“Assessment of the fiscal autonomy of local governments in Armenia”

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ASSESSMENT OF THE FISCAL AUTONOMY OF LOCAL GOVERNMENTS IN ARMENIA

Abstract

Fiscal decentralization is a key component of effective economic governance, enhancing the role of local governments and promoting more efficient allocation of public resources. A central dimension of fiscal decentralization involves the distribution of tax revenues across different levels of government. The purpose of this study is to assess the level of fiscal autonomy of local governments in the Republic of Armenia using the OECD methodology and tax autonomy as a measure of local government taxing powers. By comparing Armenia with OECD unitary states through cluster analysis, the analysis identifies an optimal structure for local tax revenue systems. Armenia exhibits a low level of tax autonomy comparable to the weakest cluster of OECD unitary countries, which includes Estonia, Ireland, Israel, Lithuania, New Zealand, and the UK. The findings suggest that increasing local government revenues by deducting from existing indirect taxes, such as excise duty and VAT, is challenging due to administrative inefficiencies and difficulties in accurately estimating the tax base. Due to their narrow and centralized nature, excise taxes are poorly suited to local use, while the complexity of VAT and its allocation of revenue to customs authorities limits its effectiveness at the local level. In light of its findings, the study recommends shifting the focus toward direct taxes to improve local revenue more effectively and sustainably.

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INTRODUCTION

The fiscal autonomy of local governments is crucial, as it directly affects their ability to manage resources, deliver public services efficiently, and reduce their dependence on central government transfers. For a local self-government system to function well, it is essential to guarantee both the financial independence of local governments, which gives them the ability to create their own financial resources and implement their own financial policies, and a stable and adaptable base of financial resources sufficient to the execution of the legal authority granted to them (Reddy et al., 2015). Nevertheless, local governments worldwide still face a strong dependence on central government transfers, which can limit their fiscal autonomy and ability to self-finance (Grdinić et al., 2019; Tan, 2020; Petrova, 2021). This issue is crucial for unitary states.

To improve the process of power delimitation, the Republic of Armenia's authorities have been working for years to give the local level of self-government more weight in the public administration system. However, the issue of widespread management decentralization has not yet been resolved, either in terms of specific implementation strategies or at a general, ideological, and legal level. The main scientific question, which remains unclear, is to what extent does the formal grant of fiscal autonomy to local governments in this unitary state translate into effective, practical autonomy in revenue generation, expenditure decisions, and service delivery, and what is the optimal structure of tax revenues of local budgets? This problem arises from a persistent gap between the theoretical framework granting fiscal powers to local governments and the actual, observed fiscal independence and responsiveness at the local level.

1. LITERATURE REVIEW

According to the theory of fiscal federalism (Oates, 1972), decentralization of finances is more efficient because it allows for better consideration of regional preferences in the provision of public services. This can be achieved through three channels: enhanced awareness among local authorities of the population's needs, competition between regions for resources, and stimulation of innovation in public administration (Weingast, 2009; Oates, 2005). Giving local governments a larger share of tax revenue lets them benefit more from regional growth (Yan et al., 2022; Kwon, 2013). This encourages them to spend more (Jiao, 2021), boosting local economies and improving governance, which in turn increases tax revenue. A higher share of tax revenue also eases financial pressure from increased responsibilities (Chen et al., 2019), reducing competition between local governments and giving cities and regions more control over their finances. This makes them more responsible for their spending, reducing risky behavior and improving governance.

Numerous studies support the theoretical assumptions about the relationship between fiscal decentralization and dynamic socioeconomic development, although they reveal its complexity (Baskaran et al., 2016; Li & Gu, 2025). For example, Zhao and He (2024) show a positive correlation between decentralization and the development of innovation capacity. Lin and Zhou (2021a) and Chu (2025) demonstrate the positive impact of fiscal decentralization and environmental efficiency, and Cavalieri and Ferrante (2016) confirm the social well-being. Tax autonomy is essential for improving local governance, accountability, responsiveness to community needs (Ligthart & van Oudheusden, 2015), has a strong impact on sustainable territorial development (Hakhverdyan & Badadyan, 2023; Ratner et al., 2024), and often is directly associated with democracy (Canavire-Bacarreza et al., 2017; Martinez-Vazquez et al., 2017).

