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## **Regional Investment Policy in The Context of Economic Growth, Employment and Income of the Population**

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**Abstract:**

**Purpose:** *The purpose of the article is to substantiate proposals for expanding the tax independence of sub-federal authorities, that will activate the investment processes.*

**Design/Methodology/Approach:** *Domestic and foreign conceptions on the issue of state support for investment activity, as well as open data of the government of Rostov Region are used in the article. On the basis of the systematic logical and semantic analysis, the comparison, and the theoretical and practical materials synthesis the authors analyzed measures of regional support for investment activity.*

**Findings:** *The investment attractiveness of each region directly depends on the created comfortable environment for business, capable to finance various sectors of the economy. The possibility to use tax incentives encourages investment activity of economic entities. The authors propose to expand the tax independence of the Russian Federation's subjects through simplifying the investment tax deduction mechanism, restoring tax powers in terms of reducing the corporate income tax rate credited to the regional budget.*

**Practical Implications:** *The research results can be used by state authorities and administrative bodies of the Russian Federation's subjects for improving tax support for investment processes.*

**Originality/Value:** *The proposed measures aimed at expanding the sub-federal government tax independence will ensure the investment processes activation contributing to the economic development of the regions, the employment growth, income and savings.*

**Keywords:** *Investment attractiveness, forms of state support, tax benefits, special investment contracts, tax costs, economic growth, employment recovery.*

**JEL Classification Codes:** G23, H20, J23, O10.

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## **1. Introduction**

Investments is a basis of the competitive economy, an important tool for the functioning of the economic system, increasing the labor productivity and, as a result, improving the life standard of the population (Garina *et al.*, 2020). The key indicator of the economic growth is investment in fixed assets, which indicates the investment attractiveness of business and characterizes the business climate in the country. In accordance with the Decree of the President of the Russian Federation from 7.05.2018 "On national goals and strategic tasks of the development of the Russian Federation for the period up to 2024" and the Message of the President of the Russian Federation from 15.01.2020 by the end of 2024 the capital investment volume should increase to 25% of the GDP. The task is extremely difficult. Unfortunately, the pandemic had a negative impact on the economy and the social sphere, but it is necessary to achieve strategic goals nevertheless.

Investment policy is a priority for every subject of the Russian Federation, so it is important for them to receive both domestic and foreign investments (Loginov and Karanina., 2019). "... the created conditions for attracting them will provide expanding production, developing popular sectors of the economy, increasing employment, and the growth of the socio-cultural facilities number, which will ensure the sustainable development" (Samoylova *et al.*, 2019).

## **2. The Regional Investment Policy Results Analysis**

### **2.1 Factors Determining the Investment Attractiveness of the Region**

So far, Rostov region has formed the legislative framework to support the relevant investment activity, monitoring the development level and trends in investment activity, and providing conditions for the investment infrastructure formation. Regulation and support of investment activity by the sub-federal government makes it possible to create the image of Rostov Region as an attractive investment region.

According to the authors, "the investment attractiveness of the Russian Federation' subjects directly depends on the measures taken by state authorities to create a comfortable business environment and then attract investors who will invest their own funds to various sectors of the economy. Thus, each region strives to create the most favorable and attractive conditions for investors who are able to invest financial resources to promising projects".

The main factors that determine regional investment attractiveness include: convenient geographical location, natural resources availability, human capital quality, developed infrastructure and institutional environment, high production potential of the regional economy, balanced budget and financial stability of economic entities (Dzwigol *et al.*, 2019). The contents of the listed factors for Rostov Region are presented in Table 1.

