

ORIGINAL

Financial sources of support for economic development of territorial communities

Fuentes financieras de apoyo al desarrollo económico de las comunidades territoriales

Tetiana Dei¹  

¹Department of Finance and Credit, College of Information Technologies and Land Management, State University "Kyiv Aviation Institute". 03058, 1 Liubomyr Huzar Ave., Kyiv Ukraine.

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Corresponding Author: Tetiana Dei 

ABSTRACT

The article is aimed at highlighting the peculiarities of using various sources of financing for economic regional development of countries. This study uses various methods of scientific research, in particular, methods of economic and statistical analysis, description, systematization, logical generalization, induction and deduction. The article analyzes the revenues of local communities in the UK for the period 2017-2022. In particular, the structure of revenues, the distribution between communities' own revenues and grant funds were analyzed. The presentation of the Danish experience included an analysis of the local community financing system, including a map of the country, taking into account the implementation of the structural reform. Particular attention was paid to the main sources of funding: tax revenues and intergovernmental transfers. The rates of some local taxes as of 2024, such as municipal tax, church tax, labor market tax, and land tax, are systematized. Furthermore, the article describes and systematizes the experience of financing local communities in France, where tax revenue mechanisms, grant support, and financial equalization instruments that ensure the sustainable development of territorial communities are considered. The structure of local budget revenues for the period from January 1 to April 4, 2024 is examined using economic and statistical methods.

Keywords: Budget Revenues; Grant Support; Regional Development; Sustainable Development; Tax Revenues.

RESUMEN

El artículo tiene por objeto poner de relieve las peculiaridades de la utilización de diversas fuentes de financiación para el desarrollo económico regional de los países. Este estudio utiliza diversos métodos de investigación científica, en particular, métodos de análisis económico y estadístico, descripción, sistematización, generalización lógica, inducción y deducción. El artículo analiza los ingresos de las comunidades locales en el Reino Unido para el período 2017-2022. En particular, se analizó la estructura de los ingresos, la distribución entre los ingresos propios de las comunidades y los fondos de subvención. La presentación de la experiencia danesa incluyó un análisis del sistema de financiación de las comunidades locales, incluido un mapa del país, teniendo en cuenta la aplicación de la reforma estructural. Se prestó especial atención a las principales fuentes de financiación: los ingresos fiscales y las transferencias intergubernamentales. Se sistematizan los tipos de algunos impuestos locales a partir de 2024, como el impuesto municipal, el impuesto eclesiástico, el impuesto sobre el mercado laboral y el impuesto sobre el suelo. Además, el artículo describe y sistematiza la experiencia de financiación de las colectividades locales en Francia, donde se consideran los mecanismos de ingresos fiscales, las ayudas en forma de subvenciones

y los instrumentos de perecuación financiera que garantizan el desarrollo sostenible de las colectividades territoriales. Se examina la estructura de los ingresos presupuestarios locales para el periodo comprendido entre el 1 de enero y el 4 de abril de 2024 utilizando métodos económicos y estadísticos.

Palabras clave: Ingresos Presupuestarios; Subvención; Desarrollo Regional; Desarrollo Sostenible; Ingresos Fiscales.

INTRODUCTION

A characteristic feature of the stage of economic development in many developed countries is the realization of the importance of developing each region and each territorial community. Local governments play an important role in this process, as they have constitutional guarantees to exercise their delegated powers. The main task of local authorities is to ensure the full provision of public services to residents of territorial communities, which improves the level of well-being and quality of life within the administrative-territorial entities. The determining factor in this is the level of financial support of each community, the availability of sufficient financial resources, their mobilization, and efficient use. Therefore, the issue of financial support for local governments is becoming increasingly important.

Various aspects and peculiarities of financing the regional development of local communities are a well-studied topic in the academic community. The authors of Edwards et al. (2015) emphasized that decentralization has proven to be an effective strategy for post-conflict recovery in Sierra Leone. The researchers noted that increasing the discretionary powers of local governments increased their accountability to citizens. Horbova et al. (2023) revealed the peculiarities of attracting financial and investment resources for territorial communities. They emphasized the need to optimize resource use mechanisms to ensure sustainable development.

