

INCOME TAX AS A COMPONENT OF FINANCIAL CAPACITY OF NEW AMALGAMATED COMMUNITIES IN UKRAINE

Summary

The influence of the state tax mechanism on the formation of the income part of communities is substantiated. It is noted that the decentralization reform largely shifts the provision of social services and ensuring the quality of life of its citizens to local governments. It is established that on the way to achieving the independence of territorial communities there are obstacles at the national and local levels. In order to establish a correlation between the effectiveness of the tax mechanism of regulating the income of the population and the financial capacity of local communities, the regulatory framework and taxation practices in EU countries were studied. The budget-forming role of personal income taxes in the formation of local budget revenues has been established. The shortcomings of the modern tax mechanism for regulating the income of the population have been identified and directions for its improvement have been proposed.

Keywords: state regulation, tax capacity, personal income tax, household income, tax mechanism.

PRZYCHODY Z PODATKU DOCHODOWEGO OD OSÓB FIZYCZNYCH JAKO PODSTAWA ZDOLNOŚCI NOWYCH ZJEDNOCZONYCH WSPÓLNOT TERYTORIALNYCH NA UKRAINIE

Abstract

W ramach artykułu udowodniono wpływ krajowego systemu podatkowego na kształtowanie się części dochodowej gromad (gmin). Wykazano, że reforma decentralizacyjna w znacznym stopniu przenosi świadczenie usług socjalnych i zapewnienie jakości życia obywateli na samorządy lokalne. Wyniki badania wskazują, że na szczeblu krajowym i lokalnym istnieją przeszkody na drodze do autonomii gromad terytorialnych. W celu ustalenia korelacji między skutecznością mechanizmu podatkowego regulującego dochody ludności a możliwościami finansowymi gromad lokalnych preanalizowano ramy regulacyjne i praktyki podatkowe w krajach UE. W badaniu określono rolę podatku PIT w kształtowaniu dochodów budżetu lokalnego. Zidentyfikowano braki nowoczesnego mechanizmu podatkowego regulującego dochody ludności i zaproponowano kierunki jego poprawy.

Słowa kluczowe: zarządzanie publiczne, zdolność podatkowa, podatek dochodowy od osób fizycznych, dochody gospodarstw domowych, mechanizm podatkowy.

НАДХОДЖЕННЯ ВІД ОПОДАТКУВАННЯ ДОХОДІВ НАСЕЛЕННЯ ЯК ОСНОВА ФІНАНСОВОЇ СПРОМОЖНОСТІ ОБ'ЄДНАНИХ ТЕРИТОРІАЛЬНИХ ГРОМАД УКРАЇНИ

Анотація

Обґрунтовано вплив державного податкового механізму на формування дохідної частини громад. Відзначено, що реформа децентралізації значною мірою перекладає на органи місцевого самоврядування надання соціальних послуг та забезпеченні якості життя її громадян. Встановлено, що на шляху до досягнення самостійності територіальних громад є перепони загальнонаціонального та місцевого рівнів. З метою встановлення кореляції між ефективністю податкового механізму регулювання доходів населення та фінансовою спроможністю територіальних громад, досліджено нормативну базу та практику оподаткування в країнах ЄС. Встановлено бюджетоутворюючу роль податків з доходів населення у формуванні доходів місцевих бюджетів. Визначено вади сучасного податкового механізму регулювання доходів населення та запропоновано напрямки його вдосконалення.

Ключові слова: державне регулювання, податкова спроможність, податок на доходи фізичних осіб, доходи населення, податковий механізм.

Significant changes in the local self-government system have taken place in Ukraine during last few years. It's connecting with formation of local budgets and a new powerful local self-government entity – United Territorial Communities (hereinafter referred to as UTC). Decentralization has become a real opportunity for the economic recovery of Ukrainian cities and villages. The established communities received considerable financial resources as an opportunity to manage their money independently.

Analysis of recent research and publications. The issue of revenue generation of the budgets of the united territorial communities in the context of ensuring the implementation of the commitments is in the center of attention of a number of Ukrainian representatives of economic and financial science. Thus, many of them advocate for certain level of financial independence of communities, believing that local budgets are central to the economic system of each state (Balatsky [1]), that decentralization is a very progressive and effective form of public

¹ Balackij Y. O. *Byudzhet mista u sistemi finansiv teritoriji* : monografiya. Sumi : DVNZ "UABS NBU", 2011. 302 s.

finance, when distribution system between different levels of the budget system constructed properly and harmoniously (Buryachenko [2]). The main aspect of decentralization is transferring of powers and resources to the level of local governments to best meet the social needs of local residents (Kravtsiv, Storonyanska [3]), as well as diversification of sources of income (Lunina, Kirilenko, Luchka [4]). We also find a positive perception of the idea of budget federalism in world authors: Wallace E. Oates [5], Barry R. Weingast [6], Roderick MacKinnon [7].

The aim of the study is to establish a correlation between the effectiveness of the tax mechanism for regulating the income of the population and the financial capacity of local communities.

