

# Constructing the Russian Arctic as a Special Economic Zone

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*The Russian Federation has the biggest land area in the Arctic and has been gradually expanding its definition by joining new regions and territories that previously were not considered Arctic to its Arctic Zone of Russian Federation (AZRF). In recent years, two incentivizing programmes, the Arctic Hectare and the Resident of the AZRF, were introduced to stimulate the social and economic development of the AZRF. The resident status in the AZRF provides an investor with a set of privileges for investment activity, including tax incentives. From 2020 to November 2022, 510 companies received the status of resident and are collectively all support programmes are expected to contribute to over 33,400 new jobs. This study is aimed at comprehensively reviewing the construction of the AZRF concept as a Special Economic Zone. In the analysis, I focus on the business incentivizing programmes through the lenses of sustainability, hence identifying how economic, social and environmental concerns are incorporated into the Resident of the AZRF programme. Results demonstrate that the economic pillar of sustainability outweighs social and environmental concerns in the construction of the Russian Arctic as a Special Economic Zone.*

## Introduction

The Russian Arctic has been the focus of development by the Russian state. The last 15 years saw growing attention to the Arctic in Russia, which has been reflected in legislative and strategic efforts. Strategic documents for the future of Arctic development in Russia position Arctic territories as a strategic resource base to accelerate the country's economic growth, improve socioeconomic conditions of local populations, and protect the environment and Indigenous peoples' original habitat and traditional way of life in this territory.

Economic growth in the Russian Arctic is fuelled by extractive industries. Rapid industrialization and urbanization of the Russian Arctic affects local communities and Indigenous Peoples that continue to face difficult socioeconomic conditions, including the loss of their traditional homes and methods of natural resource management due to land allocations for industrial development or pollution of land, water, and other natural resources.

The recent addition to the management of Russian Arctic territories was the introduction of the Federal Law “On State Support for Investment Activities in the Russian Federation's Arctic Zone” in July 2022, which creates a set of preferences and benefits for large, medium, and small businesses willing to invest in developing the Russian Arctic (Federal Law 2020, N-193-FZ). The law makes the whole territory of the Arctic Zone of the Russian Federation (AZRF) equivalent to a Special Economic Zone (SEZ) with a defined set of benefits and appointed a managing company in the name of Far East Development Corporation. This approach is novel for modern Russia because it involves support mechanisms not for specific sectors, but the whole AZRF when the state puts efforts and resources to enable the region's growth. Some initial studies investigate quantitative and qualitative indicators of the current state of AZRF, including the number of residents, their business activities, and their relationship to future investment projects (Anciferova & Vasil'eva, 2021). However, the empirical base is rather small due to the novelty of the support mechanisms.

The purpose of this study is to conduct an in-depth analysis of the AZRF idea as it relates to the creation of a Special Economic Zone. In the analysis, I trace the creation of AZRF from a historical perspective and later highlight incentive programs from the lenses of sustainability, thereby highlighting how economic, social, and environmental issues are incorporated into these initiatives. In addition, I assess how international sustainability frameworks, such as the United Nations' Sustainable Development Goals, are reflected in these programs.

The article proceeds as follows. Section 1 discusses methodology and data. Section 2 reviews the literature on Special Economic Zone (SEZ) research. Section 3 provides evidence of the development of the AZRF concept and its composition. Section 4 focuses on the business incentivizing programmes in AZRF and Section 5 provides results and discusses challenges regarding these programmes from a sustainability angle. Section 6 concludes.

## **Methodology and data**

The study builds on reviewing the development stages of the AZRF in line with regulatory changes and by looking at the expansion of the AZRF composition. A review of SEZ literature is evoked to see how the current regime in the AZRF corresponds to international practices, especially on the sustainability dimension.

The data is gathered from the regulatory legal acts of the Russian Federation, the Federal State Statistics Service, and publications of domestic and foreign scientists. Since the incentivizing programmes for the development of AZRF are relatively new starting from 2020, there is still a very limited number of scientific publications. Comprehensive statistical data is lacking. Hence findings from this study are of an exploratory nature.

## **Literature review on Special Economic Zones**

Special economic zones (SEZs) are areas with particular economic advantages, for example lower taxes than the rest of the country to encourage investment. SEZs are generally defined as geographically delimited areas that are administered by a single body. These zones offer certain incentives to businesses that are physically located within the zone, such as generally duty-free importing and streamlined customs procedures (FIAS, 2008).

