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Article

Strengthening the Financial Sustainability of Local Budgets Under Fiscal Decentralization: Evidence From Uzbekistan

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Abstract: This study examines the financial sustainability of local budgets in Uzbekistan within the framework of fiscal decentralization. It analyzes the theoretical foundations of local budget autonomy, recent budget reforms, and institutional mechanisms for strengthening local public finance. The study finds that improving tax collection efficiency, expanding local revenue sources, enhancing expenditure management, and increasing public participation are essential for ensuring the financial sustainability of local budgets. The findings provide policy recommendations for improving local budget management and promoting balanced regional development.

Keywords: local budget; fiscal decentralization; financial sustainability; financial autonomy; public finance; Uzbekistan.

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1. Introduction

Local budgets constitute an integral component of the national budget system and play a significant role in ensuring the country's economic stability, financial capacity, and balanced regional development. Their financial resources are formed through locally assigned revenue sources as well as allocations from national revenues in accordance with the existing legal framework. From this perspective, local budgets serve as one of the key indicators for assessing the financial sustainability of the budget system. In particular, they are essential for financing social sectors such as education, healthcare, culture, and public utilities, all of which directly influence the quality of life and living standards of the population.[1]

Differences among regions in terms of economic development, natural resource endowment, demographic characteristics, and social conditions further emphasize the importance of strengthening the revenue base of local budgets. Therefore, enhancing the stability of local budget revenues, expanding regional financial capacity, and reducing interregional fiscal disparities are among the primary prerequisites for increasing the financial independence of local governments.[2]

International practice demonstrates that local budgets are mainly financed through local taxes and fees. However, these financial resources are used not only to satisfy local needs but also to implement the government's socio-economic policies, particularly by supporting the maintenance and development of social infrastructure. Moreover, the effective management of local budgets contributes to increasing the accountability and motivation of local financial authorities in budget execution, ensuring the efficient and rational use of public funds, and encouraging the identification

of new sources of budget revenues.[3]

A review of the academic literature indicates that research on the financial independence of local budgets became more extensive during the late twentieth century. Nevertheless, an analysis of historical and economic studies suggests that the issue of maintaining a balance between local budget revenues and expenditures has long been recognized as one of the fundamental topics in public finance research.[4]

2. Methoddology.

Academic interest in local budgets, which serve as the principal financial plans of local government authorities, began to intensify in the 1950s. In particular, Charles M. Tiebout's article on the theory of local public expenditure introduced the idea that fiscal decentralization could enhance public welfare by allowing citizens to choose jurisdictions that best match their preferences for public goods and services. This theoretical approach laid the foundation for extensive academic discussions on the role and effectiveness of fiscal decentralization [5].

Building upon these studies, Richard A. Musgrave presented a comprehensive theoretical framework in his seminal work The Theory of Public Finance. In this publication, he offered the first systematic explanation of the characteristics of multi-level governmental systems, while also examining the functions, responsibilities, and operational mechanisms of the public sector within the framework of public finance theory [6]. According to the research of economist M. Goldsmith, the financial autonomy of local governments constitutes a fundamental prerequisite for the effective provision of public services. He argues that local authorities can better meet the needs of their communities by organizing territorial governance efficiently and managing their own financial resources in the most effective and accountable manner [7].

According to K. Beer-Tóth, the quality and quantity of public services provided within a country largely depend on the fiscal rules and incentive mechanisms that regulate the relationships among different entities of the public sector. In other words, the effectiveness of public service delivery is determined by the institutional design of intergovernmental fiscal relations and the incentives embedded within the public finance system [8].

Scholars from the Commonwealth of Independent States (CIS), particularly Russian economists, argue that the fundamental principle of fiscal decentralization is the transfer of decision-making authority and administrative responsibilities to local governments, enabling them to address issues that are closely associated with local needs and priorities more effectively [9].

Similarly, the Russian economist V. Lebedev emphasizes that local interests and priorities can be evaluated more accurately by local authorities than by the central government. This perspective supports the view that decentralized governance enhances the efficiency and responsiveness of public administration by allowing decisions to be made closer to the communities they affect [10].

Discussing the composition and structure of budget expenditures, Uzbek economists T. Malikov and N. Khaydarov argue that the nature and allocation of budget expenditures are determined by the characteristics of the state, the functions it performs, and the needs of the national economy. They further emphasize that the structure of public expenditures is shaped by the budgetary mechanism, which enables the government to influence various aspects of production and consumption through fiscal policy instruments [11].

According to economist Z. Srojiddinova, revising and improving the mechanisms of fiscal support would enhance the effectiveness of intergovernmental financial assistance by directing public resources toward regions with insufficient own-source revenues. Such an approach would contribute to maintaining the financial stability of economically weaker territories and reducing regional fiscal disparities [12].

In his studies on the public finance system, economist I. Alimov classifies the main sectors and components of the national financial system and identifies local finance as an integral element of public finance. He emphasizes that local budgets constitute the financial foundation of local governments and represent the core instrument through which local finance is organized and implemented [13].