1. The Main Part

The author of the concept of decentralization R. Prud'homme in his work *The Dangers of Decentralization* (1995) [8], however, points to the following risks: increasing the uneven socio-economic development of territories; complicating the implementation of macroeconomic policy; possible reduction of the efficiency of the socio-economic system (in various manifestations) and intensification of corruption at the local level. At the same time, each of the listed authors takes the position that the beneficial effect that can be obtained from decentralization depends on an individual country or community. It is an incentive to reduce differentiation through increased transparency in the allocation of budgetary resources and the effectiveness of equalization mechanisms.

According to the European Charter of Local Self-Government [9], the main feature of the financial independence of local authorities is the availability of the financial resources they need to carry out both of their own and delegated powers. The government still provides targeted financial support to newly created communities, because taxability of the territories is different and it helps to empower opportunities for giving social services. In this way, the principle of subsidiarity, as enshrined in the current legislation, is maximally achieved. At the same time, the issue of adequacy of the available financial resources to meet the full needs of the community is urgent, as well as the search for possible sources for their expansion, as it is not enough just to collect taxes at present, it

² Buryachenko A. Y. *Funkcionalna decentralizaciya ta vdoskonalennya sistemi byudzhetnih vidnosin* / A. Y. Buryachenko // *Finansi*, 2014, № 2, S. 19-29.

³ *Teritorialni gromadi v umovah decentralizaciyi: riziki ta mehanizmi rozvitku: monografiya* / za red. Kravciva V. S., Storonyanskoyi I. Z. Lviv: DU «Institut regionalnih doslidzhen imeni M. Dolishnogo NAN Ukraini, 2020, 531 s. (Seriya «Problemi regionalnogo rozvitku»).

⁴ Lunina I. O., Kirilenko O. P., Luchka A. V. *Diversifikaciya dohodiv miscevih byudzhetiv* / [Lunina I. O., Kirilenko O. P., Luchka A. V.] ; za red. d.c.n. I. O. Luninoyi ; NAN Ukraini ; In-t ekon. ta prognovuz. – K., 2010, 320 s. : tabl., ris.

⁵ Oates W. *Fiscal Federalism*. New York: Harcourt Brace Jovanovich, 1972.

⁶ Weingast B. *The Economic Role of Political Institutions: Market-Preserving Federalism and Economic Development*. *Journal of Law, Economics, and Organization*. 1995. Vol. 11 (1). P. 1.

⁷ McKinnon R. *EMU as a Device for Collective Fiscal Retrenchment*. *American Economic Review*. 1997. Vol. 87(2). Pp. 227–229. URL: http://www.jstor.org/stable/2950920?seq=1#page_scan_tab_contents [odczyt: 25.10.2020]

⁸ Prud'homme R. *The dangers of decentralization*. *The World Bank Research Observer*. Vol. 10(2). 1995. Pp. 201-220. URL: <http://documents.worldbank.org/curated/en/602551468154155279/pdf/770740JRN0WBRO0Box0377291B00PUBLIC0.pdf> [odczyt: 25.10.2020]

⁹ *Yevropejska hartiya pro misceve samovryaduvannya, ratifikovana Zakonom Ukraini № 452/97 – Verhovna Rada vid 15.07.97 – [Elektronij resurs] – Rezhim dostupu: http://zakon2.rada.gov.ua/laws/show/994_036 [odczyt: 25.10.2020]*

is necessary to provide high-quality administrative and social services in the field, than to provide citizens and taxpayers incentives for development in this particular territory.

On the other hand, a market economy and open borders can create additional problems. Thus, European practice shows that the mobility of factors of production, firms and individuals between euro area countries can lead to erosion of the tax base [10]. This encourages governments to compete for taxpayers within a country, often by lowering tax rates for taxpayers in order to attract more taxpayers. According to modern economists (Richard Musgrave, Pierre Salmon [11, p. 4]), this mobility prevents governments from pursuing policies that they (economists) find useful – such as social or redistributive.

We conclude that the tax independence of territories is the basis for the development of an individual community, so it is important to study the issue of tax capacity of communities and territories. According to the government portal [12], the main goal of decentralization reform is forming an effective local self-government and territorial organization of government for creating and maintaining a full-fledged living environment for citizens, which include: providing high-quality and accessible public services, establishing institutions of direct democracy, harmonizing the interests of the state and territorial communities. Thus, the reform aims at shifting responsibility to voters to local governments for the efficiency of their work, that is, in fact, undermining the role of the state in the processes of providing social services and ensuring the quality of life of its citizens. *However, on the way to achieving such independence there are several obstacles at the national (instability of the legal framework, redistribution of tax revenues) and local (tax capacity of territories, investment attractiveness of regions and the level of local infrastructure) levels. The complex of the specified problems is supplemented by one more important factor – efficiency of administrative decisions.*

The above problems of national scale are the cause of problems at the local level. Thus, the unstable legal framework leads to a decrease in *the investment attractiveness of the regions*, and the mechanism of crediting tax payments to local budgets is closely correlated with *the tax capacity of the territories*. Although the level of *local infrastructure* development depends on the amount of financial resources involved, it is largely related to the effectiveness of management decisions. For example, Angus Deaton, winner of the 2015 Nobel Prize in Economics for the Study of Consumption, Poverty and Welfare, [13] believed that in order to achieve economic prosperity it is necessary to increase the state's capacity, and economic aid does not contribute to this, and even more disaster than positive change. He explains that the backwardness of

