

REPORT

**LOCAL GOVERNMENTS'  
LEGAL, INSTITUTIONAL,  
AND FINANCIAL  
LANDSCAPE  
IN UKRAINE**

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The views expressed in this document reflect the authors' perspectives and  
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# LIST OF TERMS

CIT	Corporate income tax
DFI	Development financial institution
District	For Ukrainian “Rayon”
DMA	District (rayon) military administration
DREAM	Digital Restoration Ecosystem
ECU	Economic Code of Ukraine
EU	European Union
Hromada	Municipality (Territorial Community) as an administrative unit
IFI	International financial institution
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
LSG	Local self-government
LMA	Local military administrations
ME	Municipal enterprise
MNPE	Municipal non-profit enterprise
NDB	National Development Bank
NCSREPU	National commission for state regulation of energy and public utilities
PIT	Personal income tax
ProZorro	Electronic public procurement system in Ukraine
Region	For Ukrainian “Oblast”
RMA	Regional (oblast) military administration
SGEI	Services of general economic interest

# INTRODUCTION

This report provides a comprehensive analysis of the current state and operational environment of local governments in Ukraine. The structure of the report is designed to guide through the various facets of local governance, especially in the context of financial structure of municipalities (or ‘hromadas’).

The report begins with Section 1, which offers an overview of the regulations governing **local governments** in Ukraine. This section is crucial as it lays the foundation by detailing the general regulations and specific powers of local self-government executive bodies and local state administrations. It also explores the unique challenges and adaptations during wartime, including the establishment and functioning of local military administrations and the activities of utility companies, highlighting the classification, coordination, and support mechanisms for municipal enterprises.

Section 2 describes the types and activities of **municipal enterprises**. These are entities owned by hromadas that can perform public good (healthcare), municipal-specific (central heating, water supply, waste management, development, tourism) and general purpose (transportation) functions.

Section 3 delves into the financial structure and **budgets of municipalities**. It provides an in-depth analysis of general financial regulations, the sequence of expenditure execution during martial law, and the principles of mid-term financial planning. This section is important for understanding how local governments manage their finances, especially under the strain of martial law, ensuring fiscal responsibility and continuity of services. Also, this section assesses the financial resilience of municipalities in the current context. This section evaluates the adaptability and stability of local budgets, emphasising the variations in financial performance across different regions and the overall resilience demonstrated by local governments despite the challenges posed by the ongoing war.

Section 4 addresses the major **recovery and development needs** of municipalities, particularly those in regions affected by hostilities. It categorises these areas into territories of recovery and outlines the specific needs and strategic plans for their redevelopment. This section also introduces the DREAM platform, an innovative tool for managing recovery projects, and discusses various projects and funds available for recovery, illustrating the collaborative efforts between local governments and international bodies.

Section 5 focuses on the legislative regulation of **local borrowing and guarantees**. It explains the normative acts governing these financial mechanisms, highlighting recent legislative changes that expand borrowing rights to rural and settlement hromadas. This section is pivotal for understanding how local governments can leverage financial instruments to fund long-term infrastructure projects.

Section 6 elaborates on the procedures for implementing investment local-, state- and IFI-funded projects. It details the various funding sources, including local and reserve funds, co-financing, and international financial institutions. The section outlines the phases of project initiation and implementation, providing a clear roadmap for municipalities to secure and manage funding for development projects.

Section 7 explores **public procurement** implementation, with a specific focus on the ProZorro system. It describes the main participants, operational procedures, and categorisation of procurement items, ensuring transparency and efficiency in the procurement processes of local governments. Also, this section discusses the system of state control and audit, which is essential for maintaining accountability and ensuring that local governments adhere to legal and financial regulations.

In summary, this report systematically addresses the multifaceted aspects of local governance in Ukraine, providing a thorough understanding of the legal, financial, and operational landscape. Each section builds on the previous one, creating a coherent narrative that underscores the complexities and resilience of local governments amidst ongoing challenges.

The background is a dark teal color with a pattern of overlapping, slightly irregular circles. A diagonal line of these circles runs from the top right towards the center, creating a sense of depth and movement. The overall texture is dense and rhythmic.

**01**

**ARCHITECTURE  
OF LOCAL POWER  
IN UKRAINE**

## 1.1. POWER DISTRIBUTION

**Local self-government in Ukraine is carried out by territorial hromadas of villages, settlements, and cities through rural, settlement and city councils and their executive bodies**, as well as through district and regional councils representing their common interests. Councils are local self-government bodies representing the respective territorial communities and exercising, on their behalf and in their interests, the functions and powers of local self-government defined by laws.

**Unlike most EU countries where the community itself is a legal entity, in Ukraine, the local self-government body is the local council, and all executive bodies are separate entities.** According to the Law "[On Local Self-Government in Ukraine](#)", local government bodies make decisions on the establishment of executive bodies of councils with the status of legal entities of public law. The creation of an executive committee as a legal entity is not required. The executive committee is a collegial executive body of the council, which is established by the respective council for the term of its powers.

**The legislation does not limit the autonomy of local government bodies in forming the structure of the council's apparatus and its executive bodies**, determining their staff, as well as the number of such executive bodies. However, the existence of separate executive bodies — legal entities to exercise the powers of the local government body is directly defined by current legislation (for example, the local financial authority, the architectural authority, etc.). Regional and district councils are local self-government bodies representing the common interests of territorial communities of villages, settlements, and cities.

**Despite the principle of distribution of powers, in practice, there are still many duplications and intersections of powers between different levels of local and state authorities.** This is especially true in the case of delegated powers: social protection, public order, education, and culture. Imperfect legislative delimitation of powers for local government bodies and executive authorities not only leads to disputes and conflicts between these institutions but also significantly reduces the quality of public service delivery. It also leads to a decrease in the efficiency of budgetary funds utilisation due to the funding of duplicating functions of different levels of administration.

The main regulatory document governing the work of local self-government bodies and establishing the distribution of powers between management levels is the Law of Ukraine "[On Local Self-Government in Ukraine](#)". Fiscal activities are governed by the [Budget Code of Ukraine](#)<sup>1</sup>.

**Table 1. Levels of state and regional administration in Ukraine**

Level	Number of units	Representative (legislative) branch	Executive branch
Central	–	Parliament	Cabinet of Ministers of Ukraine and central executive authorities
Regional (oblast)	24 oblasts	Regional council (deputies are elected in general elections; the chairman is elected from among the deputies by their vote)	Regional state administration (during martial law — regional military administration).

<sup>1</sup> also available [in English](#), albeit with some delay on the latest changes



Level	Number of units	Representative (legislative) branch	Executive branch
			Headed by a chairman appointed by the decree of the President of Ukraine
Subregional (districts)	136 districts	District council (deputies are elected in general elections; the chairman is elected from among the deputies by their vote)	District state administration (during martial law - regional military administration)
Basic (territorial hromadas - village, settlement, and city councils)	1469 communities, of which 1438 are "active" before the invasion*	Village/ settlement /city council. The chairman is elected in general elections	Executive committee (during martial law — in certain communities — village/ settlement /city military administration)

\* The difference is due to the fact that with the decision approved by the Government in 2020, Ukraine formed 1469 territorial communities, of which 31 were located in the non-government-controlled territories of Donetsk and Luhansk regions on the day of the decision.

Source: KSE

**After the key stage of decentralisation reform in Ukraine (2015-2020), the administrative-territorial structure acquired its modern form.** The main changes were associated with the implementation of the subsidiarity principle. It means that those who provide the service should be as close as possible to those who receive it. This was most clearly manifested in changes to the budget system aimed at strengthening the financial self-sufficiency and accountability of local authorities at the basic level (territorial communities - village, settlement, and city councils). The main changes were as follows:

1. **Redistribution of powers:** the transfer of a significant portion of powers and financial resources from the central level of government to local self-government bodies. This enabled local communities to independently solve development issues and provide for the needs of their territories.
2. **Changes in budget structure:** the creation of a two-tier model of intergovernmental relations. All territorial communities entered into direct intergovernmental relations with the state budget (while the district level lost influence, scope of powers, and financial resources practically to zero<sup>2</sup>). Hromada budgets received a larger share of financial resources than were previously at the central and regional levels. This led to an increase in the financial autonomy of local authorities and their ability to effectively solve their own issues.
3. **Program-targeted budgeting principles:** practical application of the program-targeted budgeting method at all territorial hromadas, which allows budget resources to be targeted towards specific goals and tasks, promoting more effective use of financial resources.
4. **Medium-term (3 years) budget planning** became part of the budget process at the local level, ensuring stability and predictability of budgeting over an extended period. In 2022, after the full-scale invasion by Russia was suspended, it is being resumed this year. Accordingly, in 2024, local self-government bodies will adopt budgets for 2025 with forecasts for the next 2 years (2026-2027). This is significant for the use of

<sup>2</sup> District-level authorities have the right to manage money and other resources (land, real estate etc.) that are jointly owned by the communities within the district to satisfy common needs. However, due to changes in funding (most of the funds that used to fill the district budget now remain with the communities), district councils now lack the financial resources to function. As a result, these powers of the district councils are now merely nominal.

borrowing instruments by local councils, as they must, in any case, assess their ability to service debt. The current legislation does not explicitly require the preparation of a budget forecast aligned with the loan term for which the loan is granted. The forecast is prepared for the next two years as planned, while the loan may be taken out for a much longer period. At the same time, along with the package of documents submitted by the local government to the Ministry of Finance for loan approval, a local budget forecast for three years is also submitted.

**The areas that have remained exclusively at the state level** are legislative regulation, state control, defence, and foreign economic relations. The rest of powers have been transferred to local and regional levels in varying proportions:

- Socio-economic and cultural development, planning, and accounting;
- Budgeting, finance, and prices;
- Management of communal property;
- Housing and communal services, household, trade servicing, public catering, transportation, and communication;
- Construction;
- Education, healthcare, culture, physical education, and sports;
- Regulation of land relations and environmental protection;
- Social protection of the population;
- Foreign economic activity;
- Defence work;
- Resolution of administrative-territorial organisation issues;
- Ensuring legality, law and order, protection of rights, freedoms, and legitimate interests of citizens, and so on.

**Among the powers of local self-government bodies is the formation of their own apparatus of the local council.** The apparatus of the local council is an internal auxiliary body of the respective local council, consisting of officials, civil servants, and technical personnel, and performs functions of organisational, legal, informational, social, analytical, technical, and other support for the council activities. It does not belong to separate executive bodies and is not registered as a legal entity.

**Legislation does not define a Model Form of the organisational structure** of the council's apparatus and executive bodies, and the local self-government body independently forms it. Considering the provisions of the Law of Ukraine "On Local Self-Government in Ukraine" and other sectoral laws, each local self-government body exercises both its own and delegated powers.

**The structure of executive bodies and structural units of the council's apparatus will be formed individually according to the local specificities.** That's because the population size, area, economic, social, cultural, and geographical factors of each community are unique. For example, some communities will manage primary and secondary level medical facilities, while in others, there may be no healthcare facilities in communal ownership. Departments, administrations, and other executive bodies of the council are accountable to the council that formed them, subordinate to its executive committee, village, settlement, city head, or head of the district council in the city.

**Table 2. Powers of departments of the council's apparatus and separate executive bodies**

Departments of the council apparatus	Commentary on the functional purpose
Economic Development and Investment Department	Formation of development strategies, territory development forecasts, economic and social development programs, investment attraction, tourism, project management, grant attraction, regulatory policy, foreign economic activity, powers in the field of consumer, trade, service, catering, local markets, establishment of the operating hours of enterprises.
Department of Administrative Services	This department employs administrators and state registrars.
Department of organisational work and legal support	This department can provide economic support for the activities of local self-government bodies, record keeping and personnel work, and military registration
Department of accounting and reporting	The department's responsibilities include ensuring the council's accounting.
Finance Department	Preparation of the local budget, execution of local budgets, control over the expenditure of funds by budget funds managers, and other functions related to the management of local budget funds.
Department of Education	Ensuring the operation of secondary education institutions, preschool education institutions, and out-of-school education institutions.
Department of Social Protection and Health Care	Organises work related to the social protection of socially vulnerable citizens. Provides advice and assistance on pensions, insurance payments, social assistance, housing subsidies, benefits, compensation for care (social services), sanatorium and resort treatment, and other issues related to social support. Ensuring public access to medical services.
Department of Culture, Youth and Sports	Ensuring the operation of cultural institutions, libraries, art groups, sports education institutions, and implementing youth policy.
Service for Children	Ensuring the realisation of children's rights to life, health care, education, social protection, family upbringing and comprehensive development; identifying children in difficult life circumstances; taking measures to grant orphans the status of orphans and their placement.
Department of Housing and Communal Services and Improvement	The powers of this department include issues of municipal property, landscaping, transportation, ecology, civil defence, and security.
Department of Architecture, Spatial Planning and Land Resources	Organisation and implementation of land management, urban planning and architectural solutions. Ensuring the maintenance of urban planning cadastre at the local level.

Source: KSE

The responsibilities of local state administrations include<sup>3</sup>:

- Ensuring legality, protection of rights, freedoms, and legitimate interests of citizens;
- Socio-economic development of respective territories;
- Budget, finance, and accounting;
- Management of property, privatisation, promotion of entrepreneurship development, and implementation of state regulatory policy;
- Industry, agriculture, construction, transportation, and communication;
- Science, education, culture, healthcare, physical education, sports, family, women, youth, and minors;
- Land use, natural resources, environmental protection;
- Foreign economic activity;
- Defence work and mobilisation preparation;
- Social protection, employment of the population, labour, and wages.

**Local state administrations are prohibited from using objects of state property, property of territorial communities under their management, as collateral or other forms of security, as well as conducting operations of assignment of claims, debt transfer, debt assumption, donation, or charity.**

**Local state administrations exercise state control on the respective territories over<sup>4</sup>:**

1. Preservation and rational use of state property;
2. Financial discipline, accounting and reporting, execution of state contracts and obligations to the budget, proper and timely compensation for damage caused to the state;
3. Use and protection of land, forests, subsoil, water, atmospheric air, flora and fauna, and other natural resources;
4. Protection of historical and cultural monuments, preservation of housing stock;
5. Compliance by manufacturers of products with standards, technical conditions, and other requirements related to their quality and certification;
6. Compliance with sanitary and veterinary rules, collection, disposal, and burial of industrial, domestic, and other waste, compliance with beautification rules;
7. Compliance with trade, household, transport, communal services, consumer protection legislation;
8. Compliance with legislation on science, language, advertising, education, culture, healthcare, maternity and childhood, family, youth and minors, social protection of the population, physical culture, and sports;
9. Labour protection and timely and not lower than the state-determined minimum wage;
10. Maintenance of public order, rules for the technical operation of transport and road traffic;

<sup>3</sup> Article 13, Chapter III of the Law "On Local State Administrations"

<sup>4</sup> Article 16 of the Law "On Local State Administrations"

11. Compliance with legislation on state secrets and information;

12. Compliance with legislation on the National Archival Fund and archival institutions.

**Some of these items overlap with activities reserved for local governments indicated above.** This is due to the fact that certain state powers may be partially delegated to local governments. Decisions to delegate certain powers are made by the Verkhovna Rada of Ukraine. Accordingly, to ensure the exercise of these powers, it is envisaged that financial resources be transferred from the state budget to local budgets.

## 1.2. LOCAL POWER IN THE WARTIME

On February 24, 2022, in response to Russian aggression, the President of Ukraine [declared martial law](#). Under such conditions, **public authorities, military command, military administrations and local governments are granted all the powers necessary to avert the threat**. Accordingly, freedom of movement, pluralism of information, and some other human rights are restricted. Also, during the period of martial law, it was not possible to amend the [Constitution of Ukraine](#), hold elections, hold national and local referendums, or hold strikes, mass gatherings, and actions.

**Temporary state bodies (Military Administrations)<sup>5</sup> were created** to ensure the effective exercise of the powers granted and to repel the enemy. They are formed at the regional and district level in all regions and districts of Ukraine ["on the basis of"](#) the civilian vertical of state power at the local level (Region State Administration and District State Administration). The heads of pre-war District (Rayon) and Region (Oblast) administrations, by presidential decree, **acquire the status of heads of military administrations**. Local (hromada level) military administrations, according to the current legislation, are formed **instead of local self-government bodies** from military personnel, law enforcement agencies, and civil defence services. In other words, unlike district and regional administrations, the current heads of hromadas did not automatically become heads of city military administrations but could be appointed after appropriate checks<sup>6</sup>.

**Table 3. Military administrations**

	Municipality level (Hromada)	District (Rayon)	Region (Oblast)
Territory	On the territory of the relevant hromada	On the territory of the <b>District (Rayon)</b>	On the territory of the <b>Region (Oblast)</b>
Formed by	By decision of the President of Ukraine at the suggestion of regional state administrations and military leadership		

<sup>5</sup> Military administrations are temporary state bodies that operate for the period of martial law to ensure the operation of the Constitution and laws of Ukraine, to ensure, together with the military command, the implementation of measures of the legal regime of martial law, defence, civil protection, public safety and order, protection of the rights, freedoms, and legitimate interests of citizens. (Article 4, Article 8 of [Law No. 389](#))

<sup>6</sup> Law on the Legal Regime of Martial Law, Verkhovna Rada, [2015](#)

	Municipality level (Hromada)	District (Rayon)	Region (Oblast)
<b>Conditions for formation</b>	In case of failure of the village, settlement, city councils and/or their executive bodies and/or village, settlement, city heads to perform the functions assigned to them by the Constitution and laws of Ukraine "In other cases, provided for by this Law" (Ibid., Art. 4(3))	Formed in all regions	
<b>Composition</b>	Formed from military personnel, law enforcement officers and civil protection service	If a decision is made to establish <b>Region</b> and <b>District</b> military administrations, their status obtains <b>Region</b> and <b>District</b> state administrations, and the heads of state administrations become the heads of the respective military administrations.	
<b>Appointment of the head of the administration</b>	The head of the local military administration is appointed and dismissed by the President of Ukraine at the request of the General Staff or the <b>Region</b> Military Administration.  The head of the hromada local self-government, may be appointed (by President of Ukraine) as head of local the military administration in this hromada.	The heads of <b>Region</b> and <b>District</b> administrations are appointed by the President of Ukraine.	
<b>Accountability</b>	<b>District</b> and <b>Region</b> administrations	General Staff of the Ukrainian Armed Forces and <b>Region</b> administrations (on defence-related issues)  Cabinet of Ministers of Ukraine (on other issues)	General Staff of the Armed Forces of Ukraine (on the defence-related issues)  Cabinet of Ministers of Ukraine (on other issues)

Source: KSE Institute Center for Sociological Research Decentralization and Regional Development Report

**Before the full-scale invasion of Ukraine, there were military-civilian administrations (MCA), which can be called the prototype of military administrations.** They are governed by their own law<sup>7</sup> and can be **established by law only in the Donetsk and Luhansk regions**. In fact, this institute replaced local self-government in controlled territories (CHESNO Movement, [2023](#)) as a response to the challenges at that time, not to introduce martial law, not to stop the reforms, and at the same time ensure defence capability in the east (CPPR, [2023](#)).