Researchers from various nations around the world have been and continue to be interested in the problems of decentralization of the public administration system, which refers to the hierarchical transfer of jurisdiction and authority to lower territorial levels and the granting of greater autonomy to regional government bodies to conduct economic policy. For example, Boetti et al. (2012) highlight that increased fiscal autonomy can lead to more efficient public service delivery by reducing vertical fiscal imbalances and holding local politicians more accountable to citizens. With greater control over their finances, local governments are less likely to behave in an inefficient manner. Surówka (2018) claims that fiscal autonomy empowers local communities by ensuring that local self-governments can independently manage their financial resources. Petrova (2021) also supports this idea, arguing that fiscal independence is fundamental for the effective functioning of local self-governments, allowing them to perform public tasks without excessive reliance on central government transfers.

Canales et al. (2024) found that greater fiscal autonomy enables governments to better align their budgetary priorities with local needs, resulting in more sustainable local development. According to Indonesian researchers, this autonomy allows for the customization of public services and investments according to the specific demands of the community (Zevaya et al., 2024). Some investigations have found that fiscal decentralization can also lead to positive trends in green development and decarbonization (Wang et al., 2022; Ahmed et al., 2023). Li and Bai (2024) prove that both fiscal and financial decentralization have a positive impact on urban high-quality development.

In this context, effective management of local taxes and revenue generation is crucial for enhancing fiscal autonomy. This includes improving tax collection mechanisms and ensuring that local governments have the necessary tools and authority to manage their finances effectively (Tan, 2020).

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It is also well-known from the literature that in federal systems, subnational/local governments typically have greater fiscal autonomy (Danziger, 1991; Letelier-Saavedra & Saez-Lozano, 2015). They usually have more control over their revenues and expenditures, which allows for policy experimentation, efficient resource allocation, and responsiveness to local economic conditions (Naisho, 2024). In contrast, unitary states usually centralize fiscal decision-making at the national level, which can limit the fiscal autonomy of local governments and lead to different types of inefficiency (Busygina et al., 2018). Local governments in unitary states often lack sufficient independent revenue sources and rely heavily on central government transfers, which undermines true fiscal autonomy (Kapidani, 2018; Michael et al., 2022; Sergi et al., 2023). They typically only exercise fiscal powers that the central government chooses to delegate to them, and these powers can be limited or revoked at the center's discretion (Hewitt, 1992; Arnold et al., 2021). Even when local governments are legally empowered to collect taxes and make spending decisions, central authorities frequently impose regulations, set tax rates, or issue directives that limit local discretion (Michael et al., 2022). Therefore, there is a problem of central oversight and regulation, which is difficult to detect and measure. There is only limited knowledge of differences between small and large unitary countries in the context of fiscal decentralization. Moreover, there is still an ongoing discussion about the best way to decentralize fiscal power to local governments to improve their efficiency and governance (Jia et al., 2020; Lin & Zhou, 2021b).

Another scientific problem discussed by Mauri (2024) and Baskaran and Feld (2013) is that traditional indicators of fiscal decentralization (such as the share of local expenditure in total government spending) may overestimate real autonomy, as local governments may not have genuine control over revenue or spending decisions. The ability of local governments to make autonomous decisions regarding their revenues and expenditures without central government control is implied by fiscal decentralization (Vetter, 2007; Pratchett, 2004). Therefore, the tax authority granted to local governments also determines the extent of fiscal decentralization (Movsisyan et al., 2022).

