the nation's commitment to democratic values and the promotion of citizen-centred recovery at the grassroots level.

5. Conclusions

The financial crisis triggered by the full-scale war in Ukraine has had a considerable impact on local self-government. The repercussions on both functional responsibilities and fiscal resources have been substantial. A shift in the traditional functions of local self-government bodies has been observed, often resulting in these entities acting as emergency responders without adequate legal or financial support. The decline in own-source revenues, the disruption to intergovernmental transfers and the suspension of participatory budgeting have created an uncertain and strained environment.

At the same time, local self-government bodies have shown great institutional resilience. Many adapted quickly, creating local solutions and continuing to provide essential services even in the most difficult conditions. These experiences offer valuable lessons

for the future. One key finding is that legal flexibility and financial safeguards need to be better integrated, particularly in emergency contexts. Another fundamental aspect pertains to the significance of promoting participatory and inclusive governance, even during periods of crisis. It is imperative that legal clarity be reinforced and that financial stability be provided for hromadas. This should become a policy priority at both national and international levels.

Furthermore, Ukraine's experience provides a more comprehensive understanding of the operational effectiveness of democratic institutions under pressure. While centralised decisions were necessary to coordinate national defence, the decentralised system proved crucial in maintaining day-to-day local self-government and citizen trust. The suspension of

participatory instruments, such as local budgeting, should be considered provisional, with the legal framework promoting their full reinstatement during peacetime.

In the aftermath of the war, local self-government bodies are poised to assume a pivotal role in the reconstruction process. The capacity to orchestrate reconstruction efforts, provide assistance to displaced populations, and advocate for democratic principles will be pivotal in shaping Ukraine's future. Ensuring that local self-government survives the crisis and emerges stronger, more closely aligned with the principles of European multi-level governance and democratic resilience requires strengthening legal clarity, restoring fiscal autonomy and reactivating public participation.

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