Challenges for sustainable regional development in Russia after the constitutional reform 2020.

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Abstract. Equilibrium of centralization and decentralization is one of the sustainable development drivers for regions in federal countries. The constitutional reform 2020 in Russia was an important political development relevant both for Russia and international discussion. Constitutional amendments made an important contribution to the center-region relations promising to understand better the needs of regions by means of State Council and introducing new actors - federal territories, initially meant for better ecological protection of certain territories. The study allows to conclude that the representation of regions in legislative power is diminished after the reform 2020, but the upgraded State Council opens new opportunities for better center-region communications. Another finding is that the new constitutional phenomenon “federal territories” is unclear and not aimed for ecological needs. It is likely to cause unjustified inequalities in redistributions of finance and revenues between the territories in Russia. Spontaneous creation of federal territories is likely to cause uncertainties in the sustainable development of regions.

Key words: regional development, sustainable cities, sustainable region, constitution of Russia, Olympics

1. Introduction

The optimal redistribution of fiscal powers in a federation with numerous constituencies is at the core of a viable and sustainable financial system and usually covered by the notion of fiscal federalism. Reasonable attribution of tax collection and spending activity to the different levels of government opens the opportunity to overcome crises efficiently. In 2020 Russian Constitution was changed and the changes have an impact on the sustainability of regional development. The academic discussion on the impact of constitutional reform has been evolved already for two years [1]. Sustainable development concept was in the focus of regional science since the XX century [2], but it turned to be the key issue recently with the growing importance of the regional sustainability [3]. The issue of Russian regions’ sustainability is widely discussed in general and with reference to specific sectors of economy [4-7]. Since the introduction of fiscal federalism notion to the economy theory by Musgrave in the middle of XX century [8] this concept has been widely discussed in the literature and in international analytical documents [9,10]. Basic concept of federalism has already evolved and has been enriched by new approaches [11-13]. The issues of center-regions fiscal relations in Russia were in the focus of the studies [14,15] as well as the asymmetries and imbalances between the needs of regions, including their ecological situation, industrial development etc. [16]. This paper is focused on discussion of imbalances in redistribution of fiscal powers and spending activity based on the amendments to the Constitution of Russian Federation affecting sustainability of regions.

2. Objectives of the study

We present the following hypothesis for the paper. Supporting the centralization trend in distribution of powers and as a result the fiscal centralization the constitutional amendments 2020 may improve communications between the center and the regions which is relevant for enhancing of regional sustainability in Russia.
Our second hypothesis is that the new constitutional phenomenon “federal territories” initially meant for ecological purposes, environmental protection and local development support in fact became an unclear tool at the disposal of federal center. This may cause new uncertainties in the redistribution of fiscal and other powers between center and regions and further asymmetries in the development of Russian regions.

3 Methodology

The general scientific methods like analysis and synthesis, deduction and induction were used in this study, as well as methods specifically meant for legal studies like economic analysis of law, comparative legal methods.

This research is based on the Constitution of Russian Federation with amendments made by the Law of Russian Federation of 14, March 2020 No 1-FKZ “On improvement of the regulation of certain public governance organization and functioning issues”. This research is referring to codified acts and other relevant legislative acts concerning public finance and fiscal relations. The main acts referred in this study include: The Tax Code of Russian Federation, The Budget Code of Russian Federation, The Federal law of 10, June 2016 “On the general principles of the organization and activity of the public authorities in the subjects of Russian Federation”.

The Federal Law of 22, December 2020 No. 437-FZ “On the federal territory “Sirius” is relevant for the discussion of the new type of administrative and territorial units in Russian Federation.

The study refers also to the analytics in mass media forming the context of the constructional reform and providing the information about the legal acts’ implementation.

4 Results

Amendments to the Constitution 2020 supported the centralization trend with further concentration of finance in the center. Due to the constitutional reform the representation of regions is reduced in the legislative branch but by means of the State Council now regions have better opportunities to communicate directly with the President of Russia. Better understanding of the regional needs may alleviate imbalances in the regional development improving sustainability of regions.

After 2020 the Constitution of Russia comprises a novelty - “federal territory” initially discussed as a tool for ecological, environmental, and social problems resolving. Now the legal framework for federal territories raises concern as a possible cause for new asymmetries including the fiscal imbalances.

By now there is only one federal territory in Russia – Sirius. Sirius shows an example of spontaneous administrative unit formation within a region. Moreover, the fiscal basis of Sirius is unclear, but the legislative norms which are already in force suggest possible fiscal inequalities around Sirius. Krasnodarsky krai – constituency where Sirius is situated - shall be deprived of the incomes generated by this innovation technology center which amounts to ongoing unjustified imbalance. The lack of legislative framework of federal territory creation leaves the constituencies of Russian Federation with uncertainty of their fiscal potential and affect their sustainability. This finding points out to the issue of federal territories in Russia advising the legislators to address the predictable and fair legislative framework for federal territories creating process.