Other authors, Afonso and Venâncio (2019), proved that territorial reform at the local level had a positive impact on regional spending efficiency, including optimizing management structures and reducing costs. The authors noted that the reform increased transparency and efficiency in allocating budget resources.

Guan et al. (2024) examined the connection between local debt, local government financial platforms, and green development performance in their study. The authors noted that excessive debt limits investment in sustainable development programs. Patynska-Popeta and Zinchuk (2022) emphasized promising areas for managing the financial potential of sustainable development of territorial communities. The researchers noted that important tasks include finding new financial resources and increasing efficiency. The authors of another study, Káposzta et al. (2016), examined local economic development in transition economies as a tool for sustainable urban development. The authors noted that increased economic activity at the local level could help reduce socioeconomic imbalances.

Akapelwa and Mwange (2023) analyzed the main theories of local government financing and emphasized various approaches to ensuring the financial sustainability of regions. The authors emphasized the need to consider the specific conditions of the regions for the efficient use of financial resources. Bondarchuk et al. (2022) provided a methodology for assessing financial revenues in territorial communities. The researchers noted that the proposed approaches contributed to a more accurate analysis of community revenues and increased financial transparency and predictability of budgets.

Bruno and Cozzolino (2023) studied fiscal instruments to support sustainable regional development. The authors emphasized the importance of integrating innovative financial mechanisms to ensure the sustainability of regions in the long term. La Torre et al. (2019) substantiated the use of business models for financing using the example of social bonds. They noted that social bonds are an innovative tool for solving social problems and financing sustainable programs. Thus, despite the above studies covering a wide range of issues related to local government financing, sustainable development of territorial communities, and cost-effectiveness, the specifics of financing in European countries and Ukraine require further research.

The study's purpose is to highlight the specifics of forming sources of financing for the local economic development of territorial communities, such as advanced countries and Ukraine. To achieve this objective, the study set the following tasks:

1. To analyze the instruments of financing local economic development of territorial communities in the UK, Denmark and France.
2. To analyze the peculiarities of financing of territorial communities in Ukraine and to propose ways to improve them based on the experience of advanced European countries.

METHOD

The research methodology uses economic, statistical, and analytical methods that provide a comprehensive approach to analyzing local community financing. In the first stage, economic and statistical analysis methods

were used to study the financial data of territorial communities in the UK for 2017-2022 and the structure of their revenues, including grants and their own sources.

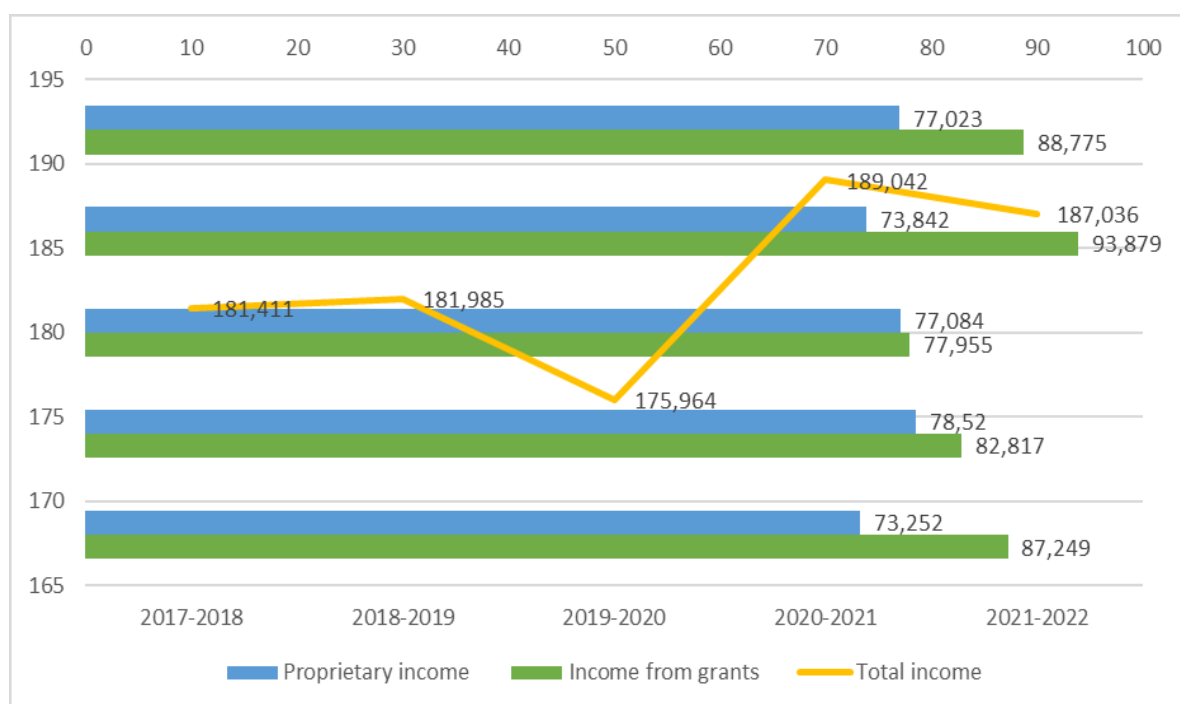
Methods of classification and grouping were used to systematize the experience of financing communities in Denmark, which made it possible to identify the primary sources of funding and the specifics of the tax system. The map of Denmark, created with structural reform in mind, became the basis for the spatial analysis conducted using cartographic visualization methods. The French experience was also assessed using economic and statistical analysis methods (distribution of funding sources for local communities in France and climate initiatives and regional investments in France from 2020 to 2023).