A local government with complete fiscal autonomy can decide what taxes to impose, as well as the tax base, rates, and exemptions (Blöchliger & Nettley, 2015). However, a local government will function as a small independent state and cease to be regarded as "local" in any intergovernmental system if it is granted complete autonomy over its tax structure (Bird, 2011). A more pragmatic definition of fiscal autonomy is the degree of control local governments have over their tax base, rates, and other features.

Since 1995, the OECD has conducted regular assessments of the financial independence of local and regional governments in 34 member countries. To evaluate the degree of fiscal autonomy in various nations, the OECD developed a specific classification. Numerous scholars have used this methodology to compare the degree of fiscal autonomy of local governments across nations with those of OECD members. Thus, Reschovsky (2019) specifically evaluated the tax autonomy of US local governments and came to the conclusion that the United States would have significantly more tax autonomy than the majority of OECD nations if its tax structure were similar to that of the typical OECD nation. There are significant differences in the level of local government revenue autonomy amongst states, even those that mostly rely on the property tax.

Matić et al. (2024) assessed Croatia's local tax autonomy by applying the OECD methodology in terms of the definition and scope of taxes and their classification according to taxing power and autonomy. According to the analysis, Croatia continues to trail significantly below the average compared to other OECD unitary nations. Blöchliger and Nettley (2015), Pietrovito et al. (2023), and Vdovichen et al. (2024) applied the OECD methodology to assess the level of tax autonomy of EU countries, so it can be stated that the OECD methodology has become an international standard for assessing tax autonomy, which is widely used in both developed and developing countries.

Relying on the limited number of studies on post-Soviet countries (Siegel, 2022; Yushkov, 2015; Turyan, 2024), it is possible to conclude that they lag behind the OECD average in terms of fiscal decentralization, but the difference between unitary and federal countries has not been the focus of the study in this region before. Another important issue is the optimal structure of tax revenues of local budgets. Some empirical research shows that in situations when local governments have greater control over their own tax bases (such as exclusive authority over property taxes), it typically reflects and reinforces a higher level of fiscal decentralization (Liberati & Sacchi, 2013; Kim et al., 2013; Papcunová et al., 2020).

Therefore, the purpose of this study is to assess the level of fiscal autonomy of local governments in the Republic of Armenia using the OECD methodology and tax autonomy as a measure of local government taxing powers. The hypotheses can be formulated as follows:

H1: Local tax autonomy in the Republic of Armenia is below the average of the OECD unitary countries.

H2: The structure of tax revenues of local budgets in the Republic of Armenia is not optimal.

2. METHODS

This study uses the OECD's methodology to evaluate tax autonomy and employs cluster analysis to identify groups of OECD countries with a similar level of tax autonomy as Armenia. The OECD's methodology provides a standardized framework for assessing tax autonomy and is widely used in international practice to analyze and assess the level of tax autonomy of local government bodies. This methodology enables a direct comparison of the Armenian tax system with that of OECD unitary countries despite Armenia not being a formal member of the organization. Consequently, it provides a benchmark against a group of developed economies and helps to investigate whether Armenia is moving toward or away from the tax autonomy models seen in more developed economies.

Using a six-level scale, the OECD evaluates the tax autonomy of various governmental levels based on the proportion of tax revenues attributable to each level. There are twelve sub-levels within these levels (OECD, 2025a):

a) regional and local government bodies are free to set tax rates and tax privileges (two sub-levels: full and limited freedom);

b) local and regional governments are free to choose tax rates (which can be divided into three sub-levels: full, within a specific upper and lower range, and freedom within a specific income limit);

c) regional and local government bodies are free only in matters of establishing tax privileges;

d) local and regional government bodies take part in the tax-sharing program among different levels of government (four sub-levels depending on who and when determines the sharing proportions;

e) tax rates and exemptions are determined by the central government;

f) other (unspecified) mechanisms.