5 Discussion

Constitutional reform 2020 contributes to the centralization and therefore has a substantial influence on regional development in Russia. Quite a few constitutional amendments 2020 are concerned the bodies representing the interests of constituencies on the federal level, namely - the Federal Council and State Council.

The Federal Council is the upper Chamber of the Federal Assembly - parliament of the Russian Federation. The Federal Council is formed with representatives of regions and its main purpose is to protect the interests of regions with no difference in territory or economic potential. The Federal Council may veto any federal law. All the laws concerning finance like laws on taxes and federal budget need to be approved by this legislative chamber. In fact, the Federal Council used to speak up for the regions in fiscal matters many times before. Mostly the Federal Council insisted on reimbursement for regional budgets than they lose their inflows due to the regional tax allowances established by federal laws. For example, the Federal Council insisted on compensations for regional budgets when movable property was exempt from regional taxes in Russia.

Since 2020 the representation of regions in the Federal Council has been reduced. Amendments 2020 introduced the federal representatives appointed by the President of Russian Federation amounting to 30 members which is 15% of the votes in the updated the Federal Council. It should be mentioned that Presidents
Another body related to the regional representation after 2020 started to enjoy a constitutional status. It is the State Council which used to be regulated by federal laws. Constitutional amendments 2020 introduced the State Council as a part of federal level of power and vested the President with the right to form the council with regional representatives. More detailed regulation of the State Council is provided by the Federal Law of October, 08 2020 № 394-FZ «On the State Council of Russian Federation». One of the key powers of the State Council is the review of federal budget drafts. As the State Council is stuffed with representatives of regions it keeps on representing the interests of constituencies and municipalities of Russia. Even though the State Council plays only a consultative role. Main purpose of the State Council is to ensure the uniform functioning of the vertical axis of public authorities including the regional and municipal powers [17]. It could be suggested that this approach contributes to the centralization trend as well.

Centralization means that financial resources will be allocated to regions from the center rather than derived from the local sources. This model elaborated in Russian Federation in 1997-2006. Federal legislation step by step limited the fiscal powers of regions and established strict control of the federal government over the financial flows. Most of the limitations were challenged by regional authorities in Constitutional Court:

- Ruling of the Constitutional Court № 5-P dated March, 21 1997 on Law of Russian Federation “About principles of tax system in Russian Federation” - fiscal powers of regions are limited by list of regional taxes established by federal law. Regions may set a tax rate for regional tax only in limits are established by federal law.

- Ruling of the Constitutional Court № 12-P dated June, 17 2004 on provisions of Budget Code about maintaining of settlement accounts of regions in Central Bank only - federal law may stipulate special rules for maintaining of funds regional and local budgets to secure unit financial system of the Russian Federation, its stability and transparency.

- Ruling of the Constitutional Court № 10-P dated December, 15 2006 on provisions of Budget Code about control of cash flows of regional budgets by the Federal Treasury - control of cash flow of regional and local budgets on federal level shall increase efficiency and transparency of government expenditures and secure unit budget system.

The Constitutional Court justified the limitation of regional fiscal powers. Lack of fiscal powers of regions and local governments affected the financial potential of regions causing disbalances. Only a minor part of regions could be characterized as wealthy (Moscow, Tatarstan, Saint-Petersburg, etc.), while the others are not sustainable without financial aid from the center.

Centralization helps to eliminate inequality of regions through redistribution of financial flows from rich regions to poor regions in the nearest prospective. However, it is also true that the federal center not always efficiently redistributes the finance omitting some disparities and ignoring the needs.

Redistribution of financial aid for the regions from the center is mostly based on the minimum social standards ensuring that any citizen residing in any region of Russia gets equal minimum of public services. However, it is quite a formal criterion sometimes ignoring real needs of locals. Comparing the regions of Russia, it becomes obvious, that Siberia regions differs from Far East regions in many ways and differences affect the needs of their citizens.

The State Council as a council which is really close to the decision-taking process can be expected to improve the communication between regions and center providing more efficient finance allocation.

Besides the set of amendments reforming the federal level of powers there is a totally new phenomenon in the Constitution of Russia after amendments 2020 – “federal territories”. The members of working group drafting the constitutional amendments 2020 commented many times that federal territories are introduced in the Constitution for ecological needs, better protection of special natural zones like Baikal Lake, Mineral sources of Caucasus etc. In fact, these purposes were never expressed in the legislation. Ecological purposes of federal territories have not been discussed after the constitutional amendments 2020 came into force. The reformed constitution allows the federal government of Russia create federal territories in any part of Russia. Federal territory can be set by federal law presenting the legal regulation for the specific federal territory.