**There is no clear legal distinction between the powers of local authorities and LMAs.** As a result, local authorities and LMAs [can duplicate](#) each other's powers in some hromadas. The law does not have clearly defined and prescribed indicators for assessing the ability of local government to perform its functions, which gives room for political manipulation and the creation of LMAs even instead of effective municipalities.

**The vertical subordination of administrations remained the usual.** Local military administrations are subordinate to district administrations, which, in turn, are subordinate to the General Staff of the Armed Forces of Ukraine, the District and Region state administration (for issues related to defence), and the Cabinet of Ministers of Ukraine (for other issues). The

<sup>7</sup> Law "On military-civilian administrations"

regional military administration is subordinate to the General Staff (on defence issues) and the Cabinet of Ministers of Ukraine (on other issues). In the context of changes in the governance structure, we can talk about the formalisation of interaction between these institutions.

**Martial law does not cancel local self-government bodies.** When the local military administration is created, the head of the Region Military Administration approves its structure. They register a separate legal entity, which is registered in the treasury as a body that manages the budget. The military administration exercises its powers during martial law and for another 30 days after its termination (after that, LMA gives all power and obligations to LSB of hromada). However, the formation of the military administration itself [does not stop the](#) city council as a legal entity. It does not terminate either utility companies, utility establishments, or utility establishments on the territory of the city.

**There is an exception though.** In addition to the powers provided for by the martial law, the Verkhovna Rada of Ukraine at the request of the President may make a decision on the exercise by the head of the military administration of the powers of the executive committee of local council and the mayor of hromada.<sup>8</sup> In this case council and mayors authorities are suspended due to 30 days after end of martial law.

In fact, there might be **two work formats of military administration**:

- The head of the military administration receives a **full list of powers of the city council and the executive committee**. That is, he has **all the power in the territory of the hromada**.
- When the administration is created, the local council and the mayor retain part of the powers of the executive committee.

The option of transferring the full scope of powers was approved by its Resolution of the Verkhovna Rada of Ukraine. According to our analysis, as of the time the study was published **19 such Resolutions, each of which expands the rights of several LMA chiefs**. The latter, according to the Parliament website, was issued [in August 2023](#).

**In this case, the activities of the local council members do not stop, but they are limited in their powers.** Thus, the local council does not assemble, sessions are not held, executive committees are not held, and **everything is decided by the chief of the local military administration alone**.

**In both cases, local borrowing is possible.** In the case of establishment of the military administration of a settlement<sup>9</sup>, the head of the military administration exercises the powers of the village, town, city council, its executive committee, village, town, city mayor. Accordingly, the head of the military administration makes a decision on borrowing and authorises the head of the financial local authority to conclude a loan agreement.

**In addition, in hromadas, where local self-government bodies have been retained, the powers of hromada heads have increased.** They now have the opportunity to make decisions on their own on issues that, in peacetime, are within the competence of collegial

<sup>8</sup> Article 10 of the Law "On the Legal Regime of Martial Law"

<sup>9</sup> Article 10 of the Law "On the Legal Regime of Martial Law"

bodies of local self-government<sup>10</sup>. With the mandatory notification of the head of the region's regional military administration within 24 hours, the head of the hromada "can make a decision exclusively for the implementation of the measures of the legal regime of martial law" *transfer of funds from the relevant local budget for the needs of the Armed Forces of Ukraine, release of communally owned land plots from illegally placed temporary structures, establishment of institutions for the provision of free primary legal assistance, appointment and dismissal of heads of such institutions, [sale of alcohol in the community](#) and [defined in changes to other powers](#).*

**But this decision did not give additional powers to the head of the administration in budget issues** because, anyway they remained within the competence of the local council. This means that the head of the hromada received the sole right to make some budget decisions, but technically the fact of making related budget expenditures will be possible only after amendments to the local budget, which remains the responsibility of the local council.

**The functioning of elected bodies at the regional level, such as district and regional councils and their interaction with district and regional military administrations under martial law was highly debated during the first months of the war.** However, with the adoption in May 2022 of the Law of Ukraine "On Amendments to Certain Laws of Ukraine on the Functioning of the Civil Service and Local Self-Government under Martial Law," the issue of the coexistence of district and regional councils was clarified (Verkhovna Rada, 2022). In particular, it was stated that if a district or regional council continues to operate, the establishment of the relevant military administration should not stop its work, but the council's powers will be limited to ensure that the administration fulfils its powers in accordance with Article 15(3) of the Law of Ukraine "On Local Self-Government" (Verkhovna Rada, [2015](#)).

**The functions of the district and region level de facto remained almost unchanged** from the controlling ones, although specific martial law-related responsibilities were added by law. Most Region Military Administrations did not even change the functions on [their official websites](#) from the previous versions of the Region State Administrations.

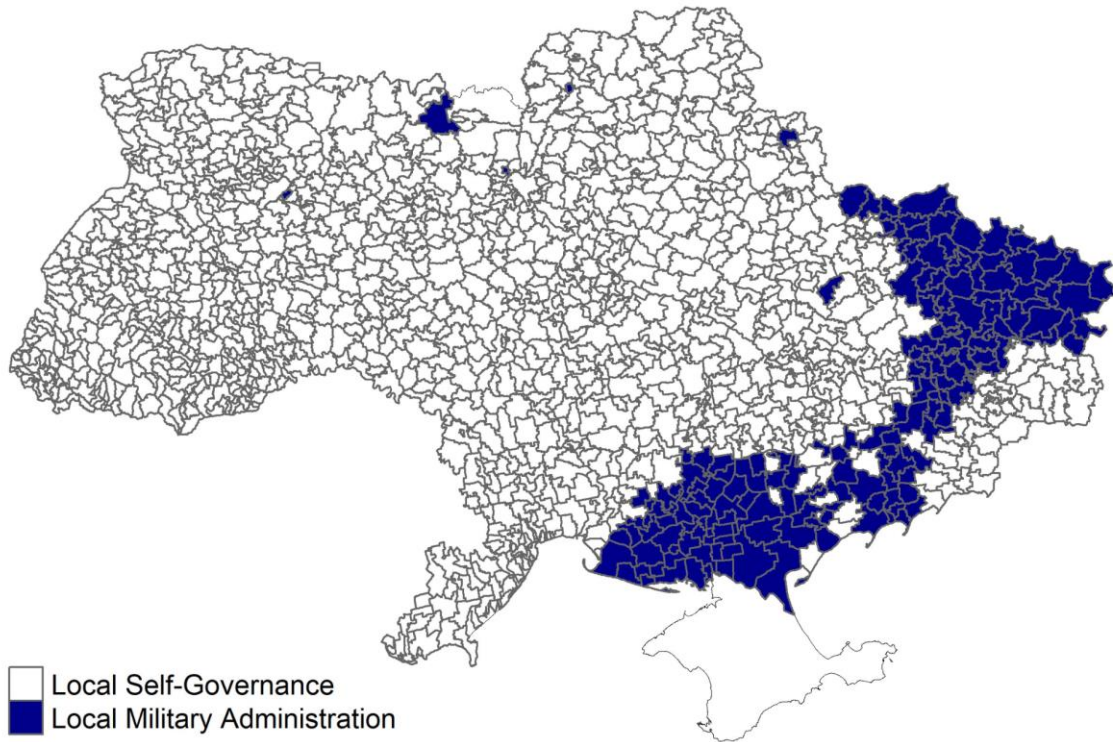
**Being temporary, the military administrations exercise their powers during the martial law period and 30 days after its termination or cancellation.** But even in this part, there are points that need to be legislatively regulated before the end of martial law. Currently, there are no rules on the resumption of the activities of local authorities and the procedure for transferring their powers back after the termination of martial law.

**Most often, military administrations of hromadas are created where the government is restored in the liberated territories** or to ensure governance in the temporarily occupied territories or territories where hostilities are taking place. As a result, most local military administrations appeared in Kherson (49), Zaporizhzhia (37), Donetsk (36), Luhansk and Kharkiv (26 each) regions(oblats), i.e. in relative proximity to the frontline. At the same time, the work of almost half of the military administrations is impossible due to the occupation of their hromadas. These administrations often operate in other cities on government-controlled territory. Only LMAs have been created in absolutely all hromadas in the Kherson region. In the Luhansk region, this number is at 70%, and in Zaporizhzhia and Donetsk, LMAs were created in 55% of hromadas. In total, LMAs were created on 13% of hromadas.

<sup>10</sup> [May 12, 2022 amendments to the Law of Ukraine "On the Legal Regime of Martial Law"](#)



Figure 1. Geography of LMAs created in Ukraine



Source: KSE Institute Center for Sociological Research Decentralization and Regional Development Data.

The background consists of several overlapping geometric shapes in shades of teal and black. A large, dark teal shape is in the top right, a black shape is in the top left, and a lighter teal shape is in the bottom right. A diagonal black band runs from the top left towards the bottom right, intersecting the other shapes.

**02**

**MUNICIPAL  
ENTERPRISES**

**An integral part of the activities of most hromadas is the functioning of municipal enterprises**, i.e. business entities owned by the local council. A municipal enterprise is a separate economic entity that has preferential rights to engage in commercial activities primarily aimed at generating profit. Municipal property is provided to such enterprises on the basis of economic management rights. Over the years, the number of municipal enterprises has continued to increase to an estimated 15,000 currently. They are mainly active in the healthcare, administration, utilities, and transport sectors. The information on these enterprises is scattered as they were never mapped.

**The head of such an enterprise has the authority to independently approve staffing schedules, open accounts in banking institutions, and make managerial decisions** within the scope of authority defined by the statute. Municipal enterprises have independent financial statements, and their accounts are not consolidated with the budgetary accounts of local self-government bodies.

**A municipal enterprise is not a budgetary institution but rather an economic entity of municipal ownership** that operates according to legislation<sup>11</sup>. Accordingly, the local self-government body does not provide direct and full financing for the activities (maintenance) of municipal enterprises. However, as the founder and owner, it bears responsibility for the consequences of the activities of the economic entity of municipal ownership.<sup>12</sup> For example, during the term of the local guarantee agreement, local councils make their own budget decisions for expenditures to fulfil guarantee obligations for payments due in the respective budget period. Such expenditures shall be provided for the guaranteed contracts under which the guarantee event has already occurred in the amount equal to the amount of payments under such contracts. Thus, if a ME goes bankrupt, the municipality take over the debt and becomes responsible for its repayment.

**The main forms of support for a municipal enterprise include:**

- additional contributions to the statutory capital
- repayable financial assistance
- design as the executor of the local program and recipient of budget funds in the network of the spending units responsible for implementing the budget program

**Exclusive powers of local councils include issues related to the creation, liquidation, reorganisation, and reprofiling of enterprises of communal ownership**<sup>13</sup>. When creating an enterprise, the council makes decisions regarding the size and form of the contribution to the enterprise's statutory fund. The source of replenishment of the statutory fund of a municipal enterprise is a special fund from the corresponding budget<sup>14</sup>. The specifics of the activities of municipal unitary enterprises, including the formation of the statutory fund and ownership of property, are regulated by Articles 78 and 78-1 of the ECU.

**If the statutory capital of a municipal enterprise is fully formed, current legislation allows for its increase** through additional contributions from budget funds, reserves, or non-current assets. The basis for increasing the statutory capital will be the decision of the local

<sup>11</sup> Economic Code of Ukraine (in particular, Chapter 7 of the ECU)

<sup>12</sup> Article 24, paragraph 5 of the ECU

<sup>13</sup> Article 26, paragraph 30 of the Law of Ukraine "On Local Self-Government"

<sup>14</sup> Paragraph 3 of Article 71 of the Economic Code of Ukraine (ECU)

council. However, before receiving additional contributions to the statutory capital from the budget, the municipal enterprise must submit a plan for the use of such funds to the State Treasury authorities<sup>15</sup>.

**The main source of replenishing the own capital of municipal enterprises is predominantly budgetary allocations, rather than net profit**, as it should be for enterprises operating in a competitive market. This means that **most municipal enterprises do not sustain themselves but are subsidised by local budgets. To ensure the financial sustainability of utility companies, including reimbursement of the difference in tariffs for households, the founders (local councils) adopt local support programs at the expense of the local budget.** This is characteristic not only for those enterprises unable to self-finance due to tariff constraints but also for municipal pharmacies, printing houses, markets, parking lots, television companies, and household services.

**Any loss of a ME should be covered by a budget.** A local government body sets tariffs for housing and utility services not lower than the costs of their production<sup>16</sup>. But if these regulated tariffs make it impossible to make a profit, the respective body is obliged to reimburse the difference between the tariffs and the costs from the relevant local budget to the contractor<sup>17</sup>. Therefore, to maintain the financial stability of enterprises providing public utilities, the local council may adopt a financial support program, including the allocation of funds to reimburse the difference in tariffs for the population from the local budget.

**Tariffs are established within the framework, and limits are determined by legislation**<sup>18</sup>. Setting tariffs for housing and communal services provided by enterprises jointly owned by territorial hromadas falls within the competence of district and regional councils<sup>19</sup>. For instance, tariffs for municipal electric transport services are regulated by the [Order of the Ministry of Infrastructure of Ukraine dated November 25, 2013, No. 940](#)<sup>20</sup>.

**Services of utilities are provided to consumers on contractual terms**<sup>21</sup>. A consumer must enter into contracts for the provision of housing and communal services. Prices (tariffs) are determined by agreement of the parties<sup>22</sup>, except in cases where prices (tariffs) are regulated by law. In such cases, prices (tariffs) are set by authorised state bodies or local self-government bodies in accordance with the law.

**Currently, the authority to establish tariffs for utilities' services lies with the National Commission for State Regulation of Energy and Public Utilities (NCSREPU) and local self-government bodies.** NCSREPU sets tariffs for communal services for natural monopoly entities and entities operating in adjacent markets, the activities of which it licenses. Local self-government bodies, in turn, establish tariffs for communal services for other enterprises that are not licensed by NCSREPU.

<sup>15</sup> Paragraph 10.1 of the Procedure for Treasury Servicing of Local Budgets, approved by the order of the Ministry of Finance of Ukraine dated August 25, 2012, No. 938.

<sup>16</sup> Article 10 of the Law of Ukraine "On Housing and Utility Services" and Article 15(1) of the Law of Ukraine "On Prices and Pricing",

<sup>17</sup> Part 1 of Article 15 of the Law of Ukraine "On Prices and Pricing"

<sup>18</sup> According to paragraph 2 of Article 28 of the [Law of Ukraine "On Local Self-Government in Ukraine"](#)

<sup>19</sup> Paragraph 37 of Article 43 of the [Law of Ukraine "On Local Self-Government in Ukraine"](#)

<sup>20</sup> The [Resolution of the Cabinet of Ministers of Ukraine dated April 3, 2019, No. 291](#)

<sup>21</sup> Law "On Housing and Communal Services"

<sup>22</sup> Article 10 of the Law "On Housing and Communal Services"

**The Government will start looking into the optimisation of municipal enterprises.**<sup>23</sup> Steps needed include mapping all MEs, measures to increase transparency in their transactions, and corporatisation strategies for all MEs that have a strong rationale for state ownership.

## 2.1. CLASSIFICATION OF MUNICIPAL ENTERPRISES

There are several types of municipal enterprises, depending on the role of municipal enterprises for local self-government bodies. They are categorised into those providing services of general economic interest (SGEI), enterprises performing specific functions of executive departments, and municipal enterprises operating in competitive markets.

**Enterprises providing SGEI ensure access to services that are a function of the municipality.** The list of such services is approved by the Cabinet of Ministers of Ukraine<sup>24</sup>. These services include:

- Supply of natural gas services
- Electricity supply services
- Utility services:
  - Centralised heating and thermal energy supply services
  - Centralised hot and cold water supply services
  - Centralised wastewater disposal services
  - Household waste collection and management services

Out of these categories, MEs typically fall within utilities. Other enterprises provide residents with services such as Public transport, Infrastructure related to the provision of public services, urban amenities, management of multi-apartment buildings, healthcare services, etc.

**Including these services in the list of services of general economic interest implies that their provision by companies of all ownership forms may not be sufficiently profitable without receiving state aid.** Therefore, regulation of this sector by various government bodies may be inconsistent and play a crucial role in this sector. This includes both the regulation of energy resource prices on one hand and the regulation of tariffs for utility services on the other. Local government body sets tariffs for housing and utility services in the amount not lower than the economically justified costs of their production. If a local government establishes tariffs for housing and communal services at a level that makes it impossible to make a profit, the body that approved them is obliged to reimburse the difference between the established tariffs and the economically justified costs of producing these services from the relevant local budget to the contractor. A utility company cannot independently decide

<sup>23</sup> According to the Ukraine Plan developed under the Ukraine Facility

<sup>24</sup> [Resolution on the Approval of the List of Services Constituting General Economic Interest](#)

whether to provide or refuse to provide services. Such decisions are made by the founder (local council) only.

Therefore, to maintain the financial stability of enterprises providing public utilities, the local council may adopt a financial support program, including the allocation of funds to reimburse the difference in tariffs for the population from the local budget. (Such expenditures are planned in the local budget for the planning year and in the forecast for the next 2 years). Tariffs de facto represent a political compromise between the enterprise, the management body, and the tariff-setting authority.

**Waste management constitutes a separate category.** Municipalities determine, through competitive bidding, the company responsible for solid household waste transportation, which can be either private or municipal<sup>25</sup>. This company independently collects waste and enters into contracts with landfills or waste incineration plants.

**Transport enterprises are typically not natural monopolies** (except for subways) and do not service all routes within a city. Tariffs for them are set separately from private carriers, and new transport vehicles are purchased using credit funds guaranteed by local authorities. A municipal guarantee is provided in each case. This should be reflected in the 3-year budget forecast.

**Most hospitals that were state institutions were transformed into municipal non-profit enterprises (MNPEs)** during the first stage of healthcare reform in 2018-2019. This was done to increase the autonomy of medical institutions and to transition them from budgetary funding to contracts with the National Health Service, the central executive authority.