¹⁰ Eurostat Statistical Book. *Taxation trends in the European Union. Data for the EU Member States, Iceland and Norway*. Luxembourg: Publications Office of the European Union, 2018. – 302 p. Elektronnij resurs. Rezhim dostupu: https://ec.europa.eu/taxation_customs/sites/taxation/files/taxation_trends_report_2018.pdf [odczyt: 27.10.2020]

¹¹ Pierre Salmon *Decentralization and Supranationality: The Case of the European Union* // <https://www.imf.org/external/pubs/ft/seminar/2000/fiscal/salmon.pdf> [odczyt: 25.10.2020]

¹² Yedinij veb-portal organiv vikonavchoyi vladi [Elektronnij resurs]. – Rezhim dostupu: <https://www.kmu.gov.ua/diyalnist/reformi/efektivne-vryaduvannya/reforma-decentralizaciyi> [odczyt: 01.11.2020]

¹³ Ekonomika otdelnogo cheloveka Chem izvesten laureat Nobelevskoj premii Engus Diton: Vox <https://meduza.io/feature/2015/10/12/ekonomika-otdelnogo-cheloveka> [odczyt: 26.10.2020]

countries is not due to lack of resources, but to poor governance, because the inflow of money only reduces the incentives of their governments to reform institutions and promote growth.

By *instability of the tax base* we mean frequent changes that are made to regulations governing primarily the procedure for collecting taxes and fees, as well as their redistribution between different levels of local budgets. Such circumstances not only do not allow to make realistic long-term plans for the development of territories, but also reduce their investment attractiveness to domestic and foreign investors.

According to changes which were made to the Budget Code of Ukraine, the united territorial communities have at their disposal a number of financial resources (see Table 1).

Table 1. The Financial Resources of the United Territorial Communities

Taxes	Fees and other charges	Other income
– 60% of tax on personal income	– tourist tax	– official government transfers
– excise tax on sales of excisable goods by retailers	– parking fees for vehicles	– own revenues of budgetary institutions
– corporate income tax for enterprises and financial institutions	– fees for licenses and certificates for certain types of business activities	– targeted and voluntary contributions of businesses, institutions, organizations and citizens to local environmental funds
– single tax	– State Duty	– local borrowing
– 25% of environmental tax	– 3% of rent on using mineral resources for the extraction of oil, natural gas and gas condensate	– revenues from assistance programs and grants from international financial institutions and the European Union
– property tax	– 5% of rent for using of mineral resources for mining of national value	– funds from the sale of landless property, finds, hereditary property
	– 37% of rent for special use of forest resources in the part of timber harvested in the order of logging	– repayment of loans from local budgets to individual rural developers, young families and single young people for construction and purchase of housing, as well as penalties and interest for their use
	– 30% of rent for the use of amber for the extraction of amber	– other income credited to the UTC
	– 75% of the compensation for losses of agricultural and forestry production	

Source: created by the author on the basis of the Byudzhetnij kodeks Ukrainy vid 08.07.2010 № 2456-VI (zi zminami ta dopovnenniyami) [Elektronnij resurs]. – Rezhim dostupu: <http://zakon3.rada.gov.ua/laws/show/2456-17> [odczyt: 03.11.2020]

As can be seen from Table 1, only six taxes form the tax revenues of the budgets of territorial communities, four of them depend on private business, the other two – on individuals. In the general structure of revenues (excluding intergovernmental transfers), the share of revenues from personal income tax is the largest and tends to increase and in 2019 was about 60.0% (2015 – 53.7%) [14]. Thus, if we do not take into account the volume of intergovernmental transfers,

¹⁴ Oficijnij sajt Ministerstva finansiv Ukrainy / Vikonannya dohodiv miscevih byudzhetiv <https://mof.gov.ua/uk/vykonannya-dokhodiv-misesevykh-biudzhetiv> [odczyt: 03.11.2020]

the main source of revenue of the general fund of local budgets are tax revenues, among which the personal income tax plays a key role.

We conclude that the size of wages and the transparency of their payment significantly affects the amount of tax revenues to local budgets. At the same time, these two indicators are significantly influenced by the national income policy, which should take into account the global tendencies to deepen the processes of globalization, democratization of governance and informatization, on the one hand, and indicators of socio-economic development within the country on the other. Public administration is adapting to the following conditions, which today must fulfill a number of “new functions”:

- a socially oriented market economy with an accent on the needs of the individual;
- search for additional sources of revenues for the implementation of the main socio-economic functions of the state in order to implement the principle of fiscal sufficiency;
- decentralization of public administration and keep the principle of subsidiarity in social services;
- increasing the participation of the taxpayer in the decision-making processes;
- overcoming inequality of income distribution in society, solving the problem of fairness of taxation and distribution of tax burden;
- improvement and optimization of the tax system according to the challenges of today;
- promoting the equivalence of the exchange of taxes on goods;
- reducing the level of shadow economy.