Countries have been divided into the following four groups based on the degree of local government tax autonomy, depending on which of these levels is most prevalent:

1. Broad level of tax autonomy: tax authority level (a);

2. Moderately broad level of tax autonomy: tax authority levels (b) and (c);

3. Moderately narrow level of tax autonomy: tax authority level (d);

4. Narrow (unspecified) level of tax autonomy: tax authority levels (e) and (f).

In addition, local taxes/local budget revenues, local taxes/total taxes, and local budget tax revenues/GDP indicators were computed in order to diagnose the tax autonomy of the Republic of Armenia's local self-government bodies and to compare them with OECD unitary nations. Descriptive statistics, correlational, and comparative analysis techniques were applied, taking into account the research goal and focus.

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Data for calculations were obtained from the OECD Fiscal Decentralization database (OECD, 2025b), the Ministry of Finance of the Republic of Armenia database (Ministry of Finance of The Republic of Armenia, 2024), and the Armstat database. The year 2022 was chosen as the period under study.

In addition to the OECD classification system of tax autonomy, this study employed an exploratory statistical technique to strengthen the comparative dimension of the analysis: multivariate cluster analysis. Specifically, the objective was to group countries with similar tax autonomy characteristics in order to determine Armenia's relative position within the broader spectrum of OECD unitary countries.

Seven indicators characterizing the level of tax autonomy were selected for cluster analysis:

1) x_1 – local tax revenue as a share of local budget revenue, %;
2) x_2 – local tax revenue as a share of total tax revenue, %;
3) x_3 – local tax revenue as a share of GDP, %;
4) x_4 – taxes on income, profits, and capital gains as a share of total taxation, %;
5) x_5 – taxes on property as a share of total taxation, %;
6) x_6 – taxes on goods and services as a share of total taxation, %;
7) x_7 – other taxes as a share of total taxation, %.

These variables were standardized and subjected to hierarchical clustering to obtain a preliminary understanding of groupings, followed by K-means cluster analysis for refinement. The Euclidean distance was used as a measure of the distance between objects (country *i* and country *j*).

$$d_{ij} = \sqrt[2]{\left(x_{1i} - x_{1j}\right)^2 + \left(x_{2i} - x_{2j}\right)^2 + \ldots + \left(x_{7i} - x_{7j}\right)^2}. \quad (1)$$

The rule for grouping objects into clusters is the Unweighted Centroid Method.

This two-stage approach enhances the robustness of the findings by mitigating initial sensitivity to distance metrics. The application of the K-means method identifies homogeneous groups (clusters) in which intra-group variability is minimized while maximizing inter-group variability. The algorithm is formulated in such a way that it groups the most similar objects together based on their studied features (Gomonov et al., 2021). As a result, the countries under consideration were grouped into three homogeneous clusters in such a way that the objects contained in a given cluster are similar to each other and, at the same time, different from objects belonging to other groups.

3. RESULTS

The budget system of the Republic of Armenia is a set of two-level budgets: state and community budgets, as defined by the RA Law On the Budgetary System of the Republic of Armenia. In Armenia, the community budget is currently funded by state taxes (income tax, profit tax, and environmental fees), local taxes (land tax for land located in the administrative territory of the community, property tax for property located in the administrative territory of the community, hotel tax, and vehicle parking tax), and other legal acts for community budgets.

In Armenia, local tax administration and fiscal policy are carried out through the following methods:

1) The Law of the Republic of Armenia On the Tax Code of the Republic of Armenia establishes the powers of the local tax base, rates, and privileges defined in the budgets of the communities of the Republic of Armenia, and local self-government bodies use these rates.

2) There is no legal definition for hotel and car parking taxes, and local self-government organizations have not yet imposed them.

3) The Law on the State Budget determines the percentages of deductible taxes and environmental payments each year; however, since the Law On Local Self-Government was adopted, no income tax or profit tax deductions have been granted to communities.

4) The Law of the Republic of Armenia On Local Duties and Payments specifies the different kinds of local duties and payments as well as the lowest and highest rates for them.