**Municipal non-profit enterprises in other sectors do not have similar financial relationships with executive authorities.** A municipal non-profit enterprise is the same municipal enterprise formed from the separate property of a territorial hromada for the purpose of performing statutory functions but without the aim of making a profit. "Non-profit" does not mean that the enterprise cannot provide paid services or receive monetary receipts. The "non-profit" nature of the enterprise lies in the fact that monetary funds received from providing paid services or other sources are directed solely to the fulfilment of statutory tasks. In other words, profit can only be reinvested, not paid out to the city budget.

**There are also special purpose enterprises.** Various agencies (investment, tourism, etc.) may belong to municipal enterprises. These enterprises essentially function as separate executive departments of city councils, but they have freedom in choosing salary payment models, conducting economic activities, selling goods and services, etc. This helps because such municipal enterprises partially or fully cover their own expenses (related to performing local government functions) through commercial activities.

**At last, municipalities may have enterprises operating in competitive markets.** For example, companies provide services in telecommunications, security, property rental, construction and repair, trade, and various auxiliary services. The services of these enterprises do not have unique social value and can be procured through transparent auctions from private companies.

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<sup>25</sup> The Law on Housing and Communal Services

## 2.2. FUNCTIONING OF MUNICIPAL ENTERPRISES

**A hromada, as the owner of municipal enterprises, is represented by many bodies:**

1. The head of the hromada, who decides personnel matters and effectively directs the work of municipal enterprises, determines the strategy and main directions of work.
2. The city council's deputies approve the enterprise's charter, development program of the municipal enterprise, and investment program and may also increase the authorised capital.
3. Standing committees on budget and competitive/economic policy, communal property and the work of municipal enterprises, etc., which can be instruments of influence, as they have the right to provide recommendations and publish their findings on personnel and financial decisions.
4. The management body — a unit or unit of the executive bodies of the city council (oversees the operational activities of the enterprise).
5. The executive committee of the city council may influence and control the activities and financial planning of the municipal enterprise.

**As an owner, a municipality has a full set of powers over its enterprises.** For example, the mayor appoints and dismisses heads of both management bodies and directors of enterprises, institutions, and organisations belonging to the municipal property of the respective territorial hromadas<sup>26</sup>. The local council establishes the share of profit to be credited to the local budget for enterprises belonging to municipal property<sup>27</sup>. In most cases, the net profit remains in the company. If the council decides to allocate a part of the profit to the local budget, it approves a rather small part of it (up to 5%).

**Municipal enterprises also manage the property.** For strategic assets, economic management of assets is justified by the preservation of these assets in ownership, as well as the ability to have unrestricted access to them when necessary. Property in economic management cannot be pledged, provided as collateral, or arrested by its custodian (municipal enterprise). To obtain loans, an enterprise with fixed assets under economic management uses guarantee instruments. Transactions regarding the property of municipal enterprises are carried out by local councils on behalf of the hromadas.

**Central government affects the activities of municipal enterprises.** In particular, the Ministry for Communities, Territories and Infrastructure Development performs tasks such as:

- Facilitating the establishment of communal services by service providers and quality management systems managers based on national or international standards.
- Monitoring the status of payments for housing and communal services.
- Improvement of settlements.

<sup>26</sup> Article 42 of the Law on Local Self-Government

<sup>27</sup> Clause 30 of Article 26 of the Law On Local Self-Government in Ukraine

- Formulation of a unified technical, socio-economic policy in the field of drinking water, drinking water supply, and wastewater disposal.
- Coordinate the activities of local executive authorities in the field of waste management.
- Approving, within the scope of authority provided by law, the terms of competition for the lease or concession of objects in the areas of water supply, heat supply, and wastewater disposal, which are in communal ownership; heating schemes for settlements with a population of over 20,000 people and regional modernisation programs for heating systems, regional programs in the field of housing and communal services.

**Support for municipal enterprises can assume various forms.** Formal means include various channels of state support and assistance. Municipal enterprises are the largest group of recipients of state support and assistance, including funds from local budgets. For example, investments in the fixed assets of municipal companies may be included in local development programs, even if such services are procured through public procurement. Municipal enterprises also have the opportunity to lease premises from the hromada at preferential rental rates or free of charge or to receive equipment for their activities from the budget. Informal means include the commitment of budgetary institutions to cooperate with local municipal enterprises in certain markets (including telecommunications, repair, security services, and public catering services).

**Another form of support for municipal enterprises is the provision of local guarantees.** This instrument has not yet gained widespread use but is already being used by some hromadas, primarily in large cities. As of December 31, 2023, 31 hromadas have used local guarantees, and the total amount of guaranteed debt of territorial hromadas is 10.7 billion UAH. Please see Section 5.2 for more information.



The background is a vibrant teal color with a dynamic, circular brushstroke pattern that creates a sense of movement and depth. The strokes are thick and layered, radiating from the center towards the edges.

**03**

**LOCAL BUDGETS**

## 3.1. REVENUE STRUCTURE

**Budget revenues (for both state and local budgets) consist of taxes, non-tax revenues, and other receipts on a non-refundable basis** (including transfers, fees for administrative services, and own revenues of budgetary institutions). The revenues of local budgets are classified into the following sections:

1. **Tax revenues** (share of national taxes and local taxes and fees). In the structure of tax revenues of local budgets, the share of national taxes is 76.4% (the largest share is Personal Income Tax (PIT) - 67%), while local taxes and fees account for 23.6%.
2. **Non-tax revenues:**
  - i. Revenues from property and entrepreneurial activities (e.g., part of the net profit (income) of communal enterprises (*local councils make decisions that determine the share of profits that will be transferred to the local budget. In practice, this percentage is quite small, 3-10%*); fees for the placement of temporarily available funds of local budgets);
  - ii. Administrative fees and charges, revenues from non-commercial economic activities (e.g., fees for the provision of administrative services; revenues from rent payments for the use of property owned by the municipality). This applies to municipally owned premises or parts of them that are not used by the local council and are leased out (administrative buildings, cultural centres, libraries, etc.). The share of these revenues is 0.6%. They belong to own revenues of the general fund of the local budget;
  - iii. Other non-tax revenues (e.g., revenues from operations with loans and guarantees).
3. **Revenue from capital operations** includes income from the sale of capital assets (fixed assets, state reserves and reserves, land) (e.g., proceeds from the sale of land and intangible assets).
4. **Transfers** are funds received from other state authorities, local self-government bodies, other states, or international organisations on a gratuitous and non-refundable basis (e.g., basic subsidy, educational subvention).

**More than 90% of local budget revenues consist of tax revenues and transfers (see figure 2).** Therefore, when analysing the revenues of territorial communities, creditors should focus their attention on them.

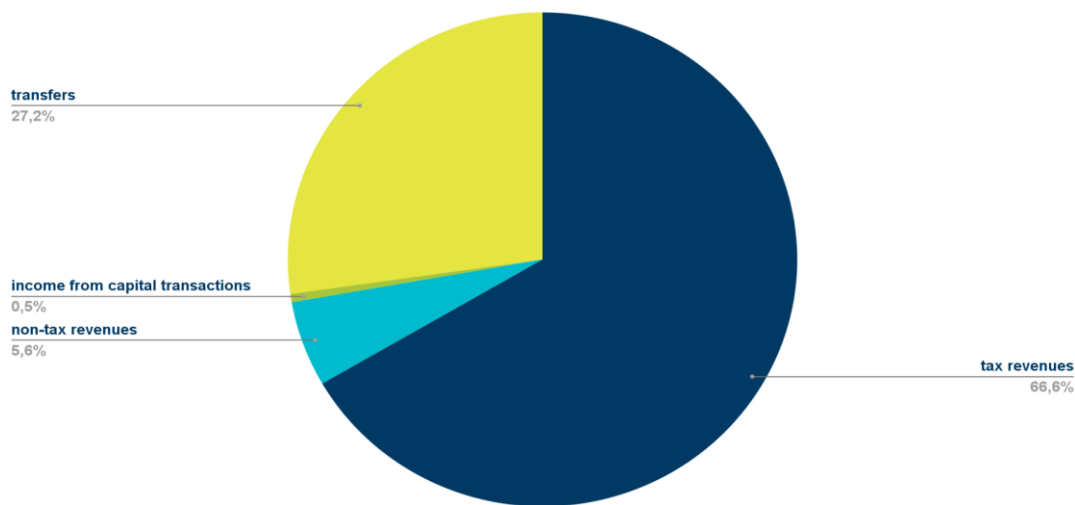
**The largest share (67%) of tax revenues is personal income tax (PIT).** Next, come the single tax (13%) and property tax (10%, tax rates for residential and/or non-residential real estate are determined by the decision of the local council depending on the area of the object, location (zoning) and types of such real estate objects, regardless of the cost of the object).

**The legal status of taxes varies.** The property tax and the single tax are local taxes and are fully credited to local budgets. However, PIT is a nationwide tax, and the state determines the distribution structure among the budgets of all levels. According to the Budget Code of Ukraine, the distribution structure is as follows: 60% is credited to hromadas budgets (with

the exception of 64% in the last three years), 15% to regional budgets, and the rest to the state budget.

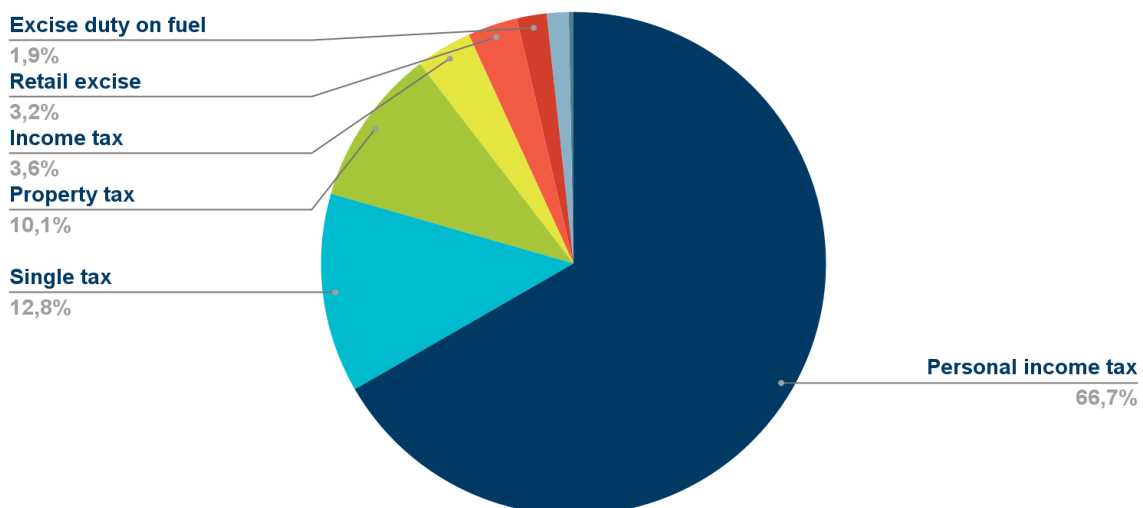
**The corporate income tax is almost entirely allocated to the state budget (90%), while the remaining 10% is allocated to regional budgets and the budget of Kyiv.** As for the budgets of territorial communities, only the corporate income tax and financial institution tax of communal ownership, founded by village, settlement, and city councils, are allocated to them. Since most of these enterprises are not profitable, the amount of revenue from this tax to local budgets is insignificant. In 2023, its share amounted to only 2.4% of all revenues to the general fund of local budgets.

**Figure 2. Structure of revenues of local budgets in 2023**



Source: Openbudget, KSE

**Figure 3. Composition of tax revenues to local budgets in 2023**



Source: Openbudget, KSE

**Transfers are divided into subsidies and subventions. Subventions have a specific purpose** and can only be used for the expenditures for which they are specifically designated (the largest share is occupied by the educational subvention — a subvention for delegated

powers from the state level, the funds from which are primarily used to pay teachers' salaries in schools). **Subsidies do not have a clear purpose** and can be used at the discretion of the local council, including servicing debt obligations (the basic subsidy occupies the largest share) (although there are exceptions and sometimes subsidies can also be limited in the options for use).

**Since transfers lie out of the scope of local powers, they are regulated by the central government.** The procedure and conditions for providing subsidies from the state budget to local budgets are determined by the Government no later than 30 days from the date of entry into force of the law on the state budget. The volume of intergovernmental transfers in the state budget is approved separately for each of the respective local budgets if there are grounds to provide and receive their respective types (Article 97 of the Budget Code). If the state provides tax incentives that reduce the revenues of local budgets, it simultaneously provides additional subsidies from the state budget to local budgets to compensate for the corresponding revenue losses of local budgets (Part 1 of Article 101 of the Budget Code) (although de facto, this regulation is often not fulfilled).

**After the implementation of the local self-government reform in Ukraine, all territorial hromadas received equal rights** regardless of their size and type (rural, town, city). Therefore, there are no separate procedures or financing peculiarities for small communities; they are the same as for large cities. The only significant difference is the size of budgets and, accordingly, different possibilities in terms of potential borrowing amounts.

**Another feature of Ukraine's budget system is that state and local budgets have two funds (two parts) in their structure:**

- General Fund. Its revenues are generated by tax revenues, administrative services, etc.
- Special Fund, which includes the development budget. A special fund is a component that includes budget revenues intended for specific activities and budget expenditures for the implementation of these activities, which are made at the expense of the relevant revenues. The local budget development budget is a plan for the formation and use of funds allocated for the implementation of socio-economic development programs related to investment and innovation activities.

## 3.2. MID-TERM BUDGET PLANNING

**Local budgets are approved for one calendar year**, followed by a forecast for the next two years. There is no direct link between the adoption of the local budget and the long-term servicing of loans. Accordingly, there are other instruments for planning for longer periods.

**For long-term financial planning, territorial communities adopt local targeted programs.** Such a program is a set of interrelated tasks and measures, coordinated by deadlines and resource provision with all involved performers, aimed at solving the most urgent development problems of the territorial community or individual sectors of the economy or socio-cultural sphere of the territorial community, the implementation of which is carried out using funds from the local budget and other attracted funds.

**Such programs can be implemented over several years.** Therefore, local targeted programs can be classified as forecasting and program documents that define goals, priorities, and measures necessary to achieve them.

**The approval of local targeted programs falls within the exclusive competence of village, town, and city councils** and is resolved at plenary sessions of the respective councils<sup>28</sup>. The implementation of measures of the targeted program may be carried out at the expense of the budget of the territorial community, regional budget, state budget, grant and borrowed funds, and other sources not prohibited by law. In order for all tasks defined in the local targeted program to receive funding, they must be included in the respective local budget.

**Another instrument of long-term planning is the community territorial strategy, developed for 5-7 years.** It is a long-term program that contains a set of goals for its development and outlines the directions and priorities of activities, as well as the allocation of financial resources necessary to achieve the defined goals within a certain time frame. In addition, the community strategy must correspond to the goals of state policy in the field of regional development and be coordinated with the "State Strategy for Regional Development" as well as the regional strategy.

### 3.3. LOCAL BUDGETS DURING THE WARTIME

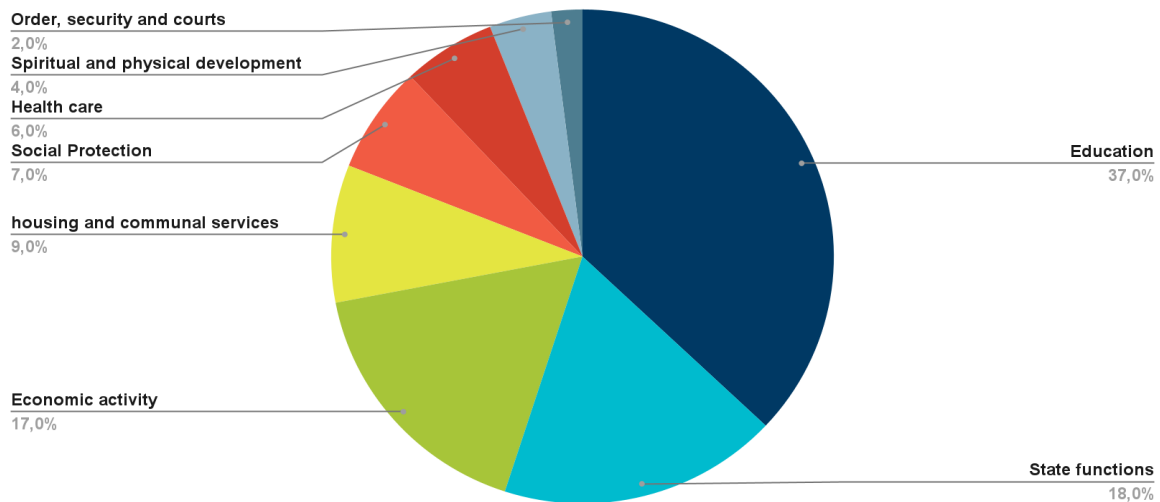
**Martial law changes the fiscal process.** Article 55 of the Budget Code regarding the implementation of protected expenditures (i.e., expenditures on salaries of employees of budgetary institutions; payment for communal services and energy resources; purchase of medicines, etc.) is not applied, although local councils must primarily take into account the need for these areas when planning budgets. The sequence of execution of payments by the Treasury authorities according to the orders of budgetary funds recipients during the period of martial law is determined by [Cabinet of Ministers Resolution No. 590](#). According to it:

- First priority - expenditures of managers (recipients) of budget funds attracted to solve tasks related to the introduction and implementation of measures of the legal regime of martial law.
- Second priority (equally important):
  - payment of salaries to employees of budgetary institutions;
  - social security;
  - **expenditures for repayment of local debt;**
  - **expenditures for servicing local debt;**
  - purchase of medicines and bandaging materials;
  - payment for communal services and energy resources.
- Third priority - capital and other expenditures.

<sup>28</sup> Paragraph 1 of part 22 of article 26 of the [Law of Ukraine "On Local Self-Government in Ukraine" dated May 21, 1997, No. 280/97-VR](#)

**Expenditures for the repayment and servicing of local debt have a high priority**, which positively affects the possibility of attracting credit funds and reduces the risks of their non-repayment.

**Figure 4. The structure of local budget expenditures in 2023**



Source: Openbudget, KSE

**In the expenditure structure, the largest share is expenditures on education (37%).** Next are expenditures to ensure the activities of local self-government bodies – mainly the salaries of local officials and the cost of maintaining administrative buildings (general state functions - 18%) and economic activity (significant part of this is the repair of local roads) - 17%.

**The share of capital expenditures has been increasing since 2018**, indicating an increase in funds allocated for the renewal of local infrastructure. Along with this, due to the increase in the price of energy resources, the share of expenditures on payment for communal services and energy resources has also increased.