In the second stage, structural and dynamic analysis methods were used to analyze the financing of Ukrainian territorial communities. Economic and mathematical methods allowed us to assess the leading indicators of the structure of local budget revenues within a given period. The use of graphical methods provided data visualization, which contributed to a clear presentation of the results and facilitated further interpretation.

RESULTS

Adequate financing of the economic development of territorial communities plays an important role in ensuring their sustainable growth and improving the quality of life. International experience shows different approaches and strategies that can serve as valuable examples for improving financial mechanisms at the local level. The UK has a multi-tiered system of local government consisting of counties and districts. Regions perform limited functions and are not treated as local governments in the context of funding. Counties and districts remain the primary levels of government. There are 89 counties, which are classified into several categories, each with its specific features.

Proprietary revenues include revenues from local taxes, such as commercial real estate tax, a portion of which is used to finance local budgets. Non-AEF (American Endowment Foundation) grants are used to finance specific services, such as housing assistance. These services are typically administered by third-party organizations with the support of subsidies provided by the Ministry of Labor and Pensions (figure 1).



Source: Department of Equalization (2023)

Figure 1. Revenues from grants and own revenues of local communities in the UK, million pounds for 2017-2022

The analysis of local community revenues for 2017-2022 revealed a number of interesting funding trends. Total grant income showed fluctuations: a decrease in 2019-2020 and an increase in 2020-2021. The share of AEF grants increased steadily from 49,66 % in 2017-2018 to 56,85 % in 2021-2022. This demonstrates the growing dependence of local governments on these grants, which can be both an advantage (more resources for important initiatives) and a challenge (risk of dependence on unstable funding).

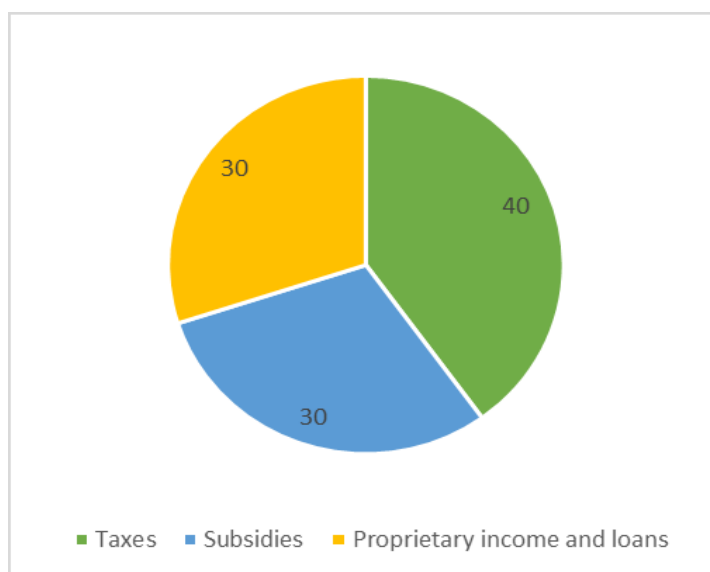
Proprietary revenues also had different dynamics. Municipal tax grew from 16,78 % to 18,43 %, indicating stable or growing tax income. At the same time, revenues from capital receipts and sales decreased, which may indicate a reduction in assets or changes in economic conditions. It is also worth noting that until 2014-2015, the distribution of funding through the local government system was based on the socio-economic and