Most developing and many developed economies use SEZs. Within these delimited areas, governments provide fiscal and regulatory incentives and infrastructure support. In 2019 there

were 5,400 zones in 147 economies, up from 4,000 five years ago, and 500 more were in the works. The SEZ surge is part of a new wave of industrial policies and a response to competition for international investment (UNCTAD, 2019). Developed countries have basic free zones for trade logistics. Developing economies use multi-industry, specialized, or innovation-focused integrated zones for industrial development. New SEZs and development programs are emerging. Some SEZs focus on high-tech, financial services, or tourism instead of trade- and labor-intensive manufacturing. Others emphasize environmental performance, science commercialization, regional development, or urban regeneration.

The premise under which SEZs are created is that they attract investment, create jobs, and boost exports directly and indirectly by building economic links. Zones support Global Value Chain (GVC) participation, industrial upgrading, and diversification. However, these effects are not automatic. In fact, many zones underperform. SEZs aren't a prerequisite or guarantee for higher Foreign Direct Investment (FDI) or GVC participation. Most zones grow at the same rate as the national economy after the build-up period and many zones become enclaves with limited impact (UNCTAD, 2019).

### ***Special Economic Zones in developing countries***

In the Chinese context, Liu et al. (2007) investigated the interaction of economic growth and environmental quality in Shenzhen, the first SEZ in China established in 1980. The massive growth of infrastructure, industrial sites, and urban communities has drastically altered the local environment. Authors apply the Environmental Kuznets Curve (EKC) which is built on a hypothesis that the relationship between economic growth and environmental degradation is inversely U-shaped, meaning that environmental pollution increases in the early phases of economic growth and environmental quality improves as income levels rise. The results by Liu et al. (2007) demonstrate that production-induced pollutants support EKC while consumption-induced pollutants do not support it. When it comes to Shenzhen's economic development, foreign investment and joint ventures were essential in creating economic growth (Liang, 1999). A study by Zhao et al. (2022) investigating a link between special zones in China and their environmental impacts finds that lower investment standards and concentrated pollution from industry agglomeration harm the environment.

Zheng et al. (2016) studied the effects of development zones on the economic development of host regions in China. Macro-level data analysis revealed that development zones, while beneficial in developed regions, do not contribute to economic growth in proportion to their land share in host cities. The authors propose that the central government of China should not expand development zones without limits, but rather should give careful consideration to the location and size of proposed development zones in relation to the regions that will host them before approving any of them.

In India, the introduction of SEZ in 2006 was aimed at improvement in terms of exports, employment, and infrastructure. At the same time, the states that introduced SEZ were accused of land grabbing. According to the findings by Akon (2018), these SEZs have not been successful in bringing about the socioeconomic development of the local community because Indian state politicians use state-owned development corporations for rent capture, which undermines the potential efficacy of SEZs. One reason for the failure of SEZs is the lack of the right incentives for local politicians.

Concentrating only on creating an investor-friendly industrial zone in the state of Jharkhand in India led to violation of the rules and ignoring the needs of other stakeholders. As a result, Jharkhand granted project approval to businesses even though no public hearings were held and little or no input from the affected communities was obtained. Jharkhand acquired privately owned land for industrial estates on behalf of private companies and established district-wide land banks (Sundar, 2011). Chaudhuri & Yabuuchi (2010) found that without government spending on irrigation projects and other infrastructural development, SEZ formation hurts agriculture in India. If agriculture receives more than a critical level of government aid, agricultural wages and economic employment may improve. To fully benefit from the SEZ policy, agriculture and industry must be balanced. The creation of SEZ relied heavily on the acquisition of vast acreage of land for new industries and mines as well as for large-scale farming and infrastructure projects. Tension over land deals in the Indian state of Goa was intensified by the introduction of Special Economic Zones (Bedi, 2015).

In the Russian context, the region of Kaliningrad represents an SEZ case study in which the development of the region over 20 years reformed from customs tariffs to profit taxation preferences in the environment of institutional instability. In the framework of the SEZ, a study by Garaeev (2013) concluded that the trade-off must be made between economic stimulation programs and economic efficiency in the Kaliningrad region.

Overall, the development of SEZs while beneficial economically can have potentially negative environmental and societal impacts. Also, since the beginning of special economic zones advancement in developing countries, people have been concerned about how zones affect employment (in terms of gender, wage levels and benefits, worker rights and working conditions, and worker rights in general), the environment, and other social factors that are related to employment (FIAS, 2008). To alleviate such imbalances design of SEZs requires holistic thinking, for example, by applying the UN Sustainable Development Goals and by incorporating ESG principles in reporting and accountability. Potential land conflicts, stakeholders' concerns, and the role of public opinion and acceptance are crucial for the functioning of SEZs. The primary goal needs to be that special economic zones (SEZs) work toward the Sustainable Development Goals (SDGs), transforming them from privileged enclaves into sources of widespread benefits (UNCTAD, 2019).