**The year 2021 was favourable for local self-government** in terms of recovery after anti-COVID measures, with expenditures from the special fund in the structure of local budgets reaching almost 30%. **However, the war forced a reduction in such expenditures** to 12.9% in the structure of local budget revenues, and the share of capital expenditures in 2022 was only 10.2%. Instead, in 2023, the share of capital expenditures increased to 23.7%, which is the highest indicator in the entire history of local budgets in Ukraine. The share of wages remains high, worsening the flexibility of the expenditure structure of local budgets.

## 3.4. FINANCIAL RESILIENCE OF MUNICIPALITIES

**Analysis of local budget execution for 2023 shows a significant difference from 2022 in favour of growth.** Thus, the increase in revenues of the general fund, excluding transfers (essentially own revenues, mainly tax revenues) for local budgets for 2023 amounted to 11% compared to 2022. The growth in local budgets is due to an increase in revenues from personal income tax (+6.3%), single tax (+18.2%), excise tax (+63.3%), and property tax

(+19.1%). As was mentioned before, the significant role in the growth of local budget revenues was played by revenues from military personal income tax. This was particularly felt by those territorial communities where military units are located, as personal income tax in Ukraine is paid based on the registration location of the legal entity, not the employees.

**Moreover, when comparing 2023 with pre-war 2021, the increase in local budgets amounts to 25.5%, unlike the state budget with an increase of 13.9%.**

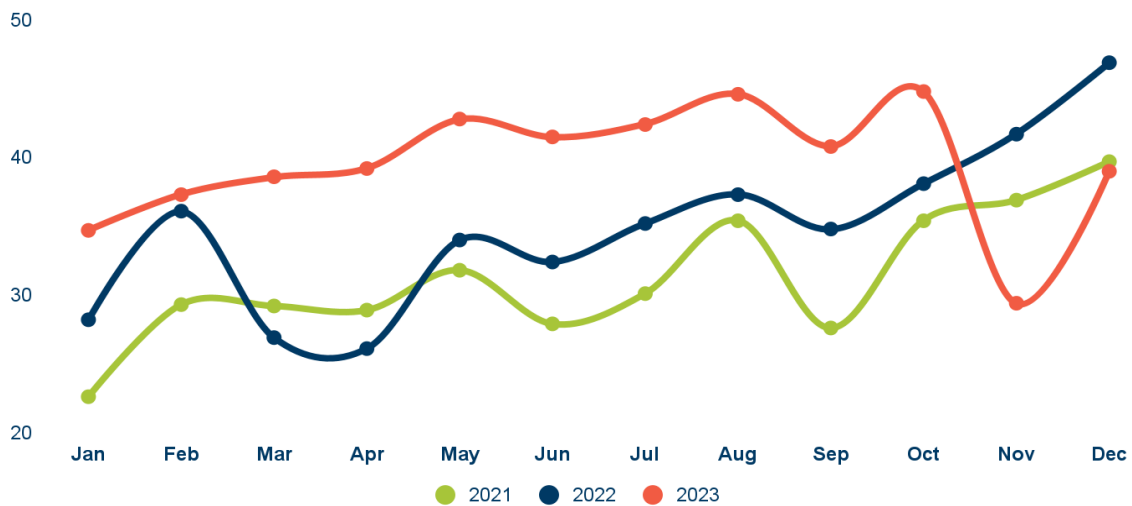
**If we consider the monthly dynamics of revenues to local budgets for the years 2021-2023, a significant decrease in revenues in 2022 is noticeable, starting from March due to the full-scale invasion, but in May, the indicators recovered above the pre-war level of 2021.** Hromadas demonstrated their resilience, financial autonomy, and stability in funding public services. Public administration at the local level and the execution of all powers (both own and delegated) were ensured by effective local management decisions through decentralisation. However, the recovery situation is quite uneven. The growth was mainly felt by rear hromadas, while front-line territories faced significant difficulties with the economy, budget, and, most importantly, people due to security risks and infrastructure destruction.

**The graph below also shows a significant recovery of revenues to local budgets in 2023 and a sharp decline at the end of the year** due to the withdrawal of military personal income tax, which was removed from October 1, 2023<sup>29</sup>. Thus, the withdrawal occurred in the previous month, so the revenues were adjusted in November 2023.

**Another issue is the exclusion of military personal income tax from local budgets in favour of the state budget.** During the first 10 months of 2023, 87.4 billion UAH were transferred from personal income tax withheld from military personnel to local budgets. It is 30% of all PITs in 2023. As a result, in the revenue structure for 2023, the share of personal income tax amounted to 44.3%, compared to 49% in 2022. These changes were introduced temporarily during the period of martial law. After the end of martial law, the military personal income tax will return to local budgets, but its share will not be as significant as it is now. This is because of the significant increase in the number of military personnel and their payments, the amount of military personal income tax in 2023 increased 8 times (from 12 billion UAH in 2021 to 96 billion UAH in 2023). However, this indicator will not affect the amount of potential borrowing, as personal income tax is completely excluded from the calculation of the amount for loans and the provision of local guarantees.

<sup>29</sup> The Law of November 8, 2023, No. 3428-IX "On Amendments to the Budget Code of Ukraine to Ensure Support for the Defense Capability of the State and the Development of the Defense Industry Complex of Ukraine"

**Figure 5. Monthly dynamics of local budget revenues in 2021-2023 (billion UAH)**

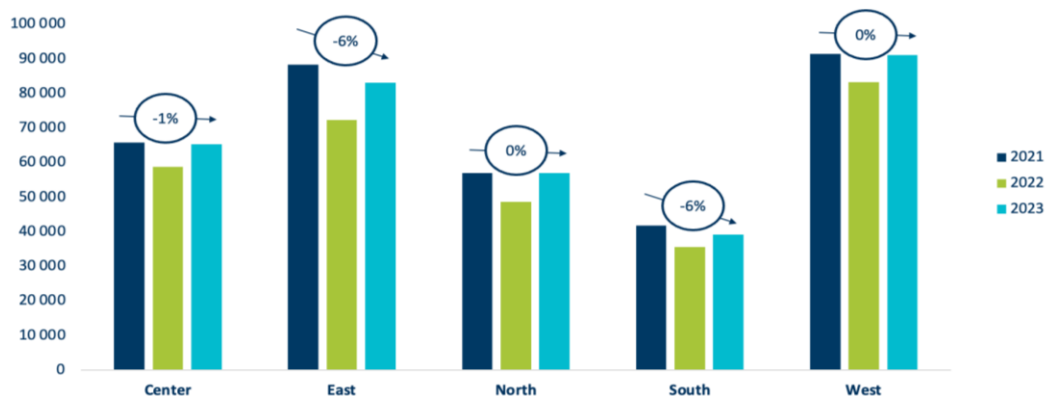


Source: [Decentralisation Portal](#)

**Figures 6-14 provide detailed information on budget revenues of hromadas**, excluding hromadas that were occupied, or partially occupied after 24th of February 2022 and have this status as of [April 2024](#).

**The total income of hromadas adjusted for CPI declined by 3% in 2023 compared to the year 2021.** The biggest contribution to the general decline was made by hromadas from the East and South. There was a fall in total income by 6% in each region. From the oblast level of perspective, the most significant decrease faced local hromadas Kherson (-33%), Kharkiv (-13%), Ternopil (-12%), Donetsk (-11%), Zaporizhzhia and Sumy oblasts (both -9%). Also, a significant decline faced the Luhansk oblast, but it is not reflected here, since as of April 2024, it is almost fully occupied by Russia. At the same time, Zhytomyr (+8%) and Kirovohrad (+6%) have significantly increased their total income since 2021.

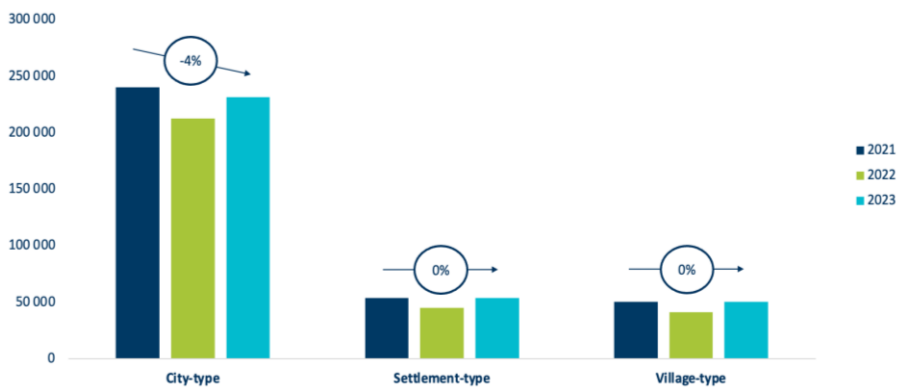
**Figure 6. Total income: CPI adjusted (million UAH)**



Source: [Openbudget](#), [KSE](#)



**Figure 7. Total income: CPI adjusted (million UAH)**

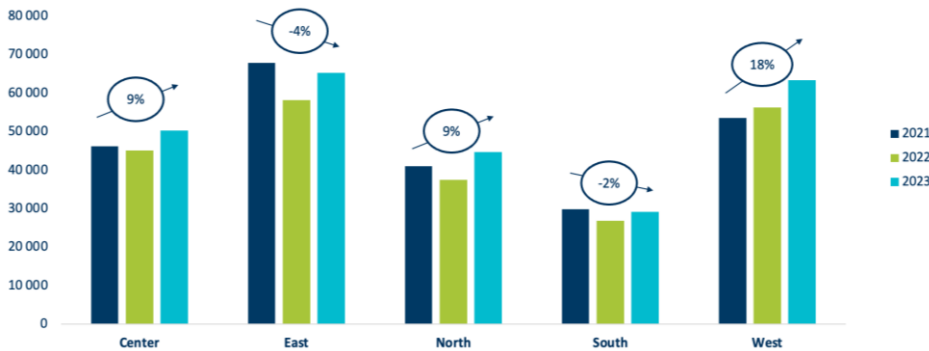


Source: Openbudget, KSE

**Own income (income that excludes subventions) in 2023 increased by 3%.** Hromadas in the East (-4%) and South (-2%) decreased their own incomes. In other regions, there was a different effect. In the Center (+9%), North (+9%), and West (+18%), own income volumes increased since 2021. Among oblasts, the most negative results were among Kherson (-50%), Kharkiv (-21%), Zaporizhzhia (-9%) and Donetsk (-5%) oblasts.

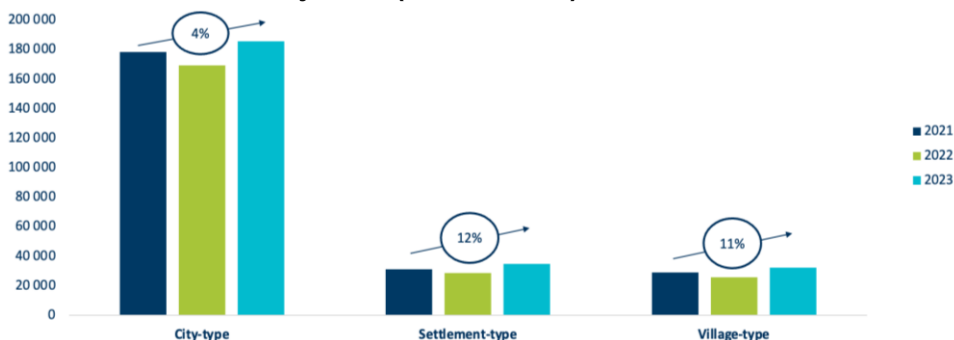
**The most significant decrease in the total income at the hromada-type level was among urban-type hromadas,** where the decline made up 4% in 2023 in comparison to 2021. In the settlement-type hromadas and village-type, there have been no significant changes since 2021. In terms of own income, urban-type hromadas exhibited a slight decline (-1%) in comparison to settlement-type (+3%) and village-type (+6%) in 2023.

**Figure 8. Own income: CPI adjusted (million UAH)**



Source: Openbudget, KSE

**Figure 9. Own income: CPI adjusted (million UAH)**



Source: Openbudget, KSE

**Examining the proportion of one's own income to the total income provides insights into a hromada's capacity to generate fiscal inflows** from diverse tax streams, fees, and other non-central government transfers. These metrics offer perspectives on the hromada's self-reliance and vulnerabilities stemming from reliance on state funding. Additionally, this measure acts as a gauge of the effectiveness of economic decentralisation within hromadas, showcasing efforts to retain greater economic autonomy at the local community level.

**On average, one's own income makes up 75% of the total income of hromadas in 2023**, which is more than in 2021, when it was 69%. However, its' share varies depending on the hromada type. In urban-type hromadas it is the highest, reaching 80% in 2023, increasing by 6% in comparison to 2021. In settlement-type communities, it is 65%, which is 7% more than in 2021. In the village-type hromadas, the income share of total incomes is the lowest, making up 54%, with an increase of 6% since 2021.

**Figure 10. Income Own: CPI adjusted (%)**

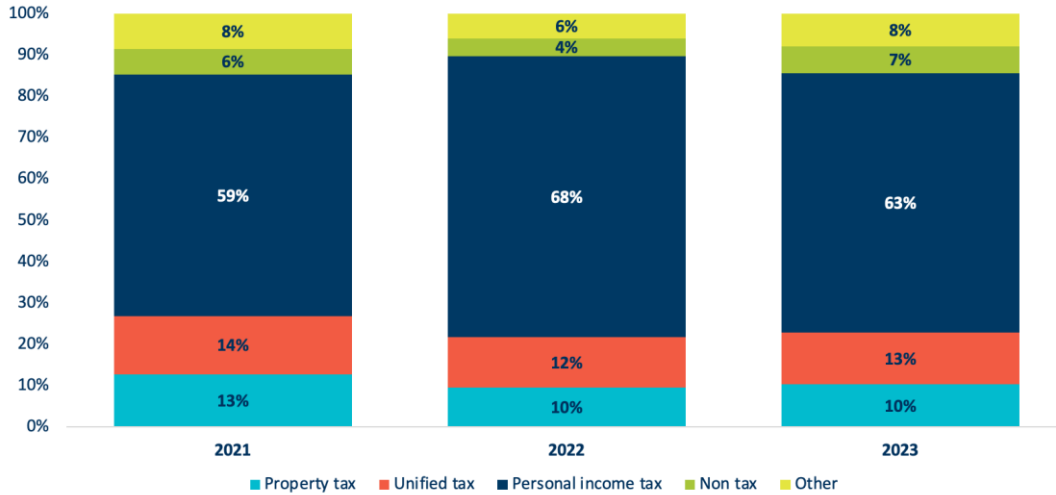


Source: Openbudget, KSE

**In terms of own income structure, the highest contribution is made up of personal tax income – 61%.** This is 4% more than it was in 2021. The important note is that the distribution of personal income tax in Ukraine hinges on enterprise registration rather than their specific physical location, thus making the own income indicator a proxy for hromada governance. It also serves as an incentive for businesses to register within the specific hromada and fulfil their tax obligations there. Other significant sources of own income in 2023 were single tax (13%), property tax (11%), and non-tax income (7%, income from property and business activity; administrative fees and payments, income from non-commercial and side sales; income from fines and financial sanctions; other non-tax revenues). Other sources of income contribute to the remaining 8% of their own income.

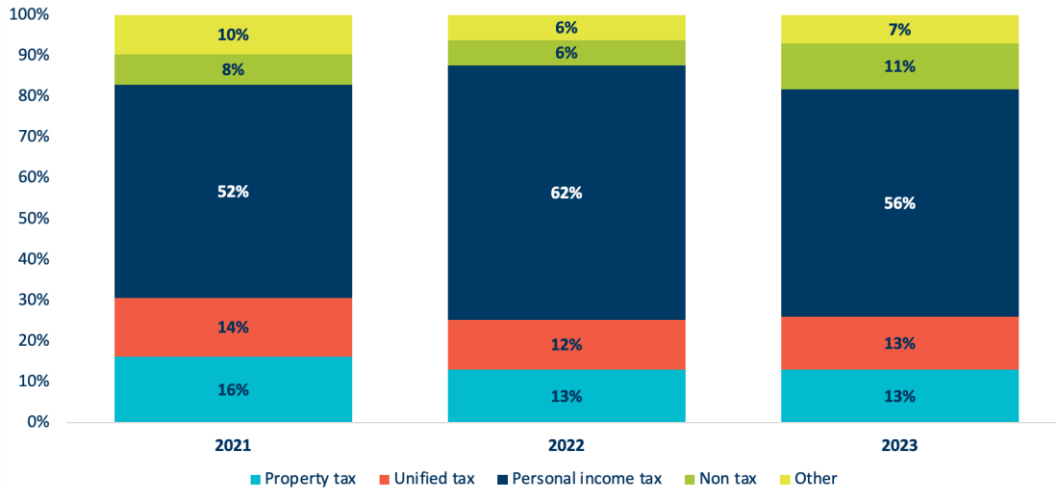
**The structure of the income among different types of hromadas varies.** In the city-type hromadas, personal income tax increased from 59% in 2021 to 63% in 2023. The unified tax share declined to 13% in 2023 from 14%, property tax declined from 13% to 10%, and non-tax incomes increased from 6% to 7%. In the settlement-type hromadas, personal tax income shares also increased in 2023 from 52% to 56%, unified tax income slightly decreased from 14% to 13%, property tax decreased from 16% to 13%, and non-tax income increased to 11% from 8% in 2021. Village-type hromadas also exhibited similar patterns in their own income structure over the years: personal tax income has the largest share with an increase to 55% in 2023 from 49% in 2021, unified tax share decreased from 14% to 12%, property tax decreased from 18% to 15% and non-tax income share almost doubled from 6% in 2021 to 8% in 2023.