As a result, Armenian communities are not authorized to determine tax rates for taxes that are part of their overall revenue. Consequently, the Republic of Armenia's local governments are rated as having a narrow (unspecified) level of tax autonomy. Costa Rica and Israel are notable among the unitary OECD members for having a low degree of local government tax autonomy, with the central government setting 100% and 96.4% of local taxes, respectively (Table 1).

Chile, France, Latvia, Poland, and Slovenia are among the nations with a moderately limited degree of local government tax autonomy, as indicated in Table 1. The central government sets the ratio of tax revenue distribution, with an average specific weight of roughly 66%. New Zealand stands out among the nations being reviewed for having a high degree of tax autonomy for local governments, giving them total control over tax rates and incentives. Since local governments have complete or limited authority to choose tax rates, the degree of tax autonomy enjoyed by local governments in the remaining 16 nations is regarded as relatively extensive.

Local governments have a high degree of tax autonomy, particularly in nations with a high degree of fiscal decentralization. Specifically, taxes account for 76.7% and 60.9% of local budget income in Iceland and Sweden, respectively. This indicates that local governments in both nations rely between 24 and 40% on transfers from the national government. This score is within 1/5 in Armenia, meaning that local governments rely on transfers from the national government to the tune of almost 80%. It should be mentioned that local budget taxes make up 35.1% of overall tax receipts in Sweden, 27.5% in Iceland, and only 2.2% in Armenia (Table 2).

The composition and structure of the sources of tax revenue creation in local budgets also have a significant role in determining the variations in the tax autonomy levels of local governments between nations. The nations under study were categorized into four groups based on the sorts of taxes that were included in municipal budgets (Table 3). A tax type was considered prominent if its revenues were almost twice as high as those of the next most important taxes.

According to the analysis, local governments have a high degree of tax autonomy, particularly in countries where income tax and profit tax are the main sources of tax revenue for local budgets. On the other hand, there is little tax autonomy in countries where property taxes provide for the majority of municipal budget revenue.

It is necessary to note that in the Republic of Armenia, property taxes are the only source of

Table 1. Comparing the level of tax autonomy of local governments in OECD unitary countries and Armenia

Broad tax autonomy level a	Moderately broad tax autonomy levels b, c	Moderately narrow tax autonomy level level d	Narrow (unspecified) tax autonomy levels e, f
New Zealand (98.0%)	Czechia (99.9%) Denmark (89.6%) Estonia (79.9%) Finland (81.9%) Hungary (99.8%) Iceland (97.5%) Ireland (100%) Italy (69.9%) Lithuania (80.4%) Luxembourg (92.9) The Netherlands (70.2%) Norway (99.3%) Portugal (62.1%) The Slovak Republic (90.6%) Sweden (97.5%) The UK (99.0%)	Chile (65.1%) France (35.0%) Latvia (87.5) Poland (67.0%) Slovenia (75.1%)	Armenia (100%) Costa Rica (100%) Israel (96.4%)

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Table 2. Comparing the degree of fiscal decentralization in Armenia with OECD unitary countries in 2022

Country	Local tax revenue as a share of local budget revenue,%	Local tax revenue as a share of total tax revenue,%	Local tax revenue as a share of GDP,%
Armenia	20.4	2.2	0.5
Chile	30.2	6.9	1.6
Costa Rica	41.1	2.7	0.7
Czechia	2.6	1.0	0.3
Denmark	36.9	26.5	11.1
Estonia	2.2	0.6	0.2
Finland	47.1	23.0	9.9
France	59.4	14.4	6.6
Hungary	29.1	4.7	1.7
Iceland	76.7	27.5	9.7
Ireland	16.4	1.6	0.3
Israel	48.8	8.2	2.7
Italy	33.1	10.9	4.7
Latvia	49.1	16.4	5.1
Lithuania	3.6	1.0	0.3
Luxembourg	28.9	3.6	1.4
The Netherlands	9.5	3.2	1.2
New Zealand	46.0	6.4	2.1
Norway	38.0	10.3	4.5
Poland	30.5	11.8	4.1
Portugal	39.5	7.1	2.5
The Slovak Republic	8.5	1.9	0.6
Slovenia	35.9	8.5	3.2
Sweden	60.9	35.1	14.9
The United Kingdom	18.8	95.1	1.7