demographic characteristics of the territories and the ability of local authorities to collect taxes for local services, for example, based on the number of facilities on their territories, which was regularly adjusted.

The business tax retention scheme introduced in April 2013 was an important reform for local government financing, creating a direct connection between tax revenue growth and available resources to finance local services. The scheme requires governments to retain at least half of local business tax revenues and their growth. Additionally, a system of tariffs and surcharges provides an initial redistribution of resources so that no government is shortchanged in its ability to meet local needs due to changes in the business tax base (Local Government Financial Statistics England No.33., 2023).

Business tax revenues that go to the central government cover a significant portion of the Revenue Support Grant provided to local governments to help finance their expenditures. Since 2017-2018, some authorities have received more than 50 % of their revenues from local business taxes, significantly increasing their funding.

The system of financing local development in France is based on three primary sources: taxes, self-financing, subsidies, and grants (figure 2).



Source: François et al. (2022)

Figure 2. Distribution of sources of funding for local communities in France, %

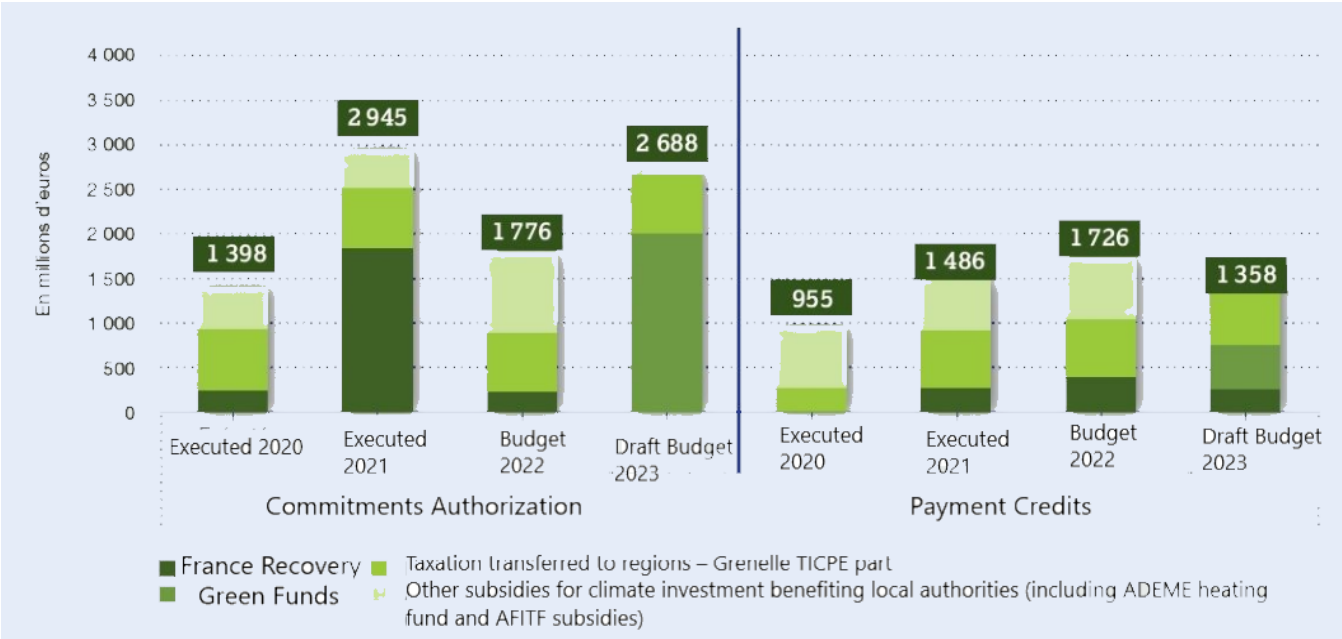
The primary financing tool for local government investments is their ability to self-finance, which is ensured by excess operating revenues over expenditures. Local government revenues are generated from taxes, grants, and revenues from the provision of services, while expenses include salaries, operating expenses, subsidies, services, and debt payments. In 2021, 59 % of capital expenditures (EUR 39 billion out of EUR 67 billion) of local governments were financed by operating cash flow, demonstrating the crucial role of self-financing in ensuring the stability of local budgets (François et al., 2022).