**Figure 11. Own Income structure CPI adjusted: City-type (%)**



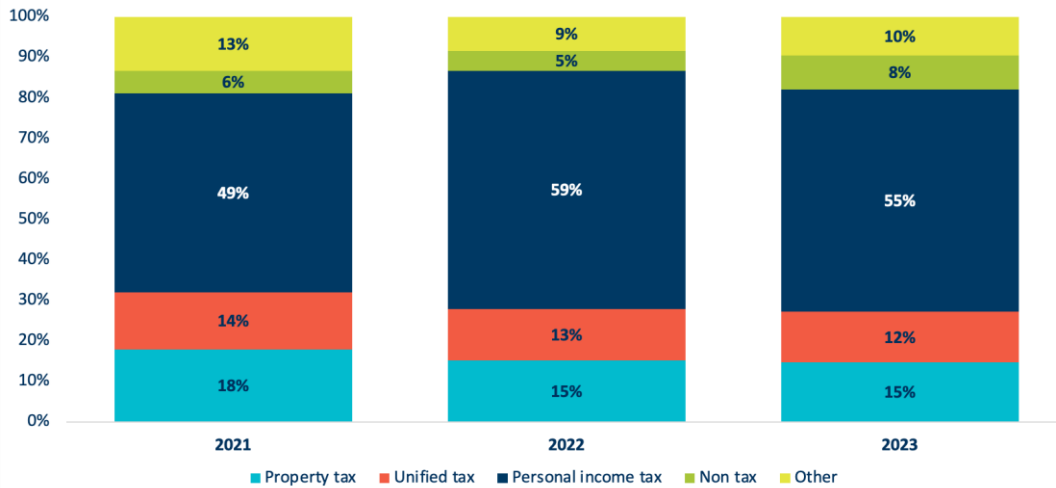
Source: Openbudget, KSE

**Figure 12. Own Income structure CPI adjusted: Settlement-type (%)**



Source: Openbudget, KSE

**Figure 13. Own Income structure CPI adjusted: Village-type (%)**



Source: Openbudget, KSE

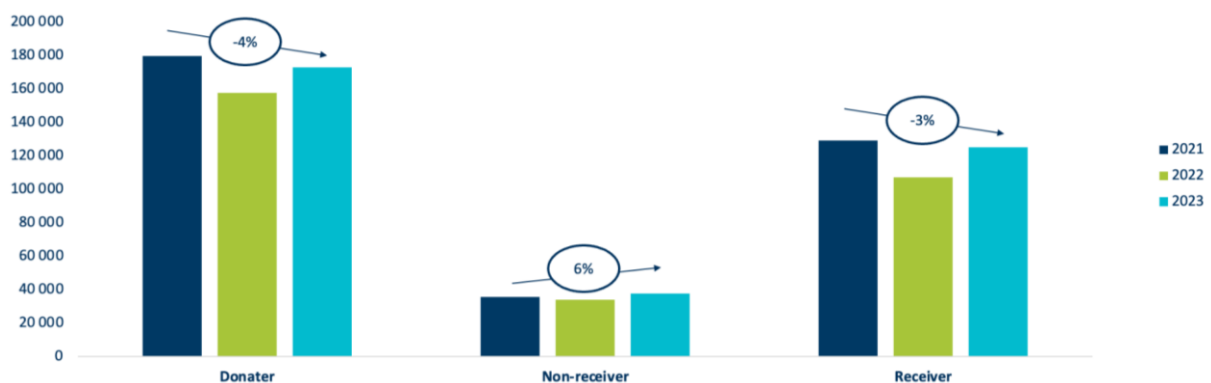
A mechanism known as "horizontal equalisation" is employed to assist hromadas with lower incomes. This involves redistributing resources from wealthier hromadas (reverse subsidy) to poorer ones (basic subsidy). The fiscal capacity index of the respective budget is considered to determine this redistribution. The fiscal capacity index is the ratio of the average Ukrainian personal income tax per person to the amount of personal income tax per person in the hromada.

Hromadas, with a fiscal capacity index ranging from 0.9 to 1.1, neither contribute to the state nor receive any budgetary allocations. When the index surpasses 1.1, the state levies half of the excess amount compared to the average personal income tax collection across all local self-government budgets in Ukraine (excluding Kyiv and Sevastopol) on a per capita basis. For hromadas with an index below 0.9, the state offers subsidies. These communities receive a basic subsidy equivalent to 80% of the shortfall required to reach the desired fiscal threshold. This subsidy isn't a full reimbursement of the deficit compared to the national average but rather covers only 80% of the required funds.

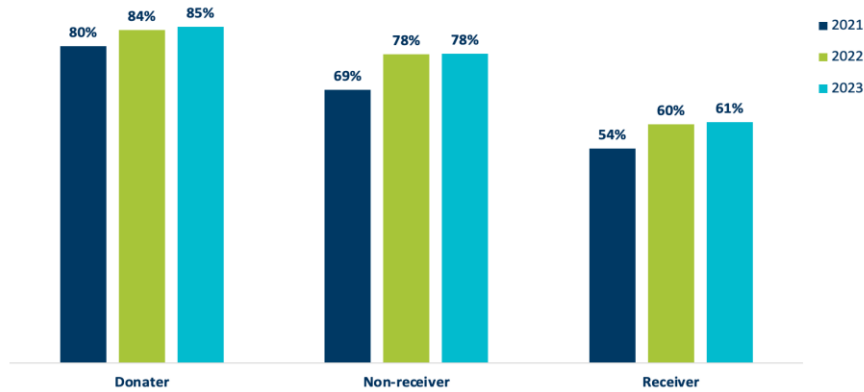
Since 2021, donator hromadas (those whose excess amount is levied by the central government) have decreased their total income by 4%. Non-receiver hromadas, on the contrary, have increased their total revenue in 2023 in comparison to 2021 by 6%. Receiver hromadas have suffered a decline of 3% in their total income in 2023. In terms of own income, the situation resembles the one with the total revenue. In donator hromadas, own revenue increased by 2% in 2023 in comparison to 2021. Non-receiver hromadas have significantly increased it by 20%. Receiver hromadas own income increased by 9%. In terms of the proportion of income that owns contributed to the total revenue, both donator and non-receiver hromadas increased their share to 85% and 78%, respectively, in 2023. Receiver hromada's share of own income is 5% bigger than in 2021.

The monthly dynamics of general fund revenues in 2023 compared to 2022 reflects a resumption of growth in the first months of 2023, compared to the difficult period of the beginning of the full-scale Russian invasion, which is why the increase in March-April is high. Instead, the removal of military PIT had a negative impact on the dynamics at the end of the year.

Figure 14. Total income: CPI adjusted (million UAH)



Source: Openbudget, KSE

**Figure 15. Own Income (%)**

Source: Openbudget, KSE

**The situation in individual hromadas varies significantly and requires an immediate response.** However, hromadas have shown that they are able to effectively manage and increase the financial resources they receive, respond adequately to unforeseen challenges, ensure a high level of service delivery in any environment, and quickly adapt to new conditions. Hromadas have shown that local government budgets form the basis for the sustainability of local financial resources.



**04**

**RECOVERY AND  
DEVELOPMENT NEEDS  
OF MUNICIPALITIES**

**The third Rapid Damage and Needs Assessment (RDNA3) estimated that the direct damages due to the war of aggression amounted to around EUR 138.2 billion.** The total reconstruction and recovery needs are EUR 440.5 billion. Housing, transport, energy, commerce, and industry are the most affected sectors. The scale of destruction continues to increase. According to the Ukraine Plan, the effective coordination of recovery processes in Ukraine requires a clear definition of the powers and responsibilities of various authorities and institutions of Ukraine in the process of reconstruction.

**Effective coordination of recovery processes in Ukraine necessitates a clear definition of the powers and responsibilities of Ukrainian authorities and institutions** involved in reconstruction, recovery, and modernisation. This includes cooperation with international partners, establishing key principles, procedures, and a financial framework for reconstruction, recovery, modernisation, and economic growth.

**Given the scope of the restoration projects, a unified project pipeline should be established.** An effective starting point would be creating a cohesive architecture of planning documents within a multi-level public administration system, addressing wartime priorities and establishing a well-defined framework for post-war recovery and development.

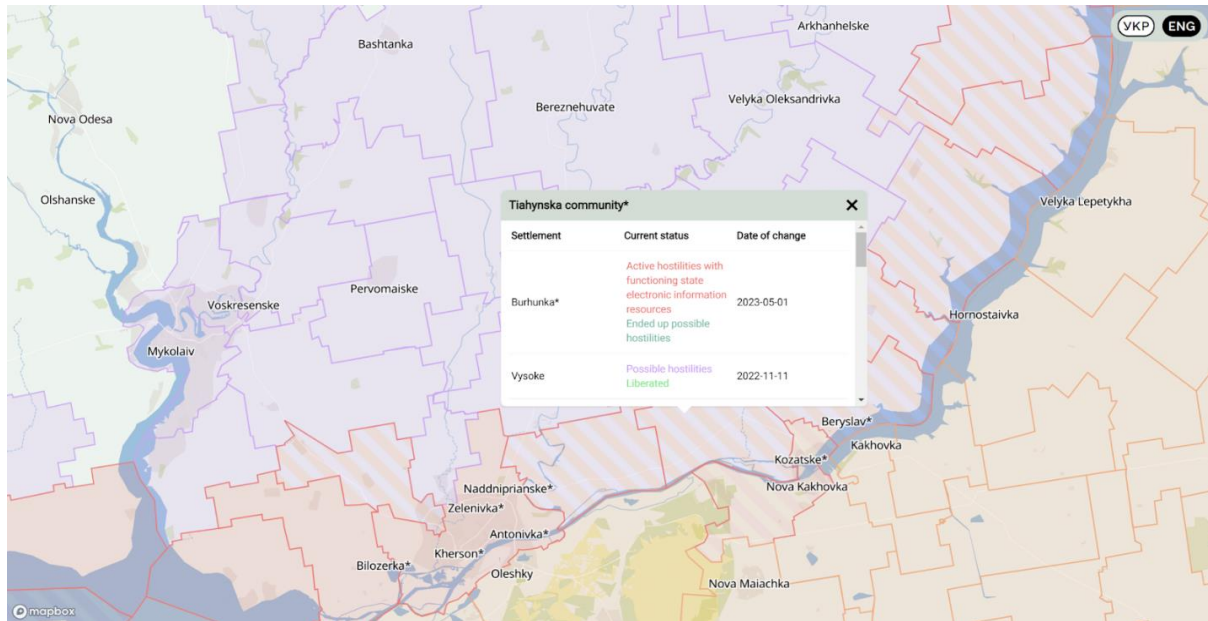
**Territorial communities are crucial to the recovery process and will be assigned a leading role in reconstruction efforts.** According to Ukrainian legislation, territorial communities are responsible for developing planning documents, establishing communication with international partners, and implementing restoration projects in the respective territories based on an inclusive approach that entails engaging and consulting with local civil society. To strengthen the capacity of territorial communities, the Government, together with development partners, is expected to work on creating mechanisms to strengthen the competencies of representatives of local self-government bodies in strategic planning, public investment management, anti-corruption, project management, urban planning, digitalisation, investment activities and work with donors.

**However, communities have very different needs and resources,** depending on the war related situation in each geographic region.

## 4.1. TERRITORIES WHERE HOSTILITIES ARE (WERE) CONDUCTED

**There are several types of affected territories.** [The Ukrainian legislation](#) divides territories by types according to their location against active war actions: where hostilities are (were) conducted, which include territories of possible hostilities and territories of Ukraine temporarily occupied by the Russian Federation. The Order of the Ministry of Reintegration of the Temporarily Occupied Territories of Ukraine [contains a list](#) of territories where military operations are (were) conducted or temporarily occupied by the Russian Federation (updated periodically). The list specifies the date of beginning and end of hostilities (the date of occurrence and termination of the possibility of hostilities) or temporary occupation. All other hromadas that are not on the list are rear communities, but there is no such definition in Ukrainian legislation. The governmental Diia portal visualises city, settlement, and village hromadas and their status on the [interactive map](#).

Figure 16. Screen of Interactive Map



Source: Diia portal

**Territories where military operations are (were) conducted** include territories of possible military operations, territories of active military operations and territories of active military operations where state electronic information resources operate. Territories of possible hostilities [may include](#) territories that meet one of the following criteria:

- border on the territories of active hostilities or on the territories temporarily occupied by the Russian Federation;
- border the state border of the aggressor state.

**The territories of active hostilities** are defined as the territories through which the line of combat contact passes or which border the temporarily occupied territories and where it is currently impossible to fully perform the functions of the state, in particular in terms of access to public electronic registers, and there is a significant threat to the life and health of the population.

**The territories of possible hostilities** are those bordering the territories of active hostilities or temporarily occupied territories or adjacent to the state border with the aggressor state, where it is possible to ensure the functions of the state, to which the population can return, but are periodically subjected to hostile shelling.



## 4.2. THE TERRITORIES OF RECOVERY

**A territorial community is classified as a restoration area** if at least one of the following criteria is met<sup>30</sup>:

- hostilities took place on the community's territory;
- the community's territory or part of it was temporarily occupied;
- there is destruction of infrastructure and housing as a result of hostilities and/or shelling;
- the community's territory is characterised by significant population displacement to other regions and/or other states and a sharp deterioration in the level of socio-economic development.

**To assess and assign hromadas to the recovery areas, the Ministry [establishes a commission](#)**, which also includes members of the Verkhovna Rada, the Parliament's specialised committee. The commission reviews proposals prepared by the Ministry, assesses whether the communities meet certain criteria, and decides on their assignment to the recovery areas. The list of communities included in the recovery areas is approved by the Cabinet of Ministers of Ukraine in the State Strategy for Regional Development of Ukraine.

**In addition, the Government approved the Procedure for the Development, Implementation and Monitoring of the Regional Recovery and Development Plan**, as well as the Recovery and Development Plans for Territorial Communities. The relevant plans will be developed for the period until 31 December 2027.

**The Draft Regional Recovery and Development plan is developed by the Ministry** together with other interested central and local executive authorities and takes into account the existing potential and prospective specialisation of the territories. The development of the plan begins within 10 days after the Cabinet of Ministers approves the list of communities included in the recovery area.

**The Regional Recovery and Development Plan includes** among other things, recovery and development tasks and measures; projected needs and possible sources of funding; indicators of the implementation of recovery and development tasks and measures and their projected values; a list of regional (local) development projects to be implemented as part of the plan; and regional recovery and development plans. The regional recovery and development plan is approved by the Cabinet of Ministers of Ukraine.

**In turn, local governments submit a draft plan for the recovery and development of the territorial community for approval within two months after the Ministry** publishes information on the development of the regional recovery and development plan. This draft plan includes tasks and measures for recovery and development; projected needs and possible sources of funding (the most common sources of funding are grants from international donors, state budget funds, and support from local businesses and residents); indicators of the implementation of tasks, recovery and development measures and their projected values; and a list of regional (local) development projects.

<sup>30</sup> According to [the Resolution of the Cabinet of Ministers of Ukraine](#)

**The Ministry annually monitors the implementation of the regional recovery and development plan** on the basis of official statistics information from ministries and other central executive authorities. The monitoring of the implementation of the regional recovery and development plan may be carried out, in particular, on the basis of the DREAM recovery management ecosystem and the Geographic Information System for Monitoring and Evaluation of the Development of Regions and Territorial Communities (GIS).

**The draft plan for the recovery and development of the territorial community includes the projected need and possible sources of funding.**

**Other types of documents are Comprehensive Recovery Programmes.** They are [strategic documents](#) in which hromadas set out their recovery plans for the medium term. They are created by taking into account all the factors, challenges, and needs that may play an important role in their future development. All programmes are being developed for the period up to 2027. So far, 126 hromadas have already decided to develop a Comprehensive Recovery Programme on their territory (as of December 2023).

**However, the interpretation of international organisations may differ from Ukrainian legislation.** According to [U-LEAD](#), the program of comprehensive restoration of the territory is an analytical and spatial document that defines the main urban planning and socio-economic priorities of the policy of restoration of the territory affected by armed aggression. The municipality recovery and development plan is a strategic planning document that will include recovery and development tasks and measures, as well as local development projects. These two types of documentation are interrelated and will help municipalities both to ensure an effective recovery process and to attract funds for the implementation of recovery projects.

### 4.3. MAPPING THE RECOVERY PROJECTS

**Currently, there is no single database with all recovery plans.** If they are already publicly available, they are on hromada websites (probably only in Ukrainian) or on the websites of partner organisations that helped the hromada develop the document. Such data can also be obtained through an official request to local authorities.

**However, the work to establish such a database is in progress.** DREAM is [a state Digital Restoration Ecosystem](#) that creates a digital route for all restoration and development projects and ensures their transparent and efficient implementation at the national, regional and local levels. DREAM is a **single window for working with restoration projects.**

**The key users of the DREAM ecosystem are local governments, central executive authorities, international financial organisations and investors, business representatives, journalists, and civil society activists.** All initiators of restoration projects will have appropriate access to a specialised interface with the necessary management and control tools. At the same time, the general public will have access to all system data in the form of convenient dashboards in the analytics module.

The **DREAM ecosystem aims to cover the entire restoration process**, so it is multi-component and interacts with 9 different systems at once. DREAM integrates with these digital

registries and systems, providing end-to-end data exchange that allows for tracking the implementation of a restoration project at every stage.

- Register of Damaged and Destroyed Property;
- GIS (geographic information system for regional development (under development));
- Unified State Electronic System in the field of construction (e-Construction);
- Diia (a single portal for public services);
- Restoration project management system;
- Prozorro (an electronic public procurement system);
- eContracting (under development);
- Spending.gov.ua (a single web portal for the use of public funds);
- Unified State Register of Legal Entities.

**The Government strives to introduce digital solutions to ensure a unified approach to managing all recovery and reconstruction processes** (including registering damages and the compensation mechanism), comprehensive planning of investment projects and monitoring of their implementation, as well as the realtime access to information by the general public. In addition, the expanded use of digital solutions that are based on the methodologies and guidelines approved by the Government will contribute to better informed decision-making at all levels and will help, at least partially, to compensate for the limited capacity to manage the investment projects. Sound public investment management with clear roles and responsibilities for the main stakeholders will play a role in attracting development partners and encouraging competitive and transparent project selection. Clearly stipulated strategic priorities for public investment and a pipeline of appraised investment projects will provide guidance to development partners and ensure more efficient use of resources during the reconstruction. A robust project monitoring framework with a high degree of digitalisation, including using new budget planning and monitoring IT systems. Specifically, the DREAM system will be implemented to provide real-time information on project implementation, allowing for transparency, timely identification of bottlenecks, and the making of necessary adjustments.

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**05**

**DEBT MANAGEMENT  
PRACTICES**

## 5.1. LOCAL BORROWING

**The local borrowing market has existed for a long time, but not everyone has been able to use this instrument until recently.** Until 2024, the right to carry out local borrowing and provide local guarantees was only held by the regional and city councils. However, at the end of 2023, the Parliament [also granted](#) this right to rural and settlement territorial hromadas, thereby expanding access to credit resources for all territorial communities (the process of approving and obtaining the loan is the same as for regional or city councils)<sup>31</sup>. The key idea of the changes was that local loans should become a strategic source of investment resources for the implementation of long-term infrastructure projects by all local self-government bodies.