Table 3. Comparing the structure of tax revenues of local budgets of Armenia and OECD unitary countries in 2022, % of total taxation

Type of the structure	Country	Taxes on income, profits and capital gains, total	Taxes on income, profits, and capital gains of individuals	Taxes on income, profits, and capital gains of corporate	Taxes on property	Taxes on goods and services	Other taxes
Predominance of taxes on income, profits, and capital gains in local budget tax revenues	Denmark	89.6	89.6	0.0	10.4	0.0	0.0
	Finland	92.3	81.9	10.4	7.7	0.0	0.0
	Iceland	80.6	80.6	0.0	16.9	2.5	0.0
	Latvia	87.5	87.5	0.0	11.9	0.6	0.0
	Luxembourg	92.7	0.0	92.7	6.2	0.9	0.1
	Norway	85.8	85.8	0.0	13.5	0.7	0.0
	Poland	67.0	54.4	12.6	28.4	0.0	4.6
	Slovenia	75.4	75.4	0.0	19.0	5.6	0.0
	Sweden	97.5	97.5	0.0	2.5	0.0	0.0
Predominance of taxes on property in local budget tax revenues	Armenia	0.0	0.0	0.0	100.0	0.0	0.0
	Estonia	0.0	0.0	0.0	79.9	20.1	0.0
	Ireland	0.0	0.0	0.0	100.0	0.0	0.0
	Israel	0.0	0.0	0.0	96.4	3.6	0.0
	Lithuania	0.0	0.0	0.0	81.9	18.2	0.0
	New Zealand	0.0	0.0	0.0	89.3	10.7	0.0
	The Slovak Republic	0.0	0.0	0.0	65.9	34.1	0.0
	The UK	0.0	0.03	0.0	100.0	0.0	0.0

Table 3 (cont.). Comparing the structure of tax revenues of local budgets of Armenia and OECD unitary countries in 2022, % of total taxation

Type of the structure	Country	Taxes on income, profits and capital gains, total	Taxes on income, profits, and capital gains of individuals	Taxes on income, profits, and capital gains of corporate	Taxes on property	Taxes on goods and services	Other taxes
Predominance of taxes on goods and services in local budget tax revenues	Hungary	0.0	0.0	0.0	16.8	83.2	0.0
No dominant taxes in local budget tax revenues	Chile	0.0	0.0	0.0	46.1	53.9	0.0
	Costa Rica	0.0	0.0	0.0	49.1	50.9	0.1
	Czechia	0.0	0.0	0.0	53.7	46.3	0.0
	France	0.0	0.0	0.0	40.1	48.1	5.7
	Italy	19.6	19.6	0.0	20.4	29.4	30.6
	The Netherlands	0.0	0.0	0.0	55.1	44.9	0.0
	Portugal	24.0	15.5	8.5	51.4	24.1	0.4

funding for local (community) budgets, and the proportion of property taxes on moveable property is rising annually.

In the next phase, the study employs cluster analysis tools to classify nations in a multidimensional manner, evaluating the intricate effects of all observable factors on the degree of tax autonomy of local governments. As an outcome of the analysis, three clusters were found: the first cluster included nine nations, while the second and third clusters each contained eight. The cluster composition per nation sample is presented in Table 4, and the final cluster centers, determined by the chosen indicators for clustering, are compiled in Table 5.