The second most important funding source is subsidies and grants that local governments receive from the state, the European Union, and other local bodies. Such subsidies and grants amounted to EUR 25 billion in 2021, 37 % of total capital expenditures. Government subsidies aimed at implementing climate initiatives play a significant role in stimulating investment. They reached EUR 2,7 billion in 2023, which was made possible by the creation of the Green Fund, which supports programs aimed at reducing climate impact and other environmental initiatives (Herczyński, 2018).

Local governments also use debt obligations as an additional tool to implement investment programs. In 2021, net borrowings amounted to EUR 3 billion, or 4 % of capital expenditures. This is a significant decrease compared to 2020, when borrowing reached 8 % due to the COVID-19 pandemic (François et al., 2022).

However, to fulfill France's international commitments to achieve carbon neutrality, local governments must double their annual climate investments from EUR 5,5 billion to EUR 12 billion, accounting for about 20 % of their total capital expenditures. It is important to increase funding and adapt to macroeconomic conditions that affect the ability to implement climate projects. Climate initiatives and regional investments in France from 2020 to 2023 are shown (figure 3).

The graph in figure 3 shows the financial commitments and payment credits for climate initiatives and regional investments in France between 2020 and 2023 in millions of euros. There was a significant increase in financing in 2021, reaching EUR 2,945 million, mainly due to the France Relance program (France's recovery plan). Although financial commitments decreased to EUR 1,776 million in 2022, they increased to EUR 2,688 million in 2023, indicating a gradual recovery.



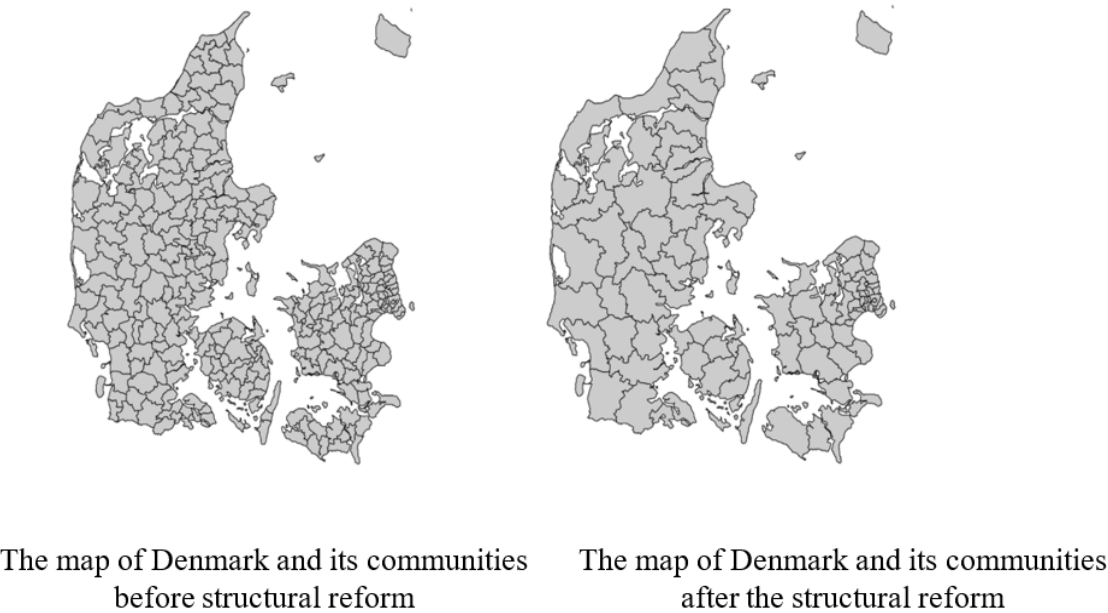
Source: François et al. (2022)