Today, we are looking for a way to integrate neoclassical (monetarist) and Keynesian models to create a new tax theory that incorporates the positive elements of different areas of financial science, developed in the past, and takes into account current global challenges and “new functions” of the state. The change in the accents of state regulation of population income is manifested in the reorientation of administrative and command functions to social protection.

Among the priority areas are the following functional changes, such as:

1. providing the conditions for earning income and create an equal opportunities for the equitable distribution of income;
2. implementation of social programs of structural reorientation of the economy, focused on housing, education, health care, as well as on supporting the sectors which provide social development;
3. conducting a sound policy of combining taxation with social support.

Therefore, the state is a necessary and indispensable regulator of the redistribution of income in society and of all socio-economic processes in the country, and it should also carefully

consider the tax policy, which is detailed in the tax mechanism. At the same time, without increasing interest in attracting as much financial resources from newly created local self-government bodies, the community budgets will not increase. In order to effectively plan the revenue part of the UTC budgets and facilitate its filling, local authorities should cooperate with the fiscal authorities, ensure that taxpayers fulfill their tax obligations in a timely manner, promote the level of voluntary compliance by taxpayers with the obligations, and avoiding official payroll, etc [15, p. 1260]. On the other hand, communities need to constantly improve the quality and accessibility of social services, improve the living conditions of citizens in order to create comfortable living conditions and generate income within the territory of a single united community. The degree of satisfaction of the socio-cultural needs of the inhabitants of such territories depends on the degree of efficiency of use of financial resources of the community.

2. European Experience

Decentralization reform in Ukraine is being implemented within the framework of the European Charter of Local Self-Government, signed by a number of European countries on October 15, 1985 in Strasbourg. It declares the right and ability of local governments within the law to regulate and manage a substantial proportion of public affairs, under their own responsibility, in the interests of the local population [16, Art 3].

If we talk about improving the mechanism of state regulation of population income, it is a good idea to explore the positive European experience. The main focus of such regulation is on primary income, particularly wage income, and the most common instruments of such regulation are usually tax rates, tax bases, tax benefits and tax rebates. In order to strengthen the financial capacity of local budgets, not only national income tax rates but also local ones apply in a number of EU countries (eg Sweden, Italy, Belgium, Denmark). However, because of secondary income taxation, EU countries are resorting to expanding their tax base. Tax pressure on wage income in developed countries is much higher than in transition economies, and *the government policy of regulating population income in EU countries has the following trends:*

- ensuring a fair and efficient redistribution of national income (through the removal from the tax base of a fixed amount of income, a broad tax base and the use of such instruments as progressive tax rates (in most EU countries), tax breaks and discounts);
- differentiated approach to taxation of different income groups (not only by type of income, but also by payer's social status);
- encouraging citizens to start families and have children;
- stable and transparent tax conditions, high tax culture;

¹⁵ Hrupovich S. *Finansova spromozhnist' byudzhetiv ob'yednanih teritorialnih gromad* / S. Ye. Hrupovich, T. V. Podvirna // *Ekonomika i suspilstvo*. – 2017. – Vip.13. – S. 1259-1262. [Elektronnij resurs]. – Rezhim dostupu: http://www.economyandsociety.in.ua/journal/13_ukr/209.pdf [odczyt: 27.10.2020]

¹⁶ Yevropejska hartiya pro misceve samovryaduvannya, ratifikovana Zakonom Ukrainy № 452/97 – Verhovna Rada vid 15.07.97 – [Elektronnij resurs] – Rezhim dostupu: http://zakon2.rada.gov.ua/laws/show/994_036 [odczyt: 27.10.2020]

- creating favorable conditions for income generation and payment of taxes within one country;
- compulsory payment of social security contributions;
- stimulation of business development among the population;
- implementation of high standards in the areas of population employment, labor productivity and social cohesion;
- the preservation and multiplication of general welfare.

An analysis of the practice of income taxation in EU revealed that all of them reformed the tax mechanism of government regulation of this income group, mainly by adjusting the tax burden through changes in tax rates, broadening the tax base, changing the list of tax benefits and simplifying tax benefits. Today, such regulation is marked by its dynamism, because it occurs in the conditions of intensification of the interstate competitive environment, democratization of management, increase of risks, uncertainty and asymmetry of information, which can be attributed to the main threats to the tax state regulation of population income in EU countries.

Taking into account the principle of nation-building without borders and the priorities of the development of the European Union, the tax policy of the member states is complemented by the social one. The synergistic effect of the realization of their basic tasks is intended to build an economy of public welfare, which should create not only comfortable conditions for the allocation of labor resources and taxation of the income of the population, but also provide a high level of state social protection for all citizens.

Unfortunately, the policy of state regulation of income in Ukraine today is accompanied by a reduction in public spending on social payments from the state budget, which in the long run will not help achieve the goals of fairness of taxation, poverty eradication and human capital development.