According to A. Mamanazarov, expanding the financial capacity of local budgets requires the introduction of market-based financing instruments. In particular, he proposes issuing municipal securities backed by local budget revenues to finance projects of local importance, as well as establishing an appropriate legal framework that would enable local governments to raise funds through debt obligations [14].

In their research, A. Burkhanov and H. Kurbanov argue that the redistribution of revenues among different levels of the budget system is primarily driven by asymmetric disparities in the socio-economic development of regions. They maintain that ensuring the financial sustainability of local budgets should begin with strengthening the economic potential of individual regions and developing effective mechanisms for the efficient utilization of their available resources [15].

The studies of Uzbek economist A. Islamkulov provide a comprehensive analysis of the financial independence of local budgets. In his doctoral dissertation abstract, he defines the concept of local budget financial autonomy through specific criteria, emphasizing that local government authorities should be granted greater independence not only in determining the local tax base but also in setting tax rates. At the same time, he argues that the central government should retain overall supervisory authority to ensure consistency, accountability, and compliance with national fiscal policy objectives.

3. Analysis and results

The coordination of local budget revenues and expenditures plays a crucial role in promoting the balanced development of Uzbekistan and its regions while supporting the implementation of the national principle of "For Human Dignity." Fiscal decentralization requires not only structural reforms in the public administration system but also a substantial enhancement of the authority and responsibilities of local governments in budget management and public service delivery.

The integrity of the local budget system enables the state to consolidate financial resources within a unified public finance framework. Consequently, these resources cannot be regarded as belonging exclusively to any single level of the budget system but rather serve the broader objectives of national socio-economic development.

An effective local budget system allows regional needs to be identified more accurately and harmonized with centrally coordinated government policies. For this reason, local authorities have a direct interest in ensuring stable budget revenues and promoting the efficient and targeted use of financial resources. The pace of economic growth, social development, and cultural progress within each region largely depends on the mobilization of local resources and the rational allocation of public expenditures, which, in turn, contributes to the successful implementation of the State Budget of the Republic of Uzbekistan.

Maintaining a balance between local budget revenues and expenditures is a fundamental prerequisite for ensuring fiscal sustainability and organizing public financial activities efficiently. Achieving this objective represents one of the primary goals of the government's fiscal policy and is largely accomplished through the effective utilization of local budget resources.

The management of local budget expenditures should be determined not by the list of enterprises or institutions subordinated to local governments but by the public functions and responsibilities assigned to them. Since these responsibilities primarily involve the provision of services to local communities, they are commonly referred to as local public services. These include housing and communal services, public transportation, social and cultural services, public safety, urban improvement, environmental protection, and the maintenance of ecological sustainability within cities and districts. From this perspective, the local economy may be characterized as a service-oriented economy focused on meeting the needs of residents. Accordingly, the significance of local budgets is reflected in the essential functions they perform.

The principal functions of local budgets include the formation of financial resources required to support the activities of local government authorities, the allocation and utilization of these resources across various sectors of the regional economy, and the supervision of the financial and economic activities of enterprises, organizations, and institutions operating under the authority of local governments.

In conclusion, improving the efficiency of local budget expenditures requires distinguishing between the direct costs of public service provision and the administrative expenses associated with managing and delivering those services. Furthermore, strengthening the expenditure potential of local budgets requires not only establishing a clear legal framework governing local taxes and mandatory payments but also continuously evaluating and improving the distribution of national tax revenues allocated to local budgets. In addition, expanding the activities of small businesses and private entrepreneurship remains one of the most effective approaches to broadening the local revenue base and enhancing the financial sustainability of regional budgets.

Budgetary relations in the Republic of Uzbekistan are regulated by the Budget Code of the Republic of Uzbekistan, which establishes the legal framework governing the formation, preparation, review, adoption, approval, execution, and monitoring of the budgets within the national budget system. The Code also regulates government borrowing and the implementation of budget legislation. Furthermore, it clearly defines the revenue sources and expenditure responsibilities of both the republican budget and local budgets, including regional, district, and city budgets.

To strengthen the financial capacity of local governments, the Cabinet of Ministers of the Republic of Uzbekistan adopted Resolution No. 445 on 29 June 2017, which introduced comprehensive mechanisms for identifying additional reserves to expand the revenue base of local budgets. The Resolution specifies supplementary sources of local budget revenues and establishes institutional arrangements aimed at improving cooperation among financial authorities, tax authorities, and local executive bodies. These measures are intended to increase State Budget revenues by broadening the tax base and improving the effectiveness of tax administration.

The Resolution also approved detailed regulations governing the responsibilities of district and city finance departments, as well as local tax inspectorates, in ensuring the full implementation of the State Budget revenue targets. These regulations establish procedures for implementing measures designed to strengthen the revenue base of local budgets, improve revenue collection, and enhance coordination among public financial management institutions at the local level.

The Ministry of Economy and Finance of the Republic of Uzbekistan, together with the State Tax Committee, is responsible for conducting continuous monitoring of the mobilization of available financial resources. Based on the results of this monitoring, these institutions are required to ensure the implementation of measures aimed at achieving the approved State Budget revenue targets. Particular emphasis is placed on expanding the revenue base of local budgets, as this is considered a key prerequisite for maintaining the stable financing of national and regional development programs.