Figure 3. Climate initiatives and regional investments in France in the period from 2020 to 2023, EUR million

Payment loans reflect actual expenditures, steadily increasing from EUR 955 million in 2020 to a peak of EUR 1,726 million in 2022. Thereafter, a slight decrease to EUR 1,358 million is planned for 2023. The primary funding sources are the Green Investment Fund, fiscal transfers to the regions (Grenelle TICPE), and other climate subventions for local communities. The schedule demonstrates France’s strategic approach to supporting regional development and climate initiatives, focusing on stimulating investment in the short term and providing stable funding to achieve long-term aims.

Denmark is also a vivid example of successful local community development. Denmark underwent a large-scale local government reform in 1974, which merged more than 1,300 administrative units into 277 municipalities and 14 counties (Kjaer, 2021). The result was increased tax rates from 15 % in 1975 to over 25 % in 2013. The second phase of reforms, implemented in 2007, involved further consolidating administrative units into 98 municipalities and five regions. The reforms included a redistribution of responsibilities and changes in the financing system, including introducing a new block grant and equalization mechanism.

Figure 4 shows a map of Denmark showing the implementation of structural reform (Kjaer, 2021).



Source: Kjaer (2021)

Figure 4. The map of Denmark with the implementation of structural reform

The above-mentioned reforms in Denmark aimed to ensure more efficient resource management and optimize local communities' financing by reducing the number of administrative units, which allowed for lower administrative expenditures, higher tax rates, and equalization mechanisms. Table 1 shows the rates of some of the local taxes that are a source of funding for local communities in Denmark in 2024.

Table 1. Rates of some local taxes, which are a source of funding for local communities in Denmark in 2024	
Local taxes	Rate, %
Municipal tax	25,067
Church tax	0,65
Labor market tax	8
Land tax	2,8
Source: Worldwide Tax Summaries (2024)	

Denmark is an example of a successful model of financing local communities. This model included a combination of tax revenues and intergovernmental transfers, ensuring the financial stability of municipalities. Following large-scale reforms that reduced the number of administrative units, an equalization mechanism was introduced to help reduce financial inequalities between municipalities. The main sources of revenue were personal income tax and property tax, as well as state block grants, which significantly improved the financial capacity of local governments (Worldwide Tax Summaries Online, 2024).

Under current military realities, ensuring the capacity of territorial communities is one of the main tasks of local self-government. It is worth emphasizing that only a capable community can mobilize the necessary resources to provide public services adequately. Amalgamated territorial communities (hereinafter referred to as ATCs) have received the powers and resources previously inherent in cities of regional significance. This includes the transfer of 60 % of personal income tax to the local budgets of ATCs, which is used to fulfill their powers. In addition, the local budgets fully retain revenues from taxes such as the single tax, the tax on profits of enterprises and financial institutions of communal property, and property taxes (real estate, land, and transportation).

Articles 64 and 67 of the Budget Code of Ukraine provide that local budgets of amalgamated territorial communities include:

1. Taxes: personal income tax (60 %), environmental tax (25 %), excise tax (5 %), single tax (100 %), income tax on municipal enterprises, property tax (100 %).
2. Fees and payments: compensation for environmental damage (50 %), compensation for losses in agricultural and forestry production (75 %), tourist tax, state duty, fees for administrative services, etc.
3. Other revenues include the basic grant, educational and medical subventions, funds from international technical assistance programs, etc.

During martial law, local governments were also given the opportunity to retain a monthly reverse subsidy, which is not subject to transfer to the state budget.