**Decisions regarding local external borrowings and the provision of local guarantees are made exclusively at the councils' plenary sessions.** Thus, key decisions are made by the local council itself, and the head of the local financial body (financial department or administration) acts solely on its behalf (the head of the financial body is an employee of the local municipality). When making a decision to borrow, the local council delegates authority to the head of the financial body to conclude contracts on its behalf.

**Local borrowings and revenues from providing local guarantees are sources of formation of the special fund of the budget** in terms of financing, meaning that the funds from them have a clear earmarked purpose. This implies additional current control by the State Treasury Service authorities when spending funds from such sources. Local borrowings are carried out, in particular, for financing the development budget and are used for the creation, expansion, or renewal of long-term strategic objects or objects that ensure the fulfilment of tasks of rural councils aimed at meeting the interests of the population of territorial hromadas.

**Capital expenditures of the development budget are directed towards the** socio-economic development of regions; implementation of investment projects; construction, major repair, and reconstruction of objects in the socio-cultural sphere and housing and communal services sector; construction of gas pipelines and gasification of settlements; construction and acquisition of housing for certain categories of citizens in accordance with the legislation; preservation and development of historical and cultural sites of Ukraine and reserves; construction and development of metro networks; purchase of wagons for municipal electric transport; development of road infrastructure; purchase of school buses and emergency medical vehicles; modernisation of the material and technical base of municipal healthcare institutions, computerisation, and informatisation of schools and hospitals; environmental measures; other measures related to expanded reproduction.

**There is a legally defined [procedure for local borrowing](#), which was updated at the end of March. Procurement legislation does not apply to loans<sup>32</sup>.** Please see **Appendix A1** for a list of legal acts that regulate procedures for local borrowing and local guarantees.

<sup>31</sup> As provided for in the European Charter of Local Self-Government (Article 9, paragraph 8)

<sup>32</sup> Clause 13 of Article 3 and of Clause 2 of Article 6, the Law "On Public Procurement"

## 5.2. LOCAL GUARANTEES

**Local guarantees can be provided by the decision of the city, settlement, or village council.** Local guarantees are intended to ensure full or partial fulfilment of debt obligations of business entities that are in municipal ownership of the territorial hromada, located in this hromada, and implementing investment projects within its territory. The purpose of such projects is the development of communal infrastructure or, for example, the implementation of resource-saving technologies.

**The maximum amount of providing local guarantees, as well as the authority to provide them, is determined by the decision on the local budget.** Like local borrowings, local guarantees can only be provided by the relevant local self-government bodies subject to compliance with the conditions of payment and maturity and the fulfilment of obligations in the manner prescribed by law. Therefore, municipal enterprises for which the council makes a decision to provide local guarantees are obliged to provide property or other security for the fulfilment of obligations and pay to the respective local budget a fee for receiving guarantees in the amount set by the council. The creditworthiness is assessed by the lender, and the local council, as the guarantor of the debt, analyses the ability to repay obligations in agreement with the Ministry of Finance.

**During the term of the local guarantee agreement, local councils provide for expenses for fulfilling guarantee obligations for payments due in the corresponding fiscal period.**

Such expenses are provided for secured guarantee contracts where the guarantee event has already occurred, in the amount equal to the sum of payments under these contracts, and for other guaranteed contracts, not less than 50% of the sum of payments under these contracts. No separate cash cover is created, but a separate budget item for guarantees is provided (at least 50%, but possibly more, subject to negotiations between the lender and the borrower). Since all local budgets are balanced, there are planned revenues for these expenditures (if the amount is not used because the guarantee event does not occur, such funds go to the free balance, and the local council plans these expenditures again for the next year).

**The legal act regarding the provision of a local guarantee is formalised in writing and must specify:**

- the subject of the guarantee;
- full names and addresses of the business entity and creditor;
- loan (borrowing) amount;
- amount of guarantee obligations and their fulfilment procedure;
- rights and obligations of the guarantor and creditor;
- conditions for the occurrence of the guarantee event;
- duration of the guarantee.

## 5.3. LIMITATIONS FOR LOCAL BORROWING AND GUARANTEES

To minimise risks, a set of limitations has been established that must be considered when applying such instruments. Specifically:

- The total amount of local debt and guaranteed debt as of the end of the fiscal period cannot exceed 200% of the average annual amount of general fund revenues of the local budget received over the three preceding fiscal periods (years), excluding personal income tax (PIT) and intergovernmental transfers. In case of expected exceeding of this limit, the local financial authority promptly applies to the relevant regional or city council for permission for temporary exceeding of such limit and submits for approval a plan of actions to bring such total debt amount into compliance with the provisions of this Code, subject to prior agreement with the Ministry of Finance of Ukraine.
- Local budget expenditures on servicing local debt cannot exceed 10% of the expenditures of the general fund of the local budget. (Here, it means that in 1 budget year, expenditures on servicing local debt cannot be more than 10% of the expenditures of the general fund of the local budget this year. The loan could be for any period).
- If the payment schedule is violated, leading to the imposition of any penalty sanctions, then it is prohibited to carry out new local borrowings and provide local guarantees in the current fiscal period.
- If, during the current and subsequent fiscal periods after the settlement of overdue debt and payment of all accrued penalty sanctions, a repeated violation of the payment schedule occurs, then local self-government bodies are not allowed to carry out new local borrowings and provide local guarantees for the next three fiscal periods.
- Providing local guarantees to an entity with overdue debt to the territorial community is prohibited.

**Table 4. Calculation of the Maximum Borrowing Limits for Territorial Hromadas**

Region (Oblast)	Hromada	Type of council	Population (thousands)	Annual budget 2023 (mln UAH)	Annual budget 2023 (mln USD)	Maximum borrowing limit (mln UAH)	Maximum borrowing limit (mln USD)
Lvivska	Lvivska	city	777,2	15088	370,71	9142,7	224,6
Dnipropetrovska	Dniprovska	city	971	20874	512,87	10024,0	246,3
Zhytomyrska	Zhytomyrska	city	263,2	4695	115,36	1962,7	48,2
Ivano-Frankivska	Kolomyyska	city	74	1325	32,56	304,0	7,5
Cherkaska	Umanska	city	82,5	1125	27,64	542,0	13,3
Chernivetska	Hlybotska	settlement	19,1	190	4,67	62,0	1,5
Mykolaivska	Yelanetska	settlement	14,3	187	4,59	83,3	2,0
Chernihivska	Ivanivska	village	7,2	84	2,06	35,3	0,9
Zakarpatska	Horondivska	village	9,2	81	1,99	21,3	0,5

Source: KSE

**The volume and conditions of local borrowing and the provision of local guarantees are agreed upon with the Ministry of Finance.** The Ministry verifies the complete set of documents and makes the appropriate decision within a monthly period. This period is calculated from the date of submission of the last document provided for consideration. To obtain approval, the local council sends a paper or electronic notification to the Ministry of Finance in paper or electronic<sup>33</sup> form to which properly executed documents are attached (see **Appendix 2** for the list). Changing significant terms (type, amount, currency, terms, interest rates on borrowing, repayment terms, debt principal amount) also requires approval. Other terms of the credit agreement are not significant. In the case of multiple borrowings, a separate written notification is submitted for each borrowing, along with all specified documents.

**The approval procedure takes some time.** If there are reasons for a refusal by the Ministry of Finance, the local council rectifies deficiencies within 15 calendar days according to the Ministry's comments and adjusts, if necessary, the volume of obligations under borrowings expressed in foreign currency. The Ministry of Finance considers the relevant documents within one month from the date of their receipt. Experts of the Ministry have the right to receive additional information, as necessary, to make a decision on approving the volume and terms of borrowing (significant changes).

**“By default” answer depends on the submission type.** In case of non-receipt of a response within the specified period, the applicant's submitted notification for approval of the volume and terms of borrowing (debt restructuring) remains unreviewed. The volume and terms of local external borrowings through obtaining loans from international financial organisations are considered approved if no decision is made by the Ministry of Finance within one month from the date of document submission for approval (with the local banks, it is declined if no decision is made by the Ministry of Finance within one month from the date of document submission for approval).

**There is a dedicated register for such deals.** All contracts for local borrowing, contracts for fulfilling obligations secured by local guarantees, and contracts for reimbursement of local budget expenses, as well as significant changes to such contracts, are registered in the [Register of Local Borrowings and Local Guarantees](#).

## 5.4. LOCAL DEBT MANAGEMENT

**There is no provision for the bankruptcy of local self-government bodies and proceedings in bankruptcy cases of debtors — budgetary institutions, as well as the sanitation of such debtors, are not allowed**<sup>34</sup>. According to amendments to the Code of Ukraine on Bankruptcy Procedures, there is a rule that prevent the opening of bankruptcy proceedings against state authorities, local governments, budgetary institutions, and organisations. Accordingly, debt collection should take place within the terms of the credit

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<sup>33</sup> Using qualified electronic signatures in accordance with the Laws "On Electronic Documents and Electronic Document Management" and "On Electronic Trust Services"

<sup>34</sup> The [Law "On Amendments to the Code of Ukraine on Bankruptcy Procedures"](#), paragraph 4



agreement, with the possibility of covering part of the debt with collateral. In case of a breach of the contract terms, debt collection should occur through legal proceedings.

**Municipalities may make deposits, too.** To control the risks associated with local debt management, the local financial authority, upon decision and in accordance with the procedure approved by the local council, may conduct operations with the placement of temporarily available funds of the local budget on deposits or through the acquisition of government securities, securities issued by the respective local council, with subsequent:

- return of such funds by the end of the budget period;
- early redemption of obligations under local debt (it is an option);
- exchange of obligations under local debt for the purpose of currency replacement;
- reduction of the interest rate;
- extension of the maturity of such obligation or reduction of the volume of local debt in case of exceeding its maximum limit.

**The local financial authority approves the debt management program** for the respective year and publishes it within a month after the beginning of the corresponding budget period (by January 31) in the official printed publication of the LSG (this information is publicly available on hromadas official websites).

**Local borrowings are not considered the state's debt obligations, and state guarantees are not provided for local loans**, therefore, local borrowings are not directly linked to the calculation of the overall state debt. According to the Procedure for Controlling Risks Associated with Managing State (Local) Debt, during the risk control process related to debt management, the Ministry of Finance (or the local financial authority):

- Conducts risk assessments to minimise them.
- Determines the optimal balance between expected expenditures of the state (local) budget on debt management and risks.
- Engages in debt management operations.

Risk assessment related to debt management is based on data including:

- Debt accounting and monitoring results.
- Current macroeconomic situation, including budgetary, monetary, and exchange rate policies.
- Domestic market situation of government securities and/or local loan bonds and the global capital market.
- Forecasted resource balance of the general fund of the state budget prepared by the Treasury.
- Prospects of the global economy are prepared by research institutions, international financial organisations, investment banks and companies, and other financial institutions.

**The Ministry of Finance (or local financial authority) approves the debt management program for the respective year** and publishes it within one month after the start of the relevant budget period on the Ministry of Finance website (in the official printed publication of the local self-government body). Based on the determination of the optimal relationship between expected expenditures of the local budget for debt management and the risks associated with managing such debt, the local financial authority includes in the forecast project of the local budget for the next two planned budget periods:

- Forecast indicators of the local budget for debt management;
- Maximum amounts of local debt and provision of local guarantees, methods of borrowing planned for financing the development budget;
- Forecast values of the ratio of external and internal local debt, floating and fixed interest rates;
- Forecast weighted average maturities of external and internal local debt volumes of operations for managing such debt.

**To better regulate the procedure of local borrowing, recently the Ministry of Finance amended the procedures for borrowing and providing local guarantees.**<sup>35</sup> By implementing these changes, the Government plans to improve control over local borrowings, reduce risks associated with debt servicing, and minimise possible abuses by local self-government bodies. By this resolution, the Government has regulated provisions regarding:

- actions of local self-government bodies in case of significant changes in local borrowing terms and/or transactions regarding the provision of local guarantees;
- creating conditions for monitoring approved decisions on local borrowings, provision of local guarantees, and changes to the local budget;
- the necessity to convert indicators of local debt, debt guaranteed by the territorial community, and the provision of local guarantees for loans in foreign currency into the hryvnia equivalent.

For the analysis of the effectiveness of local debt and guaranteed debt management and for the Ministry of Finance to conduct a comprehensive examination of materials submitted by local councils for compliance with budgetary legislation when approving the volume and terms of local borrowings and provision of local guarantees, **it is necessary to submit:**

- information on the current status of debt obligations under loans (loans), including those guaranteed by local guarantees, for three budget periods preceding the budget period in which the decision on local borrowing or provision of local guarantee is made and for the current budget period;
- schedules of planned and actual receipts and payments for local borrowings and loans (loans) guaranteed by local guarantees;
- forecast schedule of obtaining loans (loans), repayment, and servicing of local debt;
- calculate costs for repayment and servicing of loans (loans), including those secured by local guarantees, the volume, and the terms approved.

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<sup>35</sup> The Resolution of the Cabinet of Ministers of Ukraine No. 313 dated March 22, 2024

**06**

**INVESTMENT PROJECTS  
IN MUNICIPALITIES**

## 6.1. DEVELOPMENT OF PROJECT RELATED REGULATION

**Ukraine is in the process of development of the unified Public Investment Policy, driven both by the demands of external partners and by the internal necessity to establish uniform rules for reconstruction and development of both state-owned and municipal infrastructure.** As of now the approach to initiating, financing and implementing investment projects by municipalities is governed by various types of legislation (both state and local level), which makes it an extremely difficult task to formalise in the unified streamlined business process. The legislation on the segregation of duties and responsibilities of local authorities in the decision-making process is described in previous chapters.

**Investment projects initiated by the local authorities may be financed by several sources** that include local budget funds and proceedings provided by the central budget level, donor financial resources and loans (provided by local or international finance institutions).

**A private investor considers various capital investment objects (investment projects) to choose a method of allocating financial resources that will yield the highest returns at an acceptable level of risk for the investor. The analysis of an investment project for the municipal sector should begin with examining the characteristics of the investment environment (investment climate) in a similar matter, however, usually, it is stated in the local level legislation as in relatively high-level statements and principles.** At the local level, each community has a list of documents that regulate capital investment projects, among other things:

- **The comprehensive spatial development plan of the territorial community** - involves both urban planning documentation at the local level and land survey documentation, which defines the spatial organisation, the functional purpose of the territory, basic principles and directions for forming a unified system of public services for the population, road network, engineering and transportation infrastructure, engineering preparation, and landscaping, civil defence of the territory and population from hazardous natural and man-made processes, land protection, and other components of the surrounding natural environment, forming an ecological network, conservation and preservation of cultural heritage and the traditional character of the environment of settlements, as well as the sequence of decision implementation, including the phased development of the territory;
- **Local development strategy**, which could involve:
  - Program of sustainable energy development;
  - Strategy for enhancing the city's competitiveness;
  - Program for promoting the development of small and medium-sized enterprises;
  - Investment attraction program;
  - Community recovery and development plan, etc.

**The local authorities of hromadas (local self-selected bodies) possess most of the responsibilities in the selection and approval of projects, decisions on ways of financing the project, and approval of various forms of potential partnership agreements.** Local authorities may also delegate part of their functions via the creation of special departments for investments, asset management or for capital construction. Usually, such departments are created in relatively large hromadas. Examples of such delegations and departments may be found in big municipalities like Kyiv, Lviv, or Ivano Frankivsk and it is less common for the smaller hromadas.

**Within the practice of implementing investment projects, examples of investment structures existing within the executive authorities of Ukrainian cities include:**

- In Kyiv, there is the [Municipal Enterprise "Kyiv Investment Agency"](#), which is subordinate to the Department of Economics and Investments of the Kyiv City State Administration (KCSA), acting as an "investment agent." There is a separate regulation of the Kyiv City Council regarding investment contests for the construction and reconstruction of [municipal property objects](#). This regulation outlines a slightly different procedure than that provided for by the Cabinet of Ministers of Ukraine Resolution № 70 on the implementation of projects supported by IFIs. This procedure involves the Kyiv Investment Agency conducting a competition where an investor is engaged to invest funds in construction projects. The [investor is selected based on the best competitive proposal](#) for implementing the investment project.
- In Lviv, the formation of investment proposals, approval of the list of investment objects, preparation of investment projects, conduct of investment competitions, and conclusion of investment agreements are regulated by [Resolution No. 2547 of the Lviv City Council dated July 18, 2013, "On the Approval of the Regulation on the Implementation of Investment Activities in Lviv"](#). The organisation of investment competitions is ensured by the [Department of Investments and Projects of the Department of Economic Development of the Lviv City Council](#). The department's task is to implement projects with the funds of private investors and with the support of international financial organisations, development organisations, and programs. Investment projects in Lviv, including those in collaboration with international financial organisations, can be found on the [website](#).

**Since February 2024, the existing practice has divided all investment projects into two categories: projects aimed at covering urgent needs and regular investment projects.**

This distinction primarily arises from the necessity to respond to urgent challenges caused by damages, making it impractical to apply uniform approaches to all projects. Specific procedures have been established for implementing urgent projects to address damage to buildings and infrastructure.

**Taking into account the volume of restoration projects that need to be implemented, the GoU plans to coordinate the recovery process across the country on the principle of a single project pipeline.** It is expected that the framework for public investment projects will be aligned across the country and will be formalised in the official Public Investment Policy in early 2025. The government approach defined in the Ukraine Plan stated that to ensure the availability of funding for the reconstruction effort on the local level, a transparent mechanism to finance the recovery, reconstruction, and modernization needs of subnational authorities, and in particular local self-government bodies, should be created and applied. This mechanism will allow to provide financial support to subnational authorities, in particular to

local self-government bodies, in the implementation of priorities in the field of restoration, reconstruction, and modernization, which are defined in their local and regional development strategies and correspond to the priorities of the State Regional Development Strategy and relevant sectoral strategies. The Government is expected to ensure the preparation of a coherent system of strategic planning documents at the national, regional and local levels. A sound public investment management with clear roles and responsibilities for the main stakeholders will play into attracting development partners, encouraging competitive and transparent project selection. It will also include a significant digitalisation component: DREAM, E-Construction, a unified geographic information system for monitoring and evaluating the development of regions and territorial communities, Prozorro e-procurement system etc.

## 6.2. FINANCING BY THE STATE

**On the state level today there are over 10 different government procedures that may regulate financing public investment projects from the state budget** or based on the state guaranties, funds or assets.

**Special legislation for war-related projects.** Projects related to the restoration of damaged or destroyed property follow the same processes, procedures, and legislation as other investment projects initiated by local authorities, with an additional special financial source: the Fund for the Elimination of Consequences of Armed Aggression in 2022 (the Fund). The Fund is expected to use a potentially broader range of financial resources that may also include reparations or other recoveries from Russia and other legally permissible sources. The utilisation of resources from the Fund is governed by a special procedure. Funding involves providing funds for non-refundable, gratuitous, targeted spending during the budgetary period (one calendar year).