3. The Realities of the Domestic Practice of Taxes on Income

The income tax system in Ukraine has undergone significant changes and resembles similar systems in the Euroregion for the most part. This correspondence is evident in the similarity of the construction of the tax mechanism, administration procedures and a set of tools for regulating the income of the population. The main levers of influence on the regulation of the income of the population are: the tax base, the scale of taxation, tax rates, tax benefits and discounts, the minimum level of income and expenses to support the life and work qualities of the individual, as well as the amount of non-taxable income.

However, there are some disparities in regulation that have little effect on changing the degree of uneven distribution of income and the level of tax burden that are important to eliminate in order to increase the socially equitable level of income distribution in society. *The main ones include:*

1. low level of official employment of the population aged 15-70 – 56,1% [17]. This means that almost every second person of working age does not work or is employed informally, which leads to a significant “shadowing” and lack of tax revenues.
2. high rate of aging of the nation (we have 11.9 million pensioners [18] (of which more than 75% of pensioners receive retirement benefits by age) and 16.2 million officially employed persons [19] (January 1, 2017). Thus, there are 7 pensioners on every 10 employees.
3. low life expectancy compared to the euro area countries;
4. the low level of minimum social standards in Ukraine, as well as the significant influence of the inflation factor on the level of real incomes of the population;
5. lack of a differentiated approach to taxing the income of the population;
6. an imbalance of economic, social and political factors that have made it impossible for people of working age to find work in Ukraine or their income levels are insufficient to meet basic family needs. This generates poverty among employees, which is partially eliminated by the state by redistributing transfers for the benefit of the population, which may fall into privileged categories on certain grounds. Low monthly income transforms human psychology and makes a habit of living in poverty.

All this leads to impoverishment of the population. Yes, UN representative Neal Walker said [20] in 2017 that Ukraine’s poverty rate is 60% of the total population. He explained that according to the World Bank’s estimate, the poverty line is a standard income of \$ 5 per day, which for Ukrainians is about 4000 UAH per month in 2019 prices. Retirees (the average retirement benefit of which is less than twice the limit) and internally displaced persons with disabilities (about 4.5 million people) are in the risk zone. This is confirmed by the statistics of the State Statistics Committee for 2017, according to which the average per capita equivalent total income for 67.4% of Ukrainians was lower or equal to the above limit (UAH 4080 per month) [21]. Neal Walker also noted that in 2017, the minimum wage, which for Ukrainians is less than the poverty line by 20%, is also not met by UN standards. On July 17, 2018, World Bank Director for Ukraine, Belarus and Moldova – Satu Kahkonen also declared a high poverty rate in Ukraine – about 25%, and pointed to its increase for the last 4 years by up to 10% [22].

¹⁷ Oficijnij veb-sajt Derzhavnogo komitetu statistiki Ukrayini [Elektronnij resurs]. – Rezhim dostupu : <http://www.ukrstat.gov.ua> [odczyt: 26.10.2020]

¹⁸ Oficijnij veb-sajt Pensijnogo fondu Ukrayini [Elektronnij resurs]. – Rezhim dostupu : <http://www.pfu.gov.ua> [odczyt: 26.10.2020]

¹⁹ Oficijnij veb-sajt Derzhavnogo komitetu statistiki Ukrayini [Elektronnij resurs]. – Rezhim dostupu : <http://www.ukrstat.gov.ua> [odczyt: 26.10.2020]

²⁰ *V OON nazvali riven bidnosti ukrajinciv // Internet-izdanie MIR* [Elektronnij resurs]. – Rezhim dostupu : <https://iamir.info/47954-voon-nazvali-uroven-bednosti-ukrajincev> [odczyt: 27.10.2020]

²¹ Oficijnij veb-sajt Derzhavnogo komitetu statistiki Ukrayini [Elektronnij resurs]. – Rezhim dostupu : <http://www.ukrstat.gov.ua> [odczyt: 27.10.2020]

²² *Svitovij bank pidrabuvav kilkist bidnih v Ukrayini / Internet-portal «Slovo i Dilo»* [Elektronnij resurs]. – Rezhim dostupu : <https://www.slovodilo.ua/2018/07/18/novyna/suspilstvo/svitovij-bank-pidrabuvav-kilkist-bidnyx-ukrayini> [odczyt: 01.11.2020]

The disappointing statistics are confirmed by the indices of poverty individually determined by the World Bank, the International Monetary Fund and the United Nations, according to which Ukraine in 2018 was ranked 25th among 126 countries in the world with GDP per capita – 2638 \$ USA [23].

Today, the direct tax burden on wage income in Ukraine is equivalent to a tax rate of 18%. The EU-28 average is just around 12.5% [24, p. 30], above Ukraine's only in Belgium (16.5%), Germany (17.5%), Sweden and Ireland (19.5%), as well as Denmark (up to 34.0%). In addition, Eurostat annually calculates an average implicit tax rate on labor (ITR), which in addition to the basic rate of income tax, takes into account insurance contributions and other payroll taxes, paid not only by employees but also by employers. In 2016, the EU-28 average ITR was 34.3% [25, c. 249]. It was highest in Italy (42.6%), Belgium (42.4%) and Hungary (41.6%), the lowest in Bulgaria (23.5%), Malta (23.8%) and Cyprus (25.6%). The Ukrainian indicator varies depending on the industry and the employee category, but in most cases it is quite high and is in the range of 50-56% [26; 27].