**Table 1.** *Factors forming the Rostov Region investment attractiveness*

<b>Factors</b>	<b>Essence</b>
Geographical location	Favorable geographical location, as well as the most important geopolitical significance of Rostov Region for the Russian Federation
environmental resources	The various mineral resources availability, energy intensity of the territorial economy, 65% of land resources are black soil
Human capital quality	A great number of economically active population, high indicators of life expectancy and life standard, level of education, labor productivity.
Developed infrastructure	The development high level and the transport accessibility (Railways, highways, sea and river ports, international airport), energy and telecommunications infrastructure
Social stability	The real disposable income and purchasing capacity of the population are high enough.
Production potential of the economy	The annual growth of the gross regional product (GRP) during 2015-2019, from 1189.1 billion rubles to 1516.57 billion rubles, by 125.7%. The GRP grew in 2019 compared to 2018. It was 4.5%. In 2015-2019, the region's economy attracted about 1.4 trillion rubles, with the support of the Rostov Region government, more than 1,200 projects worth about 380 billion rubles were implemented.
Institutional environment	The institutional environment has been created that clearly defines the conditions for the functioning and the development of business entities, and regional legislation works, including the interaction of state authorities and investors, complying with requirements
High quality of public finance management	The proper quality of public finance management is ensured (budget revenue dynamics, budget balance, public debt volume), and program and target budgeting is developed.
Financial stability of economic entities	The sufficient financial stability of economic entities, normal state of accounts payable and receivables, the investment resources availability

*Source: Own study.*

Investment projects in recent years, such as the construction of Platov Airport, the Rostov Arena Stadium, the bridge over the Don, new roads and transport interchanges, as well as projects in the field of wind energy, the seaports modernization, the development of logistics infrastructure for e-Commerce, investment in human capital: education, health, culture, and a comfortable urban environment, have changed the life standard in the region and the business environment. In 2019, more than 160 projects worth about 30 billion rubles were implemented in the region due to private investments, including the company "AI-Plast" plant, with the investment of 1.2 billion rubles, the logistics complex of "A" class of the "FM Logistis" company with a total investment of 2.5 billion rubles.

In 2020, it is planned to run 250 projects worth about 55 billion rubles. Such a significant amount of investment indicates the confidence of business in the economic

policy pursued by the Don authorities, and the formation of quite comfortable conditions for it. These conditions, in turn, directly depend on the measures for the implementation of state support for investment activity undertaken by the government and management bodies of the Russian Federation's subjects.

## 2.2 Forms of Regional Investment Support

In accordance with regional legislation, companies implementing investment projects in Rostov Region can get state support, the forms of which are presented in the Table 2.

**Table 2.** *Classification of forms of state support for companies engaged in investment activity in Rostov Region*

Groups of government support forms	State support form
I. Small business support	Providing sureties Provision of leasing services Preferential loans for SMEs (small and medium-sized enterprises) Engineering services Formation and development of clusters Support for exporters Regional industrial development Fund
II. Program of financial support to business	Program of concessional lending to small and medium-sized business (Program 8.5). <sup>6</sup> Program for stimulating lending to small and medium-sized business of JSC " Federal Corporation for the development of small and medium-sized business» Preferential lending to agricultural producers Engineering subsidies Innovation subsidies Single-industry towns development Fund (Donetsk, Gukovo, Zverevo)

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<sup>6</sup> *The preferential crediting program is a joint program of subsidizing the Ministry of economic development of Russia and Joint stock company "The Federal Corporation for the development of small and medium-sized enterprises" (SME Corporation) in accordance with the decree of the Government of the Russian Federation from 30.12.2018 No. 1764 (in edition of the Russian Federation government resolutions No. 571 from 08.05.2019, No. 629 from 21.05.2019, No. 1204 from 18.09.2019, and No. 1927 from 28.12.2019). The preferential crediting program to small and medium-sized businesses within the framework of the national project "Small and medium-sized entrepreneurship and support for individual entrepreneurial initiative" was launched in February 2019 and it is planned to last until 2024. 90 banks participating in the program issue loans to entrepreneurs at a reduced rate of up to 8.5% per annum, and the state compensates credit organizations for lost profits.*

III. Tax support	Tax benefits for investors, including investment tax deduction Special investment contracts Tax benefits and preferences for residents of territories of advanced socio-economic development (ASED) formed in single-industry towns
IV Non-financial forms of support	Investment projects support in Rostov Region 100 gubernatorial investment projects Investment Council under the Governor of Rostov Region