### **Arctic Zone of the Russian Federation**

The Russian Federation has the largest area of the Arctic contributing to 50% of the total Arctic area, 60% of the total Arctic population, and 75% of the Gross Regional Product (ECONOR, 2020). The location outside the Arctic Circle and access to the Arctic Ocean are the two most important aspects of belonging to the Arctic. Each Arctic state has its distinct characteristics, and in exceptional cases, the boundaries of their land Arctic territories have been expanded to increase the scale of state support for the development of the Arctic zone (Gal'tseva et al., 2022)

There are many criteria for identifying what means to be Arctic and different schools of thought on what to consider the Arctic. In his monograph "Many-faced Arctic in the stream of time and meanings", Yuriy Lukin lists the following criteria: geographical, socio-economic, and political-legal criteria. The Arctic Circle (66°33'44"); geographical differentiation of Arctic landscapes and zoning of territories; natural and climatic criteria; internal administrative-territorial boundaries of

subjects and external boundaries of territorial waters, exclusive economic zones of Arctic states; cultural and ethnic landscapes; Arctic communities; economies; and geopolitics (Lukin, 2019).

More specifically, in the Russian context, Zhukov et al. (2017) and Zhukov et al. (2018) propose the following set of criteria for a territory to be considered the Arctic:

1. Latitude-based UV deficiency subzone assignment:

Inclusion in the Russian Arctic requires, in the north, subzones of moderate UV deficiency (if other criteria are met).

2. Arctic and subarctic climates assessed by bioclimatic discomfort in life of populations.

3. Arctic/subarctic landscapes:

Except for Kamchatka and the Sea of Okhotsk coast, tundra and forest-tundra territories are included in the Russian Arctic. Adding northern taiga territories to the Russian Arctic is possible (if it is justified by other criteria)

4. CAFF-border as a criterion for inclusion in the Russian Arctic (if it is justified by other criteria).

5. Arctic specifics of economic systems:

Transport and economic gravitation to the Northern Sea Route and being in the zone of its influence; adjacency to the Arctic Ocean; peripherality, isolation, and remoteness of Arctic economic systems from large industrial centres; focal nature of the territory's development; pronounced uneven settlements, the concentration of people in settlements; mono- and oligoprofile of the towns.

Analysing the southern border of the Arctic as a biogeographic boundary, Doctor of Geographical Sciences Arkadiy Tishkov states that the decision on the composition of the Russian Arctic is “not the result of a physical-geographical, medical-biological or environmental scientific study, but a political act that takes into account natural, social, demographic and political realities, as well as the convenience of the state management” (Tishkov, 2012: 31).

From a legal perspective, the Arctic Zone of the Russian Federation was defined by the Presidential Decree of May 2, 2014 No. 296 as “On the land territories of the Arctic zone of the Russian Federation” (Presidential Decree of May 2, 2014 No. 296). The AZRF stretches across four Federal Districts in Russia (see Figure 1). Internal sea waters and territorial seas, areas of the Russian Federation's continental shelf, and land and islands that do not belong to foreign nations and could in the future be opened in the Arctic Ocean from Russia's coast to the North Pole are all included in the AZRF's territory.



Figure 1. Land territories of the Arctic Zone of the Russian Federation (Source: Troy J. Bouffard, 2020).

### Changes in AZRF composition

The composition of the AZRF changed three times since 2014 (see Figure 2) when the territories included in the AZRF were stipulated by the Presidential Decree of May 2, 2014 No. 296 (Presidential Decree of May 2, 2014 No. 296). Initially, the AZRF comprised territories of four northernmost Arctic regions and all their municipalities: Murmansk Oblast, Nenets Autonomous Okrug, Yamalo-Nenets Autonomous Okrug and Chukotka Autonomous Okrug. One municipality from the Komi Republic (Vorkuta), five municipalities from the Sakha Republic, three municipalities from Krasnoyarsiy Krai and six municipalities from Arkhangelsk Oblast were included in AZFR in 2014.

Consequently, in 2017, the Presidential Decree of the Russian Federation of June 27, 2017 No. 287 introduced amendments to the composition of AZRF by adding three municipalities from the Republic of Karelia (Presidential Decree of June 27, 2017 No. 287). The leadership of the Republic of Karelia had repeatedly advocated for the inclusion of Kemskey, Loutsky, and Belomorsky of the Republic bordering the White Sea, into the Arctic zone. This would make them eligible for federal budget subsidies in the millions of dollars for the development of coastal municipalities experiencing significant economic and infrastructure issues (Batov, 2017).