**Funding from the local budget through specific programs.** Local self-government bodies have the authority to approve local programs and establish funds aimed at providing compensation and restoration for damaged or destroyed immovable property. Compensation for damaged property will be funded by the Fund for the Elimination of Consequences of Armed Aggression of the Russian Federation<sup>36</sup>. Funding involves the provision of resources for non-repayable, gratuitous, and targeted expenditure within the budget period. Sources of funding include state and local budgets; funds from state and local extrabudgetary funds (if established); own funds of enterprises, institutions, and organizations (self-financing); credit resources; and other funds from citizens and legal entities.

**Municipalities may also use funding from the state budget's reserve fund for priority restoration works on various properties, regardless of ownership form of the asset<sup>37</sup>.** Technically it involves transferring funds to regional military state administrations, which then organise and oversee the reconstruction process locally.

<sup>36</sup> Paragraph 2 of the [Cabinet of Ministers Resolution No. 118 dated February 10, 2023](#)

<sup>37</sup> Order of the Cabinet of Ministers No. 280-r dated April 10, 2022, "On Allocation of Funds from the Reserve Fund of the State Budget"

## 6.3. FINANCING BY PRIVATE INVESTORS, BANKS

**To attract additional financing for investment projects municipalities may use both forms of repayable financial instruments: bonds and credit lines.** As of today credit instruments are still not widely used by the local authorities. [The reason](#) for this is a lack of awareness about the benefits and risks of local borrowing. The Ministry of Finance actively [encourage](#) hromadas to investigate these instruments as a source for investment projects financing. Before 2023, only regional and city councils had access to such credit resources. However, recent changes to budget legislation have standardized the right for village and rural councils to also engage in local borrowing and provide local guarantees. Experts are stating that

**Ukrainian banks are actively promoting potential loans to municipalities.** Examples of unsecured loans programs are available within the state-owned banks: on UkrGasbank and Oshchadbank websites. UkrEximbank also successfully implemented projects with small communities, including cases of financing communal enterprises operating within hromadas established in the rural area. Cooperation with national commercial banks has the following advantages: loans in hryvnia (no currency risks) and relatively quick decision-making process. However, the disadvantages will include: short repayment terms (up to 5 years) and short grace periods (up to one year), restrictions on loan sizes, and relatively high interest rates. Additionally, for the loans attracted through the communally owned enterprises the state program with lower interest rates 5-7-9 might be a solution for the cheaper funding.

**Ukraine employs a specialised mechanism for financing infrastructure projects through infrastructural bonds on local market, applicable also to local municipal endeavours<sup>38</sup>.** The funds raised can only be used for financing the construction (reconstruction) of infrastructure objects or the implementation of an infrastructure project (its individual stage). Issuance of infrastructure bonds can be carried out by an entity that implements or finances an infrastructure project, following the procedures established by the National Securities and Stock Market Commission. The funds from the placement of infrastructure bonds are directed exclusively towards financing and/or refinancing the expenses of the infrastructure project. An agency implementing an infrastructure project for which the issuance of infrastructure bonds has been enabled is not entitled to take any actions that may result in early termination, cancellation, or any other loss of rights to the infrastructure project, as well as encumbrance of such rights.

## 6.4. FINANCING BY INTERNATIONAL ORGANISATIONS

**Cooperation with foreign financial institutions to raise funds is quite beneficial** and promising for the territorial communities of Ukraine. Especially considering the limitations in borrowing sizes and the high cost of credit resources in the domestic market. From the

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<sup>38</sup> Article 17 of the Law of Ukraine "On Capital Markets and Organized Commodity Markets

perspective of local councils, the advantages of cooperation with foreign financial institutions include:

- Expansion of financial opportunities for communities
- Long repayment terms (up to 30 years)
- Extended grace period (up to 10 years)
- Technical assistance provided with the loan
- Potential grant component (up to 30%)
- Relatively low real interest rates

**The significant drawback of such cooperation is foreign exchange risk** usually applied on the projects, especially in long-term financing.

**The financing of the projects with the direct international financial institution (IFI) support has a special regulation within the Ukrainian legislative system** - the Resolution №70 of the Cabinet of Ministers of Ukraine. The resolution contains procedures for all implementation stages of projects, supported by financial resources from international financial organisations (the resolution does not specially mention DFIs, NDBs, or foreign banks, only IFIs, but Ukrainian legislation may theoretically use one word for it depending if the institution has the framework agreement with the country or not) other than the International Monetary Fund (hereinafter referred to as the IMF), obtained as a loan or credit by the state or under state guarantees. Please see **Appendix A4** for more regulations related to cooperation between local authorities and IFIs. The Ministry of Finance ensures the maintenance of a registry of projects for the economic and social development of Ukraine supported by international financial organisations.

**To be eligible as a beneficiary of the investment project, a legal entity must pass this evaluation process and not have overdue debts for previous loans from IFIs or arrears to the state budget for tax payments and fees.**

The above mentioned Resolution №70 has a detailed description of the initiation stage of the project that will be described further.

**The project initiation stage consists of the following steps and the preparation of necessary documents at the initial step:**

1. Conducting preliminary consultations between the IFI and municipality regarding potential investment opportunities;
2. Performing analysis of the financial capacity of the city and the enterprise in which the potential investor is interested (analysis shall be prepared by the borrower and is subject to further MoF approval)
3. Preparation of a project proposal
4. Letter of consent from the central executive authority (for example, the Ministry of Infrastructure of Ukraine) responsible for implementing state policy in the respective field, expressing support for the project and readiness to be the responsible executor of the project or to designate a responsible executor, along with a conclusion about the project's alignment with the priorities of state policy in the respective field.



5. Letter from the international financial organisation (IFI) confirming support for the project (consent to provide funding), if available.
6. Documents for assessing the financial status of the potential beneficiary, as defined by the procedure for assessing the financial status of the beneficiary and determining the type of collateral for servicing and repaying the loan provided by financial institutions, or a letter of explanation from the project initiator about the impossibility of determining the beneficiary before signing the agreement between Ukraine and the IFI, including information on the procedure for determining beneficiaries if the project involves identifying beneficiaries after signing the agreement between Ukraine and the IFI (for projects intended to be implemented on the basis of financial self-sufficiency).
7. Certificate from the potential beneficiary indicating the absence of overdue debt on repayment and servicing of previously obtained loans (loans) from a financial institution (not required if the project involves identifying beneficiaries after signing the agreement between Ukraine and the IFI) (for projects intended to be implemented on the basis of financial self-sufficiency).
8. Certificate from the State Tax Service confirming the absence of overdue debt to the state budget for the payment of taxes and fees (mandatory payments) by the potential beneficiary (not required if the project involves identifying beneficiaries after signing the agreement between Ukraine and the IFI) (for projects intended to be implemented on the basis of financial self-sufficiency).

**Upon receiving an invitation from the IFI for negotiations, the responsible executor, either acting independently or through the central executive authority responsible for implementing state policy in the relevant area where the investment project is intended, submits the necessary documents for consideration by the Cabinet of Ministers of Ukraine.**

Several actions are undertaken, including the adoption of relevant acts:

1. The enactment of an act pertaining to the acquisition of financial resources from the IFI to execute the investment project. This act also encompasses determining the fee amount for the beneficiary, which is the business entity securing a loan (credit) facilitated by the state or providing a state guarantee. Additionally, it addresses the necessity of collateral provision if the beneficiary, a business entity, possesses state/municipal property, specifying the type and amount of collateral if required. Furthermore, it ensures compliance with other legal conditions associated with attracting financial resources.
2. Submission, as per legal stipulations, of proposals to the President of Ukraine for conducting negotiations and executing a contract between Ukraine and the IFI. This applies when finalising the contract on behalf of Ukraine.
3. Decision-making concerning negotiations and contract signing between Ukraine and the IFI. This process occurs if the contract is to be concluded on behalf of the Government of Ukraine.
4. Adoption of an act endorsing the signing of a contract between Ukraine and the IFI. This step is taken when finalising the contract on behalf of the Government of Ukraine, and negotiations are not required.

**Following the signing of the contract between Ukraine and the IFI, the responsible executor has a two-week window to sign or ensure the signing of the contract and submit it to the Ministry of Finance for final approval.**

**However, there is an alternative scenario for the development of investment projects within the potential direct interaction between the financial institution and the municipalities.** The procedure of such cooperation might be as follows:

- Conducting consultations between municipal representatives and IFIs regarding available funding options for infrastructure projects.
- Performing analysis of the financial capacity of the city and the enterprise in which the potential investor is interested.
- Obtaining an allocation letter and a project memorandum for preliminary financing (certifying that the IFI is willing to finance the project for a certain amount).
- Holding a local session of the city's executive body to discuss readiness to provide local guarantees in case of signing an agreement with the IFI (the issue of obtaining local guarantees, their terms, and scope are preliminarily coordinated by the local government with the Ministry of Finance).
- Signing the credit agreement.

## **6.5. PROJECT PREPARATION AND IMPLEMENTATION**

**Assuming that all steps of the negotiation process were conducted successfully, the progression of events in implementing the investment project may unfold as follows:**

- The customer, such as the municipality or municipal enterprise, initiates the implementation of the investment project through several key steps. Initially, they compile a list of damaged objects/objects requiring reconstruction / new construction projects and conduct an assessment of their technical condition. Following this evaluation, they prioritise the objects and proceed with the subsequent design phase. The customer's approach to organising and carrying out procurement activities for the restoration of populated areas is contingent upon the availability of project documentation for the objects earmarked for restoration. The design process, according to [DBN A.2.2-3-2014](#) includes the following stages:
  - technical and economic justification (TEA);
  - technical evaluation report (TER);
  - outline project (OP);
  - project (P);
  - working project (WP);
  - working documentation (R).

**According to the complexity category and class of consequences (responsibility) of the construction object, the design stages are divided into the following categories:**

- For objects of complexity categories I and II, design is carried out in:
  - One stage - detailed design (DD);
  - Two stages - for non-production objects, preliminary design (PD), and for production objects and linear objects of engineering and transport infrastructure - a feasibility study (FS) and for both - detailed design (DD).
- For objects of complexity category III, design is carried out in two stages:
  - Project (P);
  - Working documentation (WD).
- For objects of complexity categories IV and V, design is carried out in three stages:
  - For non-production objects - PD or, with appropriate justification, FS, and for production objects and linear objects of engineering and transport infrastructure - feasibility study (FS);
  - Project (P);
  - Working documentation (WD).

**With appropriate justification, the customer and the designer may agree to change the number of design stages. When overhauling objects, design in one stage (DD) is allowed.**

**This means that their strategy may differ depending on whether comprehensive project documentation already exists or not and the type of project complexity.** Usually, the next scheme of the project lifecycle could be observed:

- Absence of approved project documentation → procurement of works for the development of project documentation → procurement of construction works → monitoring contract execution, work acceptance, and commissioning.
- If approved project documentation has been transferred from the Regional State Administration (RSA) or local authorities (LA) → procurement of construction work → monitoring contract execution, work acceptance, and commissioning.

The Technical and Economic Assessment (TEA) and, according to best practices, Cost-Benefit Analysis (CBA) are components of an in-depth evaluation conducted to determine the practicality and viability of the proposed project and performed regardless of whether project documentation is available or not.

The scope and details of the Technical and Economic Assessment (TEA) are clearly defined by the [Resolution of Cabinet of Ministers № 515](#) and should contain the following information about the investment project:

1. Summary of the technical and economic justification;
2. Description of the market environment;

3. Assessment of the technical feasibility of the investment project and description of technical solutions;
4. Planned volume of significant investments and estimated maintenance (operation) cost of the investment object;
5. Legal aspects of implementing the investment project;
6. Analysis of the social indicators of the investment project and evaluation of the social impact from the implementation of the investment project;
7. Results of the commercial attractiveness analysis of the investment project;
8. General overview of government support, description of forms and overall volume of government support proposed for the implementation of the investment project;
9. Results of the fiscal impact analysis (budget efficiency) of the investment project, including the analysis of the project's impact on budgets at all levels (budget efficiency) in the long-term perspective (taking into account the impact of government support within the framework of the investment project implementation);
10. Analysis of the environmental consequences and risks of implementing the investment project (EIA, CRVA);
11. List of identified risks of the investment project, their assessment, and determination of the form of managing such risks.

**During the preparation of the financial model of the investment project, the following factors are taken into account:**

- Modelling cash flows is based on assumptions that include macroeconomic indicators and key parameters for long-term forecasting, Construction timelines, Planned project implementation period, Expected executive date of activities and revenue generation for the investment project, Operational activity timelines (operational revenue and expenses, maintenance costs);
- Tax legislation and accounting legislation requirements, including asset depreciation schedules considering their exploitation period, are taken into account during the financial model preparation for the investment project;
- Technical data of the investment project;
- Data on capital and operating expenses;
- Data on revenues with indication of the tariff/price setting method for the products;
- Data on financing (borrowed or own capital).

**The TEA necessary documentation may include the following requirements in terms of environmental protection issues:**

1. Environmental Impact Assessment (EIA): This assessment identifies the impact of planned economic activities on the environment and public health. It's mandated by the [Law of Ukraine "On Environmental Impact Assessment"](#) and involves several steps, such as notifying the intention to conduct the activity, informing the public, gathering information, conducting EIA, and obtaining expert evaluation;

2. Climate Risks Vulnerability Assessment (CRVA): While not legally required in Ukraine, the project's implementing agency may conduct this assessment if needed.

It is important to note that during the tendering process (for selecting a contractor to work on creating project documentation or executing works), certain criteria should be followed for selecting the tender winner:

For the creation of project documentation:

- The company should possess the relevant license for design;
- Engineers and designers involved should hold certificates for different levels of complexity of design (CC1, CC2, CC3) and demonstrate experience in designing similar projects that are subject to financing;
- The financial proposal is applicable to the Client.

For the execution of works:

- The financial capability of the company should be assessed;
- Experience in conducting similar complexity works should be considered;
- The financial and technical proposal from the tender participant must comply with the available tender documentation.

**Each of these assessments and plans plays a crucial role in ensuring the project's sustainability and compliance with financial, economic, environmental, social and other standards.**

**Nevertheless, it's important to note that any obligations related to the development of technical documentation throughout the project's duration remain independent of the project's funding source. This responsibility lies solely within the purview and decision-making authority of the parties involved in signing the agreement.**



**07**

**PUBLIC  
PROCUREMENTS**

**The public procurement system in Ukraine underwent major changes almost a decade ago.** The reform of public procurement commenced in February 2015 with the pilot launch of the ProZorro electronic procurement system, a collaborative effort between civic activists, businesses, government representatives, global experts, and NGOs. This system, a first in Ukraine, allowed suppliers to submit their bids electronically, rendering the entire procurement process transparent and open.

**For the full functioning of the sphere of procurement, which is a key component of economic development, the Parliament and the Government adopted a whole set of legal acts that provide an appropriate legal framework and regulate all aspects of this important process:**

**The key legislative act governing public procurement is the [Law of Ukraine "On Public Procurement"](#),** which defines the legal and economic principles for the procurement of goods, works, and services to meet the needs of the state and territorial communities. This law serves as the primary legal framework, outlining the general principles, procedures, and requirements for conducting public procurement in the country.

**As of April 1, 2016, this [Law](#) initiated the transition of all procurements in Ukraine to electronic format,** enabling both oversight bodies and the public to observe the procurement process online. With a vast amount of machine-readable open data available in the system, it facilitates swift access and analysis of procurement information, as well as various research endeavours.

**Other regulations include:**

- [Resolution of the Cabinet of Ministers of Ukraine No. 1178](#) introduces specific provisions for conducting state procurement during the period of martial law. It establishes additional rules and procedures for both contracting authorities and suppliers, particularly regarding the conclusion of direct contracts and the conduct of auctions with special features.
- [Resolution of the Cabinet of Ministers of Ukraine No. 166 "On Approval of the Procedure for the Functioning of the Electronic Procurement System and Authorization of Electronic Platforms"](#) approves the requirements for the functioning of the ProZorro electronic procurement system, conditions for the connection/disconnection of electronic platforms to the ProZorro electronic procurement system, conditions for their authorisation, and several other issues related to the system's operation.

## 7.1. THE PROZORRO SYSTEM

**In order to ensure maximum transparency in the process of public procurement, increase the trust of the business environment and effectively fight corruption, the innovative electronic procurement system ProZorro was implemented.** ProZorro is a centralised electronic system that brings together various participants in the procurement process in the state and municipal sectors of Ukraine, providing open access to government procurement (tenders) in Ukraine. All the functionalities offered by this system are available

to the general public without the need for registration or any barriers to access. All information about public tenders and procurement announcements is provided in Ukrainian. Additionally, announcements above certain thresholds are also published in English.

**The electronic procurement system is a hybrid monoplatform that provides technological capabilities for the activities of various entities performing different roles, uniting all participants in the procurement process — customers, suppliers, controllers and other interested parties, ensuring their interaction on a single platform.** In order to understand how public procurement works, it is important to know who is actually involved. Here are the main participants in the procurement process in Ukraine:

1. **Buyers (Customers)** — primarily budgetary institutions or enterprises that announce the procurement of necessary goods, works, or services. Here are some typical examples of customers in Ukraine:
  - State and local government bodies — they procure goods, works, and services to meet various needs of the state or territorial communities. These can be ministries, agencies, city councils, state institutions, etc.
  - Public sector enterprises — state-owned enterprises and organisations are also customers in the procurement sphere. They may procure for their own needs or to implement state programs.
  - Utilities and enterprises — organisations owned by local communities and procured to address municipal issues such as infrastructure, transportation, housing, communal services, etc.
2. **Participants** — businesses wishing to sell goods, works, or services to the state and participating in competitive bidding;
3. **Winner** — the supplier of goods, service provider, or contractor who signs a contract with the Procuring Entity;
4. **Platform** — the operator of the electronic system through which a Participant can join auctions on Prozorro. It is established and managed by private entrepreneurs. Information about procurements on all platforms is the same and is instantly synchronised - this is controlled by the State Enterprise "Prozorro", which is the administrator of Prozorro. Operators receive funds for service/transactions, which incentivises them to improve their service to attract as many clients as possible.
5. **Monitoring bodies/controlling authorities** — a set of state institutions that oversee procurement in Prozorro: State Audit Service, Antimonopoly Committee, Accounting Chamber, National Police, and Security Service of Ukraine.
6. **Non-governmental organisations** — a collection of civil society organisations and activists who monitor procurements in Prozorro to establish public control.