*Source: Own study.*

### **2.3 The Role of Regional Legislation in Attracting Investment**

It is the most urgent for investors to get regional tax support in a form of tax benefits, additional to federal ones. The study of legislation on taxes and fees presents that the legislative bodies of the Russian Federation's subjects can establish tax benefits along with other elements of taxes relating to regional taxes (corporate property tax, transport tax, gambling tax), corporate profit tax, the simplified tax system (STS) and the patent tax system (PTS) (2020). It is important for them to find a balance between regulatory and fiscal functions of taxes, stimulating the economic growth and providing necessary income to regional budgets to finance current costs, capital investment, innovation, regional programs, national projects, and anti-crisis support of business and population in conditions of the pandemic.

It is important to pay take into consideration the fact that tax powers of sub-federal authorities are unstable and limited, they have a different structure for specific taxes. For example, it is possible for legislative authorities of the Russian Federation's subjects to impose regional taxes on its territory, to establish specific tax rates limited by federal law, the procedure and terms of payment, their own tax benefits in addition to the federal ones; as for the corporate income tax they can reduce the tax rate to the regional budget and introduce an investment tax deduction (2020).

If before 2019 it was possible to reduce the tax rate for any category of income tax payers, from 2019 only "... for the residents of special economic zones, participants of the special economic zone in Magadan Region, participants of regional investment projects, participants of the free economic zone (Crimea, Sevastopol), advanced development territories residents, residents of the free port of Vladivostok provided for in article 284 of the Tax code of the Russian Federation" (2020).

In our opinion, these measures restrict the tax independence of regional authorities, as a result it is impossible for them to introduce their own taxes, raise tax rates above the level established by the Tax code of the Russian Federation, and cancel federal tax benefits for regional taxes (Rukina, 2019).

The analysis of the regional law provisions "On regional taxes and some taxation issues in Rostov Region" presented its stimulating value for the growth of investment in the economy. Investors who carry out investment on the territory of Rostov Region

have reduced rates for the payback period of the investment project provided for in the project documentation, but not more than for five years:

- for corporate income tax:

a) in terms of investments to the regional budget of Rostov Region in amount of 13.5% (reduced by 3.5 p.p. from 17.0%);

b) in the amount of 0% for organizations which are advanced development territories residents (there are 3 of them – "Gukovo", "Zverevo", "Donetsk") and which have concluded special investment contracts with the participation of the Russian Federation;

- on the property tax of organizations in the amount of 1.1% (restrictions not exceeding 2.2%) relating to newly created (acquired) property within the investment project and exemption from payment relating to newly created property of organizations – advanced development territories residents and newly created property on the territory of the industrial Park. Tax benefits for corporate property tax and corporate profit tax for legal entities that are advanced development territories residents have been in effect in the region since 2016 (2020).

The following indicators confirm the stimulating investment results. In 2017, 45 large investors took advantage of regional tax benefits in the framework of 72 investment projects; they transferred 14.6 billion rubles to the Rostov Region's consolidated budget (10 rubles for 1 ruble of tax benefit), created and maintained workplaces, and increased salaries for employees. By the end of 2018, 50 large investors under 75 investment agreements benefited mainly from corporate property tax benefits. Taxpayers under 23 investment contracts (33.3% of the total number of contracts) took advantage of the reduced corporate income tax benefit. Organizations that got investment support transferred 7.05 billion rubles to the consolidated budget of Rostov Region in 2018 (3 rubles for 1 ruble of tax benefit). In 2019, 50 organizations got property and profit tax benefits in the framework of the implementation of 70 investment projects. 11 new investment contracts were signed with investor organizations for providing regional tax benefits, as well as 15 additional agreements on amendments to existing investment agreements. By the special investment contracts number, Rostov Region takes the 5<sup>th</sup> place in the country (5.6 billion rubles) and the 1<sup>st</sup> in the Southern Federal district in terms of public-private partnership development. During two years, four contracts were signed. They will bring more than 5.6 billion rubles of investment and create hundreds of workplaces. Some of the special investment contracts are connected with wind energy.