The reforms implemented in Ukraine aim to change the nature of state participation in economic activity, reduce the share of state property, create economic conditions to ensure high business activity and reduce the differentiation of income. However, there are many threats to obtaining a positive economic effect from the reform of the tax system related to the risks of the development of public finances of Ukraine, including: increase of public debt, decrease in the rate of mobilization of revenues to the state budget, increase of the state budget expenditures and corresponding increase deficit, significant level of shadowing of the economy (about 30% of GDP in 2018 [28]).

In the sphere of state regulation of the income of the population the following problems are distinguished:

1. defects of the tax mechanism:

- uneven distribution of income in society (most citizens receive official incomes below the national average);
- lack of differentiated approach to taxation (depending on the amount of income);

²³ *The Poorest Countries in the World* [Електронний ресурс]. – Режим доступу : <https://www.focus-economics.com/blog/the-poorest-countries-in-the-world> [odczyt: 01.11.2020]

²⁴ *Eurostat Statistical Book. Taxation trends in the European Union. Data for the EU Member States, Iceland and Norway*. Luxembourg: Publications Office of the European Union, 2018. – 302 p. Elektronnij resurs. Rezhim dostupu : https://ec.europa.eu/taxation_customs/sites/taxation/files/taxation_trends_report_2018.pdf [odczyt: 01.11.2020]

²⁵ The same

²⁶ Podatkovij kodeks Ukrainy vid 02.12.2010 roku № 2755-VI v redakcii Zakonu № 3609-VI vid 07.07.2011 roku / Verhovna Rada Ukrainy. [Elektronnij resurs]. – Rezhim dostupu : <https://zakon.rada.gov.ua/laws/show/2755-17> [odczyt: 01.11.2020]

²⁷ Zakon Ukrainy «Pro zbir ta oblik yedinogo vnesku na zagalnoobov'yazkove derzhavne socialne strahuвання» vid 8 lipnya 2010 roku № 2464-VI / Verhovna rada Ukrainy [Elektronnij resurs]. – Rezhim dostupu : <https://zakon.rada.gov.ua/laws/show/2464-17> [odczyt: 01.11.2020]

²⁸ *Tendenciyi tinovoyi ekonomiki v Ukraini u 2018 roci* // Oficijnij sajt Ministerstva rozvitku ekonomiki, torgivli ta silskogo gospodarstva Ukrainy / <https://www.me.gov.ua/Documents/List?lang=uk-UA&cid=c384c5a7-6533-4ab6-b56f-50e5243eb15a&tag=TendentsiiTinovoiEkonomiki> [odczyt: 02.11.2020]

- even distribution of the tax burden on the income of the population, regardless of the amount of income (contrary to the principle of social justice taxation);
 - the main fiscal pressure of taxation is on primary income, especially from wages;
 - lack of a real regulatory role for the non-taxable minimum income of citizens;
 - a high level of total average tax burden on household incomes;
 - the imperfection of the preferential mechanism because of the low income threshold to which they apply (for example, the tax social privilege can be used for couples raising two or more children under the age of 18).
2. economic development defects affecting public revenue policy:
- a low living standards and high levels of poverty among the population;
 - significant influence of state transfers on the formation of total income of the population;
 - a low level of minimum social standards (living wage and minimum wage);
 - a low level of social services due to inefficient mechanism of collecting and using funds to trust insurance funds;
 - a low level of official employment;
 - significant influence of inflationary processes on the nominal income of the population.

4. Steps to Improving Income Taxation

Considering the fact that the reform should not be radical and cover many areas, we propose to distribute it according to urgency and time lag, using an iterative (gradual) approach to change. In addition, changes in the taxation mechanism are possible only on a national scale, but, of course, have an effect on the amount of tax revenues at the local level. So:

1. in the short term (up to 3 years) it is proposed:
 - 1.1) introduce a mechanism for accounting for tax benefits through the development of a centralized automated system. This will increase the efficiency of public finances management, allow to have operational data on budget losses from the application of the preferential mechanism in the context of taxpayers and amounts of financial resources. The proposed practice is not new and has long been applied in many EU countries (Belgium, Germany, Estonia, Spain, France, Italy, Netherlands, Austria, Portugal, United Kingdom, Finland, Bulgaria, Denmark, Latvia, Hungary, Poland, Sweden) [29] and is being implemented within the concept budget spending. Therefore, exchange of positive experience will allow to implement the most suitable European practice for Ukraine and save

²⁹ Tax reforms in EU Member States: tax policy challenges for economic growth and fiscal sustainability : 2013 report [Elektronnij resurs]. – Rezhim dostupu : http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_papers/taxation_paper_38.pdf [odczyt: 03.11.2020]

time for its development and testing. In addition, the publicity of the preferential mechanism is one of the OECD recommendations for developing countries to promote investment.

- 1.2) provide employers with a tax deduction for paying young workers who are hired for the first time.