The Constitution does not elaborate the regulation of federal territories. First federal territory – Sirius - was created in December 2020 and it could be characterized as spontaneous and a roughly designed. Federal law created federal territory Sirius seems to be “ad hoc” law. It means that Sirius regulation cannot serve as a model and unlikely to be replicated for the other federal territories created in the future. Now there is a
considerable uncertainty for the regions because federal territories can appear within their territory all over the sudden.

It could be logically expected that federal territories get finance as an allocation from the federal budget without its own right to budget. However, according to the Federal law the federal territory Sirius has its own budget which is neither a part of the federal budget nor a part of regional budget.

In terms of location the federal territory Sirius was ringfenced from the territory of the city of Sochi encompassing the Olympic village left from the Olympics 2014. The purpose of federal territory Sirius - is to be an innovative technology center. Sirius will have its own public authority which is somewhat like a hybrid of state authority and municipality. System of public bodies of Sirius includes the Federal Territory Sirius Administration and the Federal Territory Sirius Council. First temporary acting head of Administration was appointed by the Russian President.

Since December 2020 when Sirius was created there were no relevant updates to budget and tax legislation. Only in June, 2021 some changes in Budget Code and in Tax Code were issued which are coming into force on January, 1st 2022.

Regional taxes for Sirius are to be set by the Tax Code, but local taxes are to be set by the Federal Territory Sirius Council within the legally provided limits.

The updates to the Budget Code have not ruled on the budget of federal territory Sirius. The law allows only financial transfers from budgets of Krasnodarskiy krai and city of Sochi to the budget of federal territory and the retrieval of financial aid.

It follows from the federal law about federal territory Sirius that the budget of Sirius: may be formed by regional and local taxes collected in Sirius, financial support from the federal budget, budget of Krasnodarskiy krai and city of Sochi. There is also a possibility to get income from property, pertaining to the federal territory. The question about the share of federal taxes collected in Sirius and some non-tax incomes (like fines and penalties) is still unresolved.

The Sirius’ public expenditures are not regulated properly by fiscal laws. At least there is a special infrastructure legacy of Olympics 2014 and at the same time there is a normal living infrastructure as well. It is likely that the maintenance of usual living is still left on the Krasnodarski krai and the city of Sochi. The issue of delegation of powers and relevant financial transfers are not addressed in the current legislation. At the same time, it is quite clear that Krasnodarskiy krai and the city of Sochi lose the income from federal territory advanced development if it really becomes a innovative technology center. According to financial legislation Krasnodarskiy krai cannot enjoy revenues from the newly created federal territory although it is situated within its borders.

Sirius provides a clear example of financial powers’ distribution inconsistencies. Sirius’ can receive financial aid from all three levels of budgets, but the regulation of expenditures is unclear. Special fiscal regulation may be justified or not as the Olympics and the relevant infrastructure were financed mostly from the federal budget, but in any case, we deal with a serious financial distortion here which can be further replicated with the forthcoming federal territories.

Spontaneous creation of federal territory in any region of Russia increases financial disproportions around such new administrative unit. Relevant regions and municipalities are deprived revenues derived from development of federal territory, but they are likely to bear costs of living infrastructure, labor resources and other maintenance costs which are supposed to be shared with federal territory.

6 Conclusion

Regions now have less representation in the upper chamber of legislative branch for bringing their key needs in Russian legislation. However, the State Council gained more sound status and therefore regions are better represented in the executive branch although it is a mostly consultative role. The new structure of the constituencies and municipalities representation may result in better center-regions communication. Better understanding of the needs in the peripheries provides the basis for more efficient allocation of finance for solving the ecological, economic, and social problems in the regions.

Constitutional reform brought a new actor – federal territories promising them to be a tool for better protection of environment and ecologic use. However, no clear strategy for federal territories role could be identified by now. First and the one federal territory by now is the innovative technology center Sirius created within the borders of the Olympic village in the city of Sochi. Sirius was created somewhat spontaneous, and it is a very special federal territory related to the inheritance of Olympics 2014. Sirius does not give an idea
what kind of federal territories may be created further. While the way how Sirius was established provides uncertainty for the constituencies of Russian Federation. It is rather difficult to predict what kind of federal territories may be created in the future.

Spontaneous creation of federal territories leads to asymmetries and disproportions in the fiscal basis of territories in Russia.

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