From 2020, the investment tax deduction applies to organizations that pay income tax. The legislative bodies of the Russian Federation's subjects have received the right to introduce it since 2018. "The investment tax deduction grants organizations the right to reduce the amount of calculated income tax on costs related to the acquisition or the modernization of fixed assets; with donations to state and municipal cultural institutions; financing the creation of infrastructure facilities on the territory of the

Russian Federation's subjects and in the adjacent water area that are exclusively in Federal ownership (Rukina *et al.*, 2019).

During two years, more than 20 subjects of the Russian Federation have introduced the investment tax deduction (ITD) in their territories. It can be assumed that regions were not interested in the investment tax deduction conception due to the complex mechanism with numerous restrictions and nuances, which the authors drew attention to in the article "Tax support for private investment into education" (Rukina *et al.*, 2019). In Rostov Region, the right to use the ITD was granted to organizations with the priority activity for the region, organizations participating in the national project "Labor productivity and employment support", organizations making donations to state and municipal cultural institutions (clubs, museums).

For the sustainable socio-economic development and minimizing the negative impact of coronavirus infection in the region, tax benefits and preferences for business existed before have been preserved. Moreover, they are supplemented by the important measure. It is rate reduction in all the special tax regimes for the most affected sectors of the economy during 2020. As a result, the volume of tax payments will be reduced and, consequently, the tax burden on business entities.

Tax benefits are known to lead to the regional budget income loss. In the context of complete transition to the program-target budgeting principles, the term "tax costs" has been introduced in Russia legislatively. The relationship of tax costs with the goals both of state programs and the socio-economic policy is implemented by including their volumes in the state programs financing.

From 2020, the financial authorities of the Russian regions will have to evaluate the tax costs efficiency according to the methodology developed by the Ministry of Finance of the Russian Federation. The contribution of the tax benefit to the change in the value of the indicator for achieving the goals of the state program, the tax costs budget efficiency, and the total budget effect will be evaluated. It may lead to the inefficient tax benefits cancellation (Klimanov and Mikhailova, 2020).

### **3. Research materials and methods**

As the methodological basis of the research, the authors used general scientific methods of cognition such as the systematic logical and semantic analysis, the comparison, the theoretical and practical materials synthesis. Through these methods it was possible to investigate the ways of regional support for investment activity and suggest measures for their improvement. The information base of the research was open data of the government of Rostov Region, published on its website. Scientific works on these issues are very versatile, they are connected with the importance of investments for the region's development (Loginov and Karanina, 2020), the conditions for attracting them (Dzwigol *et al.*, 2019), and tax support (Rukina, 2019).

Despite a large number of publications and the national legislation improvement it is still difficult to activate investment processes contributing to the recovery of the economy and incomes of the population.

#### **4. Conclusion**

It is necessary for the sustainable economic growth, increasing the employment, real incomes and savings, as well as stable revenues to regional budgets to activate investment processes in Russian regions, especially investment in fixed assets (Denisova *et al.*, 2017). Taking into account the socio-economic development peculiarities, each subject of the Russian Federation offers investors various forms of investment support.

In the current circumstances, the tax independence of sub-federal authorities for which the positive economic dynamics, the employment restoration, and the strengthening of financial and investment potentials are primarily important should not be restricted. It is necessary for this to ensure the tax legislation stability for the period up to 2024, simplify the ITD mechanism, restore the tax power in terms of reducing the corporate income tax rate credited to the regional budget for all the categories of payers, set the limit on tax costs for sub-federal authorities in the range from 3% to 8% in the regional budget tax costs instead of a complex system of tax costs estimates. It will increase the self-sufficiency level of regions, create conditions for the tax competition and the favourable business climate. Of course, it is necessary to speed up the adoption of the draft law "On protection and promotion of capital investment and investment activity development" being formulated by the Ministry of Finance of the Russian Federation, contributing to the favourable business climate formation.

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