Today, Article 26 of the Law of Ukraine “On Employment of the Population” provides for stimulating employment of citizens who are not competitive enough in the labor market. The categories of citizens who have additional guarantees in favor of employment under Article 14 of this Law include “youth who have graduated or stopped education in general, vocational and higher education institutions, have been dismissed from conscription or non-military (non-military) service and who is first hired”. However, such a “job candidate” must meet a number of requirements:

- to be registered as unemployed in the territorial central body of executive power, which implements state policy in the field of employment and labor migration;
- get a job not later than 6 months after graduation or termination of study or service;
- to be hired for the first time.

Also important is the fact that the employer receives such a benefit provided that a new job is created and one of the categories of citizens referred to in Article 14 of the Law is hired for a period of not less than two years. Otherwise, he will not be able to use this type of benefits. On the one hand, the condition for creating a new job is fair, as it aims to increase the actual number of jobs, but it does not satisfy the condition of stimulating employment of citizens who are not competitive in the labor market, in particular young people. The question of the minimum period of employment for 2 years does not raise any objections, because it prevents the speculative nature of the application of this type of benefits by the employer.

Considering the above, we propose to adjust the mechanism of application of privileges as follows (Table 2):

Table 2. Comparative Characteristics of the Improvement of the Proposed Type of Benefits

The current Law on Employment of the Population of Ukraine	Draft amendment
Article 14. Categories of citizens who have additional guarantees in favor of employment	
Item 4 Part 1:	
4) young people who have completed education in general, vocational and higher education institutions, have retired from conscripts or alternative (non-military) service (within six months of graduation or termination of education or service) and are first employed;	4) young people who have graduated or stopped studying at general, vocational and higher education institutions, have retired from consecutive military or alternative (non-military) service (within twelve months after graduation or termination of study or service) and who are first employed;
Article 26. Stimulating the employment of citizens who are not competitive enough in the labor market	

The current Law on Employment of the Population of Ukraine	Draft amendment
1. An employer who is recruiting for the new workplace of citizens specified in part one of Article 14 of this Law (except those defined in paragraph 7 of Part One of Article 14) and who has been granted the status of unemployed, at the direction of territorial bodies of the central executive body, which implements the state policy in the sphere of employment and labor migration, for a period of not less than for two years monthly the actual expenses in the amount of a single contribution to obligatory state social insurance for the respective person are compensated for the month for which it was paid.	1. An employer who is recruiting for the new workplace of citizens specified in part one of Article 14 of this Law (except those defined in clause 4 and clause 7 of part one of Article 14) and who has been granted the status of unemployed, at the direction of territorial bodies of the central executive body authorities implementing the state policy in the field of employment and labor migration, for a period of not less than two years, are compensated for the actual costs of a single contribution to the compulsory state social insurance Vienna person per month, for which he paid. An employer who employs a person for the first job for a period of not less than two years is compensated monthly for the actual costs of a single compulsory state social security contribution for the person concerned for the month for which he or she is paid.

* Created by the author

A somewhat similar mechanism has been implemented in Poland, where young people under the age of 26 who are officially employed in Poland are exempt from paying personal income tax. This exemption applies to a certain level of the total annual income of such a person (85,528 zlotys or about 20,000 US dollars in 2020), and in case of excess – the current tax scale is applied [30].

2. in the medium term (3-5 years):
 - 2.1) to establish the amount of monthly income from wages (other equals to it in accordance with the legislation of payment, compensation and remuneration), which will not be taxed, calling it the main tax social discount (it detailed in Table 3).

Table 3. The Mechanism of Applying the Basic Tax Social Privilege

Basic Social Privilege	Fixed monthly amount of tax deductible income
Taxpayers who can get a basic tax social privilege	<ul style="list-style-type: none"> – employees under the terms of the employment contract at the main place of work; – individual entrepreneurs; – independent professional or creative activity; – students, students, graduate students, interns, adjuncts
The tax base	Aggregate monthly income received by taxpayer categories eligible for basic tax discount
Period of use	Monthly
Procedure of using	<ul style="list-style-type: none"> – automatically for persons working under the terms of an employment contract (performed by a tax agent); – is independently excluded from the tax base by other taxpayers who have a right to receive a basic tax discount
Amount of basic tax social privilege	– one subsistence minimum for aggregate monthly income less than or equal to 3 minimum wages

* Created by the author

³⁰ Oficijnij veb-sajt Respubliki Polsha. [Elektronnij resurs]. – Rezhim dostupu : <https://www.gov.pl/web/finanse/bez-pit-dla-mlodych> [odczyt: 05.11.2020]

- 2.2) taking into account the experience of a number of European countries (Germany, France, Belgium, Hungary, Slovakia) and the European integration course of Ukraine, in order to enhance the role of marriage as a social institution and stimulate demographic growth, we propose to supplement for the purposes of taxation the provision of Article 169 of the Tax Code of Ukraine children in spouses, as follows: “If a spouse (single mother / father) is raising one or more children under 18, then one spouse (single mother / father) is entitled to a reduction in the amount of the total month taxable income (regardless of the amount of such income) received from one employer as a wage of one subsistence minimum for able-bodied persons for each such child.”

According to our calculations, the introduction of this type of privilege will maximally «cost» the state 2.6 billion UAH. per year (1% of total income from the personal income tax to the consolidated budget for 2018).