Table 4. Cluster membership by country

Cluster	Country	Euclidean distance from cluster center (d_{ic})
Cluster 1	Denmark	13.2
	Finland	23.0
	Iceland	36.7
	Latvia	10.7
	Luxembourg	19.6
	Norway	7.1
	Poland	29.6
	Sweden	18.0
	Slovenia	31.9
Cluster 2	Chile	11.2
	Costa Rica	15.3
	Czechia	32.6
	France	28.7
	Hungary	44.1
	Italy	41.0
	The Netherlands	26.9
	Portugal	32.4
Cluster 3	Estonia	22.8
	Ireland	16.1
	Israel	26.4
	Lithuania	19.8
	New Zealand	30.5
	The Slovak Republic	35.4
	The UK	15.5
	Armenia	15.4

The first cluster comprises Denmark, Finland, Norway, Sweden, and others, as shown in Table 4. Due in large part to the preponderance of income taxes in local budget tax revenues (on average 85.4%), these countries have a significantly higher specific weight of taxes in local budget revenues (on average 42%) and a magnitude of indicators characterizing fiscal decentralization than other clusters. As a result, the nations that make up this cluster may be categorized as having a high degree of tax autonomy and local government financial decentralization.

Chile, Costa Rica, Czechia, France, and other countries are included in the second cluster. Except for indirect and other tax shares, where they lead, nearly all of the metrics seen in these nations fall within the average range when compared to the other two groups. Furthermore, except for a small benefit from indirect taxes, the proportions of property and indirect taxes in municipal budget revenue are nearly the same. As a result, this clus-

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Table 5. Final cluster centers

Indicator	Cluster 1	Cluster 2	Cluster 3
Local tax revenue as a share of local budget revenue	42.0	31.3	20.3
Local tax revenue as a share of total tax revenue	17.1	6.7	3.4
Local tax revenue as a share of GDP	6.7	2.4	1.1
Taxes on income, profits and capital gains as a share of total taxation	85.4	5.5	0.0
Taxes on property as a share of total taxation	12.9	41.6	89.2
Taxes on goods and services as a share of total taxation	1.1	47.6	10.8
Other taxes as a share of total taxation	0.5	4.6	0.0

ter can be viewed as a collection of nations with a moderate degree of financial decentralization among local governments and tax autonomy.

With the exception of property taxes in local budget tax collections, all of the observed variables in the third cluster – which also includes Armenia – are significantly less favorable than those in the other clusters. As a result, the nations in this cluster might be characterized as lagging behind in terms of financial decentralization and local government tax authority. The cluster dispersion analysis (Table 6) shows the significant variations between the clusters.

The data show that only in the case of the local taxes to GDP indicator are the differences in the cluster averages not significant. This indicates that the financial status of the nation has no discernible effect on the degree of tax autonomy and financial decentralization of local governments.

Therefore, as one can see, the first cluster, which includes Denmark and Sweden, has high tax autonomy due to the inclusion of income taxes in local budget revenues. The second cluster shows a moderate degree of financial decentralization. The third cluster, including Armenia, lags in financial decentralization and local government tax authority.

Thus, the study's hypotheses were confirmed. Local tax autonomy in the Republic of Armenia is lower than in most OECD unitary states, and the composition of local budget tax revenues is suboptimal.

4. DISCUSSION

The findings confirm that Armenia exhibits a low level of tax autonomy among OECD unitary countries, placing it within the third and weakest cluster identified through the applied cluster analysis. These results largely align with previous assessments by Armenian academics (e.g., Hayrapetyan, 2018), who revealed the limited financial and administrative capacities of local administrations in Armenia based on the results of local referendum votes and population statistics. They also align with the recommendations of European authorities (Chamber of Local Authorities, 2014), who, after a monitoring visit to Armenia in 2013, recommended increasing the 'own' financial resources of local authorities. Additionally, Aristovnik (2012) and Slavinskaite (2020) have made similar recommendations regarding the clustering of European countries.