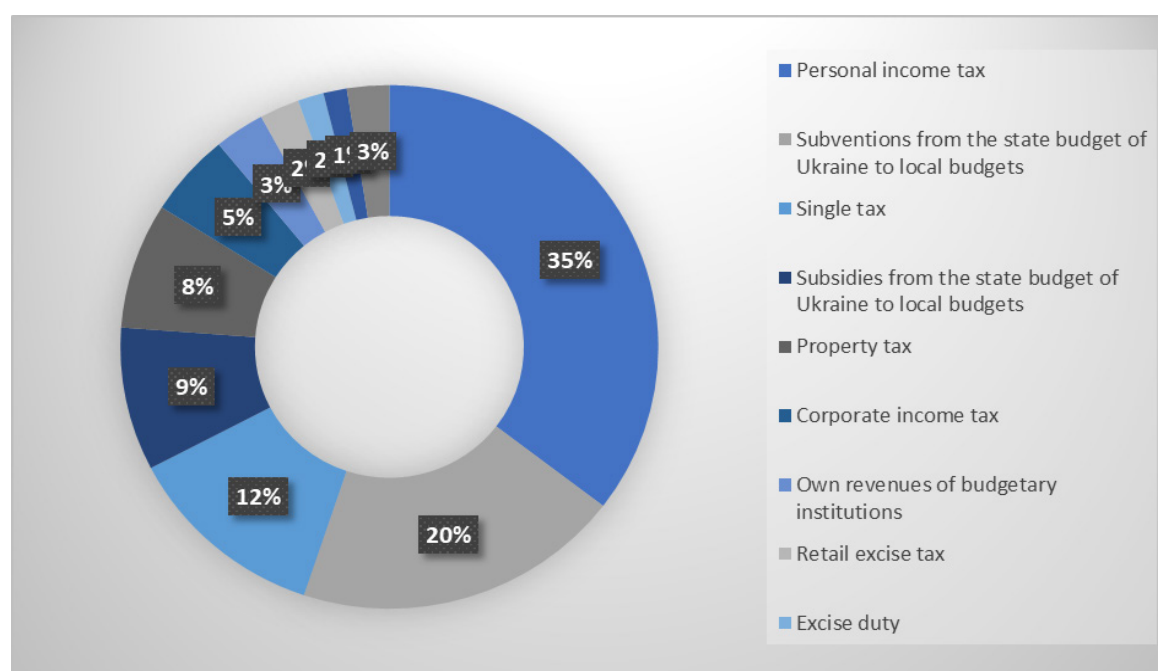
Figure 5 shows the structure of local budget revenues for the first four months of 2024 (01.01.2024-04.04.2024).

The Russian Federation's military aggression has resulted in local budgets in all regions of Ukraine receiving less than planned revenues, which often jeopardizes the exercise of powers defined by law. Some local councils have found themselves in a situation where budget revenues are insufficient to cover even the minimum required expenditures. Legislative changes were adopted in response to this, providing local governments with an expanded list of tax revenues.

The ability of a community to provide the required level of public services to recover and develop depends on its financial sustainability. In 2023, 429 communities (29,8 %) were classified as having the lowest level of financial sustainability (critical and low levels). At the same time, more than a third of territorial communities (495 communities or 34,4 %) were classified as having a high financial capacity. The critical condition was recorded in communities in 16 regions. At the same time, the low level of financial capacity is characteristic of territories directly affected by military operations or located near conflict zones. However, this group also includes communities located in the deep rear. It is worth noting that in 79 territorial communities, the costs of the administrative apparatus exceed their revenues (OECD, 2021).

Ukraine should implement several measures to strengthen the revenue base of local budgets based on the experience of other countries. One of the first steps is to determine the optimal share of transfers and targeted subventions in the total amount of transfers from the state budget, which will allow for more efficient financial

resource planning. The following important area is the rational distribution of expenditure obligations between local budgets, ensuring a more equitable and efficient distribution of funds to meet local needs.



Source: Decentralization (2024)

Figure 5. Structure of local budget revenues for 4 months of 2024 (01.01.2024-04.04.2024)

It is also worth using not only subsidies to finance capital expenditures but also different types of loans, such as bonds and intergovernmental loans, as well as loans from financial institutions, which will significantly expand the sources of financing for large infrastructure programs. An important component of the revenue base should be local taxes that are sustainable and significant, such as personal income tax or luxury tax, which will ensure the stability of local budget revenues.