The introduction of the basic tax discount and privileges for families with children under the age of 18 will allow to abolish the tax social privileges provided by Article 169 of the Tax Code of Ukraine today: subparagraphs 169.1.1, 169.1.2, 169.1.3 and 169.1.4. Having only two tax social benefits optimizes the list of available benefits, minimizes accounting and inefficient budget expenditures, which is especially true in the face of budget deficit. On the other hand, the proposed way to change the preferential mechanism will improve the system of tax regulation of incomes towards increasing its efficiency, as well as contribute to a real reduction of the tax burden on low income from wages and give a real social effect of the existence of tax social benefits for the most vulnerable .

- 2.3) introduction of a diversified tax rate on income from wages, which will increase with each additional hryvnia of income.
3. in the long term (5-10 years):
- 3.1) Studies of tax systems in some European countries (eg Germany, Norway) have found that introducing a family approach to taxing personal income tax in Ukraine is now inappropriate. We consider that the current tax system of Ukraine is oriented and written from the point of view of taxation of one person, and in order to orient it to the family, it is necessary to rewrite the whole mechanism of taxation. However, given the experience of France, the USA, Germany, it is advisable to provide social benefits to the families as a subject of taxation. This would allow to left income in families with multiple dependents. The family would thus be able to make the most of the income earned by its able-bodied members, rather than counting on subsidies and other benefits from social security funds, etc. This will encourage the able-bodied population to increase their incomes legally and reduce the desire for dependency.

We are convinced that the gradual introduction of the proposed changes in the tax mechanism will help to improve the efficiency of personal income taxation and will help to reform the tax system towards improving its social orientation and fairness in taxation. We agree with Alla Sokolovskaya's opinion [³¹, p. 30] that within the framework of tax reform in Ukraine it is advisable to develop a strategy for its reform, including the short and medium term perspective, which is relevant in the context of medium-term budgetary planning. At the same time, we consider it advisable to carry out active educational and educational work in order to establish feedback from the state and society, as well as to involve the public in the processes of discussing economic transformations in the country.

5. Conclusions and Generalizations

Therefore, in the conditions of transformation of the state paradigm of regulation of the economy of the country, it is extremely important and necessary to effectively regulate the incomes of the population through the use of fiscal methods of influence. We consider that it is advisable to carry out the state policy of income redistribution in the following directions:

I. National level

1. Ensuring the stability of the legal framework in the field of taxation in order to stimulate business and business activity among the population and attract foreign investors;
2. Improving the effectiveness of budget planning as an important tool for balancing the allocation of financial resources of the country (by preventing «overfunding» of certain types of expenditures and «underfunding» of others), including to ensure the realization of citizens' constitutional rights by real provision of state social standards;
3. Creating an opportunity to earn a decent living (enough to restore the work potential and meet the socio-cultural needs of the individual), including by:
 - increasing the cost of labor (price) labor, increasing the share of labor costs in production costs;
 - increasing the number of jobs (including by restoration/expanding of production);
4. Improving the system of personal income taxation by differentiating the system of tax rates relative to the level of income;
5. Correlation of expediency of granting tax benefits with the real material and property condition of the taxpayer and introduction it according to their granting (for example, travel, food, accommodation, etc.);

³¹ Sokolovska A. M. *Koncepcija liberalnoyi podatkovoyi reformi: docilnist i mozhlivist realizaciyi v Ukraini* / A. M. Sokolovska // *Finansi Ukraini*, 2015, № 12, S. 12-31. [odczyt: 06.11.2020]

6. Governmental programs of financial support for the development of small and medium business;
7. Creation of a single consolidated database of taxpayers in order to identify the taxpayer in order to obtain the most probable and complete information about the material and public (education, marital status, family composition) status of each member of society and to create a system of real monitoring of living standards of different population groups;
8. Data on actual census for rendering realistic revenue and expenditure;
9. Political will to de-shadow the economy.

II. Local level

1. improving the efficiency of management decisions, especially in the use of budget funds;
2. constant work on de-shadowing of employment;
3. “uniform rules of the game” for all market participants in goods and services;
4. long-term community development plans and active work on attracting grants and investments.

To sum up, raising the standard of living of citizens is possible after overcoming a number of internal problems (shadow economy sector, corruption, devaluation of the hryvnia, lack of stable economic growth) and a number of challenges inherent to the domestic public and private sectors. At the same time, it is necessary to work towards improving the social orientation of the state power. We ourselves must build Europe in Ukraine by achieving a stable, secure, non-corrupt and prosperous economy. The government needs to change its vision of reform – not as a point and situational change in individual areas of economic activity, but as a strategic and prudent policy that has a complex nature of change.

In order to promote inclusive economic growth (the aggregate increase in the well-being of society, not individual groups or categories of citizens) and effectively combat the widening of income inequality, it is necessary to transform the country's tax policy in a way that involves the use of a progressive personal income tax scale, taxation of capital and profits, as well as strengthening the link between taxes paid and benefits received. This, in turn, will help to increase the level of voluntary payment of taxes and to fill the budgets of local territorial communities.

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