In addition, the First Deputy Chairperson of the Council of Ministers of the Republic of Karakalpakstan, the First Deputy Governors of regions, districts, and cities are entrusted with coordinating activities in cooperation with tax authorities, financial agencies, other relevant local government institutions, and commercial banks. Their primary responsibility is to identify additional revenue sources by taking into account the economic potential of each district and city. Through coordinated efforts to broaden the local revenue base, these authorities are expected to ensure the full implementation of the State Budget revenue targets while strengthening the fiscal sustainability of local governments.

In our view, ensuring the financial sustainability of local budgets should primarily rely on strengthening the collection efficiency of major taxes rather than increasing intergovernmental fiscal transfers. In this regard, the active participation of consumers, together with effective public oversight, plays a significant role in improving tax compliance and enhancing the transparency of revenue administration.

To encourage consumer participation in tax administration, Uzbekistan introduced a mechanism under which individuals are entitled to receive a refund equal to one percent of the value-added tax (VAT) included in the purchase price of goods and services acquired from retail trade, public catering, and household service providers. This policy aims to stimulate the issuance of fiscal receipts, reduce the size of the informal economy, and increase VAT collection, thereby contributing to the expansion of budget revenues.

Uzbekistan has also continued implementing fiscal decentralization reforms to strengthen the stability of the budget system. In particular, the budget legislation for 2026 establishes procedures for adjusting public expenditures when the six-month execution results indicate that approved revenue forecasts are unlikely to be achieved by the end of the fiscal year. Under these provisions, expenditure reductions amounting to 3 percent or more of the total expenditures of the republican budget are to be approved by the chambers of the Oliy Majlis upon the proposal of the Cabinet of Ministers. Conversely, expenditure reductions below 3 percent of the total republican budget expenditures may be implemented through a resolution of the Cabinet of Ministers based on a proposal submitted by the Ministry of Economy and Finance. These fiscal adjustment mechanisms are intended to preserve budgetary discipline, maintain macroeconomic stability, and enhance the resilience of Uzbekistan's public finance system under changing economic conditions.

In conclusion, the effectiveness of the legal norms established by the existing regulatory framework depends not only on their formal adoption but also on their practical implementation. Therefore, strengthening public oversight, as well as enhancing the supervisory role of local representative councils (Kengashes) and their deputies, would contribute significantly to ensuring the effective enforcement of these legal provisions.

Furthermore, it would be advisable to organize regular training programs and professional development courses for members of local representative bodies in order to improve their understanding of newly introduced legal norms, fiscal regulations, and budgetary reforms. Such capacity-building initiatives would enhance the quality of budget oversight and support more effective decision-making at the local level.

In addition, the implementation of these legal provisions should be subject to continuous monitoring, particularly at the regional and local levels. Regular assessment of their practical application would facilitate the timely identification of implementation challenges, improve policy effectiveness, and strengthen accountability and transparency within the system of local public finance management.

4. Conclusion

Based on the findings of the present study, the following conclusions can be drawn.

First, local budgets should be understood as centralized public financial funds that ensure the implementation of governmental functions and responsibilities within a particular territory. Therefore, increasing public awareness and improving citizens' understanding of the formation and utilization of local budget resources are essential for enhancing transparency and accountability in local public finance.

Second, the issue of the financial independence of local budgets represents a relatively new area of academic research and has not yet been sufficiently examined by either international or Uzbek scholars. This indicates the need for further theoretical and empirical investigations into the determinants and measurement of local fiscal autonomy.

Third, the concepts of financial sustainability and financial independence of local budgets are frequently interpreted inconsistently in the existing literature. In this study, financial independence is considered to be the ability of local government authorities to make autonomous decisions regarding the formation, allocation, and utilization of local budget resources within the framework established by national legislation.

Fourth, the legislative and regulatory reforms introduced in Uzbekistan's public finance system in recent years may be regarded as the initial stage of fiscal decentralization, creating institutional conditions for strengthening the role of local governments in budget management.

Fifth, the financial independence of regions should not be limited solely to the delegation of expenditure and revenue responsibilities. It is equally important to establish effective institutional and procedural mechanisms that enable local authorities to exercise these powers efficiently and responsibly.

Sixth, while expanding the budgetary powers of local representative councils, it is also necessary to strengthen public participation in the budget process. Broader citizen engagement in

budget planning, implementation, and oversight would contribute to greater transparency, accountability, and responsiveness of local public finance.

Seventh, improving the effectiveness of the budgetary powers delegated to local representative councils requires the organization of specialized training programs for local council members. Continuous enhancement of their financial literacy and knowledge of public budgeting would improve the quality of fiscal decision-making and strengthen budget oversight at the local level.

Overall, this chapter has examined the research topic from theoretical, conceptual, and methodological perspectives. The subsequent chapters focus on evaluating the current state of local budget revenues and expenditures in Uzbekistan, assessing the effectiveness of their utilization, and analyzing the mechanisms for generating and allocating surplus revenues at the regional level with a view to improving the financial sustainability of local budgets.

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