**In order to ensure complete transparency and availability of information for all who wish to observe the procurement process from the beginning to the execution of contracts, the electronic procurement system has created the possibility of accessing all data at every stage of this process.**

- Publication of notices: Procuring entities planning to conduct procurement publish notices about planned purchases on the [ProZorro web portal](#).



- Submission of proposals: Suppliers can view procurement notices on the ProZorro portal and submit their proposals.
- Electronic auction: If multiple suppliers submit proposals for one procurement, an electronic auction may be conducted to determine the winner.
- Evaluation and selection of the winner: Proposals from auction participants are evaluated according to criteria set by the procuring entity. The winner is then selected.
- Contract signing: The procuring entity signs a contract with the auction winner through the electronic system.
- Monitoring and reporting: Procurement processes are carefully monitored, and data on completed procurements are published on the [ProZorro web portal](#), ensuring transparency and openness.

## 7.2. PROCUREMENT PROCEDURES

The procurement legislation of Ukraine defines several main procedures by which customers can purchase goods, works or services. This legislation is adapted to EU directives, which allows not only ensure compliance with international standards in the field of public procurement but also to increase the level of transparency, efficiency and competitiveness of these processes. Thanks to this, Ukraine is integrating into the European market, increasing the credibility of its procurement practices both domestically and internationally. Ukraine's procurement legislation defines several main procurement procedures that procuring entities can use to purchase goods, works, or services:

1. [Open tender](#) (from UAH 200,000 to EUR 133,000) — a procedure with an embedded electronic auction to lower prices. The procuring entity announces what it wants to purchase and sets an initial cost. Participants upload their proposals and then compete with each other by constantly lowering the price. After the auction ends, the procuring entity is obliged to select the cheapest proposal if it meets all the rules and requirements, and then they sign a contract with the winner.
2. [Open tender with English publication](#) (from EUR 133,000) — this procedure aligns with EU practices. Overall, it's almost the same as the previous method, except for two features:
  - There's a pre-qualification stage where the procuring entity checks participants' proposals for compliance with technical and other requirements before stating prices.
  - Announcements for such procurements are published in English.
3. [Negotiation procedure](#) (single-source procurement) — this procedure involves purchasing goods, works, or services from a specific supplier without conducting

competitive bidding. It can be used in cases where there is only one supplier available or when an urgent task needs to be addressed.

4. [Prozorro Market](#) — the “Amazon” for the government, a progressive option for low-value procurements. Participants add their products to the website, and procuring entities simply click and purchase. No additional procedures are required. Typically, this works for standard items such as stationery, printers, etc.

## 7.3. PROCUREMENT ITEM CATEGORISATION

**A categorisation of purchases for goods, works, and services was developed in order to clearly define the specifics of each of these categories. This categorisation allows you to apply appropriate assessment methods, set quality standards, and comply with legal requirements, which greatly facilitates the planning and budgeting process.** Procurement items can be categorised based on their characteristics and properties. The main categories of procurement items include:

- **Goods** — physical products that can be purchased, such as raw materials, materials, equipment, computers, furniture, vehicles, etc.
- **Services** — non-material executive actions or results that can be provided, such as consulting, design, maintenance, transportation, logistics, training, medical services, etc. Services can vary widely. It can be machine repair, training services, or legal services.
- **Works** — construction works performed on a specific object, such as construction, repair, installation, dismantling, road construction, electrical works, etc.

**This categorisation helps to organise and classify different types of procurement items.** Defining the procurement item is a key step in planning public procurement. According to the Law of Ukraine "On Public Procurement," the subject of procurement is goods, works, or services purchased by the procuring entity within the procurement procedure or simplified procurement. The law clearly defines the terms "goods," "services," and "works." To determine the procurement item, procuring entities use the [relevant classifier](#).

## 7.4. STATE CONTROL AND AUDIT

**Control of public procurements is extremely important.** It ensures the transparency of all processes, prevents corruption and fraud, guarantees the efficient and rational use of budget funds, promotes public trust in public institutions, and also ensures fair competition among suppliers, which ultimately leads to receiving the best goods and services at favourable prices. The control over the financing of expenditures from the local budget (including funds obtained through local borrowings) is carried out by two institutions, the State Audit Service of Ukraine and the Treasury Service of Ukraine.

**The State Audit Service of Ukraine is a part of the system of central executive bodies and is a separate legal entity under public law.** The main tasks of the authority responsible for public financial control include the exercise of public financial control over the use and saving of public financial resources, fixed and other assets, correct identification of the need for budgetary funds and liabilities, efficient use of funds and property, status and reliability of accounting and financial statements of the controlled undertakings, as well as over compliance with the budget and procurement legislation, and over the activities of undertakings, regardless of their form of ownership, which are not classified by legislation as controlled undertakings, according to a court judgement delivered in criminal proceedings.

**The public financial control is ensured by the State Audit Service by conducting public financial audits, inspections, procurement audits and procurement monitoring.**

- The public financial audit implies verification and analysis of the actual state of affairs as regards the legal and effective use of public or communal funds, property and other public assets, the correctness of accounting and the reliability of financial reporting, as well as the functioning of the internal control system. The results of the public financial audit and their assessment are presented in the report.
- Inspections are carried out by the public financial control authority in the form of revision and consist of a documentary and factual check of a certain number of issues or individual issues pertaining to the financial and economic activities of the controlled undertaking, which should ensure the identification of the existing facts of violation of the legislation, identification of officials guilty of their commission and of financially liable persons. The revision results are presented in the report.
- Compliance with procurement legislation is controlled through procurement monitoring and procurement audits, as well as through public financial audits and inspections.

**At the same time, the Prozorro electronic procurement system provides free access to all information on public procurements that is subject to disclosure** in accordance with the law and also provides for the possibility to report the violations by informing the State Audit Service of the detected signs of violations.

**The Treasury exercises two types of control over the targeted allocation of budget funds** received from all sources: preliminary control during registration of the budget commitments undertaken by the spending units and recipients of the budget funds (checking the availability of necessary allocations) and routine control when executing the payment orders.

**The spending units assume budgetary commitments and make payments only within the limits of budgetary allocations** envisaged by the estimates and made from a special budget fund and only within the limits of the respective actual revenues to that special fund. The Treasury's IT system contains a separate module that provides for the registration of all budgetary commitments and their accounting only if they fall within the budget disbursements of the respective spending unit. When registering budget commitments, the budget allocations for the relevant budget period (i.e. one calendar year) are taken into account.

**Commitments undertaken by any participant in the budget process without appropriate budgetary allocations or in excess of its powers established by the Budget Code of Ukraine and the State Budget Law are not considered budgetary commitments** (except

for subsidies, allowances, benefits for housing, utility and communication services (subscription fees for the fixed phone), and compensation paid to citizens from the budget). Prior to making payment under the procurement contract, the Treasury uses the electronic procurement system to assure itself of the existence of the annual plan, the procurement contract and the report on the results of the procurement procedure, which confirms that the procurement procedure/simplified procurement procedure took place and resulted in the conclusion of the procurement contract.

**The budgetary commitments, accounting, and payment procedures are closely linked.**

The Treasury makes payments on the basis of payment orders based on the instructions for spending units within the balance of available allocations, provided that the respective budgetary commitment and budgetary financial liability are duly recorded. With the help of such controls, the spending units and recipients of budget funds are able to eliminate any violations or errors in a timely manner and prevent their occurrence in the future.

**The Ministry of Finance and the Treasury maintain the necessary supporting infrastructure** for accounting, making payments and reporting with many benefits, such as financial data integrity, as reported in the 2019 PEFA assessment by the World Bank.

**The Treasury is responsible for all the back office work.** Having due regard to the resources available in the general fund of the State Budget, the available and forecast balances on the TSA, registered budgetary commitments and the priority of expenditures and loans, the Treasury makes payments on behalf of the clients, keeps records of the receivables as well as loans granted and repaid, and prepares reports on the execution of the State Budget, local budgets and consolidated budget in the relevant year (including revenues, expenditures, lending and financing of the budget, guarantees issued, public debt and debt guaranteed by the state). According to the 2019 PEFA assessment, these reports and their transparency are considered to be the strong points.

**The Treasury also submits its reports to the President, the Verkhovna Rada, the Accounting Chamber, the President, the Cabinet of Ministers, and the Ministry of Finance.** The reports are prepared in accordance with the budget classification using detailed codes and indicators and are easily compared with the approved budget. The reports on revenues and expenditures, lending, financing of the budget and budgetary debt, and information on state guarantees are prepared on a monthly, quarterly, and annual basis. The expenditures in the form of transfers from the State Budget to the Pension Fund of Ukraine, local budgets, and state-owned enterprises are reflected in the Treasury's reports on budget execution. Under martial law, the Treasury strictly adheres to the requirements and deadlines set for submitting these reports.

**The Treasury services all budgetary transactions at the national and local levels,** allowing for regular monitoring and cross-checking of financial information, which results in accurate reporting. Cash balances on the TSA with the National Bank of Ukraine are consolidated on a daily basis.

**The Treasury maintains its records in the automated accounting and reporting system (E-Kazna),** which is also interrelated with the electronic payment system of the National Bank of Ukraine and the proper uninterrupted functioning of which in wartime is ensured, *inter alia*, through the support of critical IT infrastructure received by the Treasury as part of the material and technical assistance under the USAID Cybersecurity for Critical Infrastructure in Ukraine Activity.

**Access to the system and authorisation to carry out transactions is restricted** and requires using a qualified electronic signature on a secure storage medium. No records in the accounting system can be created or modified without affixing a qualified electronic signature and exercising control over the authority to perform such actions. The system has an information security block that ensures the accessibility, confidentiality and integrity of the information processed, accumulated and stored in the system. The automated accounting and reporting system and the Treasury's information and communication system meet all the requirements set by the National Bank of Ukraine for the bank automation systems in Ukraine.

**The national public sector accounting standards in Ukraine largely comply with the International Public Sector Accounting Standards (IPSAS).** According to the 2019 PEFA assessment, more than 80% of Ukraine's national standards are in line with IPSAS. The high level of responsibility is also confirmed by the public sector accounting assessment conducted in 2023 using the World Bank's PULSE methodology, which resulted in a B+ score. Ukraine is further improving and implementing reforms aimed at bringing its regulations in line with international standards, even in wartime.

**Moreover, a central-level system of internal control and audit has been established,** with more than 400 internal audit units operating in the public authorities (including territorial departments thereof) and other public institutions. An organisational framework for internal control within spending units has been established in Ukraine. The framework provides, in particular, that the internal control should be based on the principle of responsibility and segregation of duties, which implies the division of duties between the senior management of the institution and its employees, establishing the limits of their responsibility in decision-making (in decision development or performance of other actions). According to this instrument, controls will be implemented at all operational levels and for all functions and tasks of the institution and will include appropriate rules and procedures, the most typical of which provide for (i) authorisation and confirmation by obtaining permission from those responsible for the execution of transactions through signing, approval or confirmation procedures; (ii) segregation of duties and powers, as well as staff rotation to reduce the risk of errors or losses.

**To effectively prevent and detect all forms of corruption and to ensure transparency and integrity in the Government and public sector, there is a system of anti-corruption authorities functioning.** These authorities cooperate with each other and with other agencies to effectively combat corruption and ensure the rule of law:

- the National Anti-Corruption Bureau of Ukraine (NABU), an independent investigator of high-level corruption;
- the Specialised Anti-Corruption Prosecutor's Office (SAPO), responsible for supervising the observance of laws during the pre-trial investigation activities of the National Anti-Corruption Bureau of Ukraine;
- the National Agency on Corruption Prevention (NACP), responsible for the development and implementation of the state anti-corruption policy;
- High Anti-Corruption Court, which considers cases of corruption and adjudicates fairly.

**There is also effective legislation in Ukraine that regulates the activities of whistle-blowers and the protection of their rights.** The whistle-blower protection legislation provides mechanisms for reporting corruption, misconduct, or harmful acts and guarantees

the protection of whistle-blowers from retaliation or reprisals. It also provides for the confidentiality of the whistle-blower's identity, prohibition of discrimination and protection from any negative consequences that may arise in connection with their reporting. In addition, proper procedures are established for receiving and examining reports.

# APPENDICES

## Appendix A1. Legal acts regulating procedures for local borrowing and local guarantees

### *Main:*

- Budget Code of Ukraine (as amended on 08.11.2023, No. 3428-IX);
- Law of Ukraine "On Local Self-Government in Ukraine";
- Procedure for local borrowing (Resolution of the Cabinet of Ministers dated 16.02.2011, No. 110);
- Procedure for providing local guarantees (Resolution of the Cabinet of Ministers dated 14.05.2012, No. 541);
- Resolution of the Cabinet of Ministers No. 313 dated 22.03.2024.

### *Additional (to be brought into compliance with updated legislation):*

- Procedure for monitoring risks related to the management of state (local) debt (Resolution of the Cabinet of Ministers dated 01.08.2012, No. 815);
- Procedure for maintaining the Register of local borrowings and local guarantees (Order of the Ministry of Finance dated 25.07.2012, No. 866);
- Forms of settlements for local borrowings (Order of the Ministry of Finance dated 22.10.2015, No. 922);
- Forms of settlements for providing local guarantees (Order of the Ministry of Finance dated 22.10.2015, No. 921);
- Methodological recommendations on the organisation of local borrowing, provision of local guarantees, management of local debt and debt guaranteed by the Autonomous Republic of Crimea, regional council, city, town or village territorial community (Order of the Ministry of Finance dated 16.05.2024, No. 239).

## Appendix A2. Documents for approval of local borrowing or guarantee

To obtain approval, the local council sends a paper or electronic notification to the Ministry of Finance in paper or electronic form to which properly executed documents are attached, including:

- duly certified copies of:
  - decision on the local budget for the respective year, taking into account all changes adopted as of the date of notification submission (including changes regarding local borrowing).

- financial and budgetary reporting forms on the execution of the local budget for the year preceding the year in which the decision on borrowing (restructuring of debt obligations) is made;
- local budget forecast (for next year + 2 years after it. For example, in 2024 - for 2025-2027);
- borrowing decision (debt restructuring) project, which must contain information about:
  - borrowing purpose;
  - borrowing method;
  - significant borrowing terms (type, amount, currency, term, interest rates on borrowing, repayment terms, debt principal amount);
  - information about property or other collateral to secure debt repayment (the borrower, within its authority, utilises property and property rights within the corresponding territorial community for securing its obligations under local borrowing);
- borrowing calculations and justification (in the form approved by the Ministry of Finance);
- information about the current status of local debt repayment obligations, the status of local debt payments for the five years preceding the year in which the said decision is made, as well as obligations guaranteed by the local council and the status of payments for them (in the form approved by the Ministry of Finance);
- calculation of the average annual amount of general fund revenues of the local budget received over the three preceding budget periods preceding the local council's decision on local borrowing, excluding personal income tax and intergovernmental transfers (in the form approved by the Ministry of Finance);
- in the event of borrowing through the issuance of domestic local bonds - a draft decision on bond issuance and a bond prospectus (if applicable), information on the bond rating determined by authorised National Securities and Stock Market Commission rating agencies or internationally recognised rating agencies.
- in the event of borrowing through obtaining a loan, a certified copy of the loan proposal letter from the financial institution providing the loan is needed.

### Appendix A3. Construction regulations

**Depending on the type of project, the requirements for the construction or capital reparations project also include all the legislation and technical requirements related to all construction sectors in Ukraine ([The State Building Codes](#), [The Procedure for Developing Design Documentation for Construction Projects](#), the law [On Environmental Impact Assessment](#) etc.):**

- The development of design documentation for construction is carried out in accordance with the Procedure for Developing Design Documentation for Construction Projects, approved by the Ministry of Regional Development.



- The approval of design documentation for construction and its examination are carried out in accordance with the Procedure for Approval of Construction Projects and Their Examination, approved by the Resolution of the Cabinet of Ministers of Ukraine No. 560, dated May 11, 2011 (Official Bulletin of Ukraine, 2011, No. 41, Art. 1674).
- Expenditures related to financing capital construction are carried out in accordance with the Procedure for State Financing of Capital Construction, approved by the Resolution of the Cabinet of Ministers of Ukraine No. 1764, dated December 27, 2001 (Official Bulletin of Ukraine, 2001, No. 52, Art. 2374), and the Procedure for Approval of Titles of Objects, Construction of which is Carried Out with the Involvement of Budgetary Funds, Funds of State Enterprises, Institutions, and Organizations, as well as Loans Provided Under State Guarantees, approved by the Resolution of the Cabinet of Ministers of Ukraine No. 995, dated September 8, 1997 (Official Bulletin of Ukraine, 1997, No. 37, Art. 17; 2015, No. 97, Art. 3320).
- The acceptance of objects into operation is carried out in accordance with the Procedure for Acceptance into Operation of Completed Construction Objects, approved by the Resolution of the Cabinet of Ministers of Ukraine No. 461, dated April 13, 2011, "Issues of Acceptance into Operation of Completed Construction Objects" (Official Bulletin of Ukraine, 2011, No. 32, Art. 1359; 2015, No. 78, Art. 2599).

#### **Appendix A4. The legal framework for cooperation between local authorities and IFIs**

- The Law of Ukraine, "On Investment Activity", serves as the fundamental legislation governing investment practices within the country. This law establishes the legal framework for investment procedures, rights, and obligations of investors, as well as incentives and protections for both domestic and foreign investors. It aims to create a favourable investment climate, promote economic growth, and protect the interests of investors operating in Ukraine;
- The Law of Ukraine, "On the Regime of Foreign Investment", governs the legal framework for foreign investment activities within Ukraine. This law outlines the rights, obligations, and procedures for foreign investors operating in the country, aiming to create a conducive environment for foreign investment while ensuring protection and fair treatment for investors. It covers various aspects such as investment guarantees, repatriation of profits, dispute resolution mechanisms, and incentives for foreign investors;
- The Budget Code of Ukraine, particularly Article 74, which delineates local borrowing and the provision of local guarantees;
- Resolutions of Cabinet of Ministers №110 and №541 outline procedures for local borrowing and providing local guarantees;
- Resolution of Cabinet of Ministers №70 focuses on the procedural aspects of preparing, executing, monitoring, and completing projects for the economic and social development of Ukraine, with support from international financial organisations;
- Resolution of Cabinet of Ministers №153 establishes the procedure for raising, using and monitoring international technical assistance, including the state registration, monitoring of projects (programs), accreditation of performers (non-resident legal entities), and registration of the representation of the donor institution in Ukraine.