The local taxes should be directly proportional to the level of local service provision, allowing for adequate financing of important social and infrastructure needs. It is also advisable to develop alternative sources of local budget revenues, in particular through the introduction of non-tax fees, such as rent of property of budgetary institutions, to expand the revenue base. Reducing the dependence of local budgets on state grants and subventions will reduce the level of state influence on the development of local self-government, ensuring more financial independence and autonomy for local governments.

DISCUSSION

Optimizing the share of transfers and targeted subventions in the total amount of state support has been found to allow for more efficient resource planning and fulfillment of local needs. Similar conclusions can be found in the research work of Bondarchuk et al. (2022), who also emphasized the need to improve the system of intergovernmental transfers to achieve more excellent financial stability of local budgets. An important area is the rational allocation of expenditure obligations, ensuring a fair and transparent distribution of finances. This conclusion is shared by other authors, Patynska-Popeta and Zinchuk (2022), who pointed out the need to introduce precise mechanisms for allocating expenditures between different levels of government to ensure financial transparency and equity.

The conclusions of Ariyanto et al. (2024) are consistent with the current study's results regarding the importance of effective financial management of territorial communities to ensure their economic development. Their analysis highlighted the impact of primary regional income, excess budgetary funding, and regional wealth on capital expenditures, which is similar to the important areas of local community financing in the UK, Denmark, and France.

In contrast to the experience of European countries, which emphasize financial equalization and self-financing mechanisms, the authors' study pays special attention to the role of economic growth as a factor that can partially mitigate the impact of budget surpluses and regional wealth on investment. This demonstrates a common trend: successful financing of territorial communities requires an effective combination of revenues and strategic management of budgetary resources.

The experience of the UK, Denmark, and France has demonstrated different approaches to financing territorial communities, each with its advantages and peculiarities. The UK relies on a combination of local taxes

and grants. Denmark has successfully implemented a financial equalization mechanism, while France focuses on self-financing. Adopting these models will help ensure the financial sustainability of local communities, efficient resource allocation, and sustainable economic development at the local level.

Yakymchuk et al. (2023) focused on decentralization, transparency of financial transfers, and the need to harmonize national legislation with European directives, especially in the context of natural capital conservation and international cooperation. Their study is more focused on the impact of military and political events, economic instability, and environmental problems on the financial sustainability of territorial communities. In contrast, the current study pays more attention to practical financing mechanisms and their role in regional development. The common thread is that both studies emphasize the need for a strategic approach to managing budgetary resources to ensure the effectiveness of territorial communities.

Romero Caro's findings revealed a different context, namely the Spanish territorial financing system and autonomous communities' horizontal cooperation in setting a common agenda. This study analyzes the political mechanisms of cooperation between the autonomous communities and their ability to influence the central government during financial negotiations, in contrast to the current study, which focuses on the impact of budgetary funding and regional revenue on capital expenditures. However, both approaches confirm the importance of intergovernmental cooperation and strategic coordination for improving financial management and achieving regional development, a common point for different countries, given their specific problems.

CONCLUSIONS

International experience has shown different approaches and strategies that can serve as valuable examples for improving financial mechanisms at the local level. The distribution of revenue sources between different levels of government was as follows: the central government generated most of the revenue taxes, the regions generated sales and income taxes, and the local level generated property taxes.

The French experience received special attention, as the administrative systems of these countries were similar, and their monetary and tax systems were modeled after it. Each country faced unique challenges in generating revenue and efficiently allocating local budget expenditures. Considering the development of European economies at that time, Ukraine had to consider its budgetary policies to improve the financing of local budgets.

The current study is limited to certain countries (UK, France, Denmark, Ukraine), which does not allow for complete generalization of the findings to other countries or regions with different financial and administrative systems. This limitation may affect the accuracy of conclusions about the effectiveness of different financial mechanisms in other contexts. Further research should consider other EU countries' experiences to compare and identify priority ways to improve public policy in Ukraine.

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CONFLICT OF INTEREST

The authors declare that there is no conflict of interest.

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Data curation: Tetiana Dei.

Methodology: Tetiana Dei.

Software: Tetiana Dei.

Drafting - original draft: Tetiana Dei.

Writing - proofreading and editing: Tetiana Dei.