The low level of tax autonomy in Armenia is mainly due to a structural reliance on property tax as

Table 6. Cluster ANOVA

Indicator	Cluster Mean Square	Error Mean Square	F-statistics	p-level
Local tax revenue as a share of local budget revenue	993.7	316.3	3.1	0.063
Local tax revenue as a share of total tax revenue	442.0	50.2	8.8	0.002
Local tax revenue as a share of GDP	74.2	8.8	1.4	0.272
Taxes on income, profits, and capital gains as a share of total taxation	51.4	37.2	8.4	0.002
Taxes on property as a share of total taxation	4972.9	151.1	32.9	0.000
Taxes on goods and services as a share of total taxation	12448.0	142.4	87.4	0.000
Other taxes as a share of total taxation	19734.1	66.1	298.7	0.000

the only locally administered tax. Local governments have no powers over direct or indirect taxes, such as income tax or VAT. This restricts revenue generation and policy autonomy at the local level, thereby perpetuating fiscal centralization.

Compared with countries in the first cluster, such as Sweden, Denmark, and Finland, where income taxes dominate local budgets and decentralization is relatively high, Armenia's tax autonomy remains constrained both legally and functionally. In these countries, local governments not only have broader tax bases but also the authority to set tax rates, which fosters financial independence and accountability. The contrast highlights how the presence of income and profit taxes in local budgets strongly correlates with higher fiscal autonomy and effective decentralization.

It is worth mentioning that financial capacity (as measured by GDP or economic development level) does not necessarily determine the level of fiscal autonomy. This suggests that institutional arrangements and political will are more decisive than purely economic variables in defining tax autonomy. Even relatively affluent countries may centralize fiscal control, while others with limited national resources have managed to establish more autonomous local fiscal structures.

In this regard, it is essential to explore the potential for generating own revenues for the municipal budgets of the Republic of Armenia through the collection of taxes.

Since the implementation of deductions from other types of taxes is connected with both application and tax administration problems, it is important to consider direct taxes as a source of local tax revenues in order to increase the tax revenues of the budgets of the municipalities of the Republic of Armenia. Specifically, the excise tax is levied on the production or importation of sub-excise goods and does not apply to local government operations. Therefore, it must be fully credited to the state budget and cannot be a deductible tax. VAT can be considered a regulatory tax; however, it is essential to note that customs officials receive at least 60% of the tax revenue, which is not allocated to the state budget. Secondly, it is difficult to calculate the tax base accurately and to administer the tax efficiently, as the VAT payer is considered to be the consumer.

In view of the above, it seems more appropriate to make deductions from direct taxes. The latter has the most stable revenue base in terms of geographical distribution, which could allow for more equitable and effective financing of service delivery by local self-government organizations. In addition, global experience demonstrates the practicality of deducting certain types of taxes.

However, this analysis primarily relies on quantitative measures of tax autonomy and may not adequately capture qualitative factors, such as political dynamics or local governance capacities that can also influence fiscal autonomy. The investigation in this direction will be a subject of research in the future.

CONCLUSION

This study aims to assess the fiscal autonomy of local governments in the Republic of Armenia using the OECD (1999) methodology, focusing on tax autonomy as a key indicator. A comparative analysis with OECD unitary countries by means of cluster analysis reveals that Armenia exhibits a relatively low level of fiscal autonomy, with an inefficient structure of local government tax revenues. The study concludes that increasing local government revenues through deductions from existing indirect taxes, such as excise duty and VAT, would pose significant challenges due to administrative inefficiencies and the difficulty of accurately estimating the tax base. Excise taxes are not well suited to local use due to their narrow and centralized nature. Meanwhile, the complexity of VAT and the fact that its revenue is allocated to customs authorities limits its effectiveness at the local level. Consequently, the study recommends prioritizing direct taxes as a more practical and sustainable means of enhancing local revenue.

Regarding the directions for future research, it is worth noting that the present analysis is primarily reliant on quantitative measures, underscoring the need to incorporate qualitative factors such

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as political dynamics and governance capacities, which have the potential to significantly influence fiscal autonomy. Exploring these aspects could provide a more comprehensive assessment of local government autonomy.

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