In his interview with the newspaper Izvestia, Professor Alexander Pilyasov stated that “in an attempt to change the status of the regions of Karelia, there is a certain artificiality, but it reflects the objective trend of raising the status of the Arctic territories against the northern ones, which is happening in our country” (Izvestia, 2017). The addition of three municipalities from the Republic of Karelia to AZRF was driven by the interest to raise the status of these regions, making them

eligible for budgetary funds aimed at social, industrial, and transport infrastructure development to assist in business development.

Further, in 2019 the AZRF expanded by the inclusion of an additional eight municipalities from the Sakha republic. According to the Decree of the President of the Russian Federation of 13.05.2019 No.220, the territories of the Abyisky ulus (district), Verkhnekolymsky ulus (district), Verkhoyansk district, Zhigansky national Evenki district, Momsky district, Srednekolymsky ulus (district), and Eveno-Bytantaisky national ulus (district) are included in the land Arctic zone (Republic of Sakha - Yakutia). All eight districts are fully or partially located beyond the Arctic Circle. Previously, the Arctic zone included five regions located along the coast of the Arctic Ocean.

The latest expansion is documented in the Federal Law “On State Support for Investment Activities in the Russian Federation’s Arctic Zone” (Federal Law of 13.07.2020-N-193-FZ). While the law was still in development it prompted some Russian Federation regions to justify the incorporation of new territories (municipalities) in the Russian Arctic. Eventually, three municipalities in Komi Republic, ten municipalities in Krasnoyarskiy Krai, and three municipalities in each Arkhangelsk and Karelia Republic were added to the list in 2020. The motivation to be admitted to AZRF territory is the result of a large-scale list of tax and customs preferences, as well as preferential normative regulation of labour relations for Russian Arctic residents (Khodachek, 2021).



**Figure 2.** Changes in AZRF composition (Compiled by the author).

It appears that the latest Federal Law on the AZRF takes a managerial approach and solves ambiguities in defining what territories are considered as Arctic in Russia. The list of all territories that are included in the AZRF presents what the Arctic is in the eyes of the legislator. The Federal Law determines the composition and status of the Russian Arctic that is used for supportive measures (e.g., entrepreneurial and infrastructure development support).

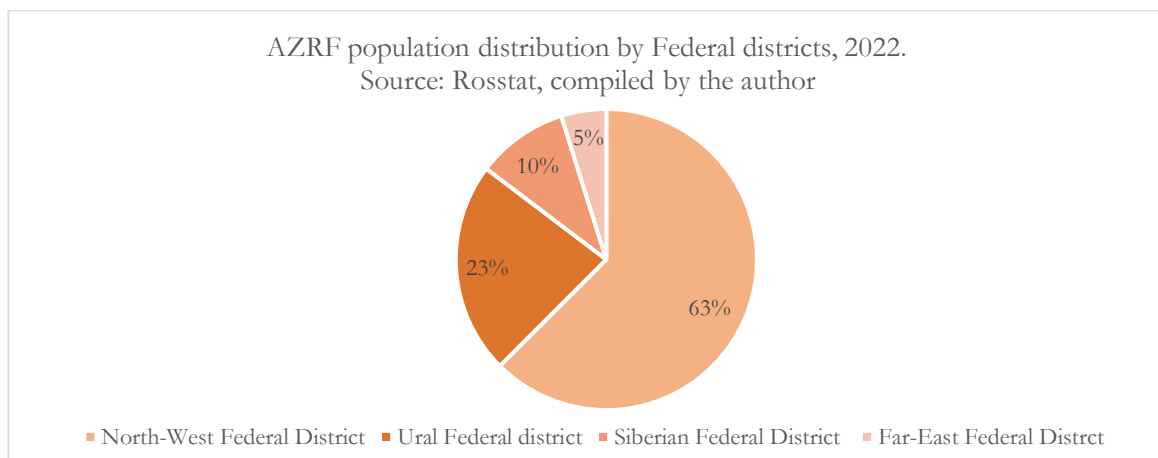
**Socio-economic characteristics of AZRF**

The population in the AZRF has been declining since 1990. Figure 3 demonstrates population change in the AZRF from 2014 when the concept was first introduced. Growth in population in 2020-2021 is stipulated by the inclusion of new municipalities, not by the natural growth of net migration. Preliminary results of the Population Census (2021) paint a not so favourable picture for the AZRF. In the AZRF areas that are fully included (Murmansk Oblast, Nenets Autonomous Okrug, Yamalo-Nenets Autonomous Okrug and Chukotka), the population has collectively reduced by 145,000 from 2010 to 2021 with the biggest decrease in Murmansk Oblast where it decreased by 16% or by 127,238 people.



**Figure 3.** Population in AZRF, million people, 2014-2020. Source: Rosstat, compiled by the author.

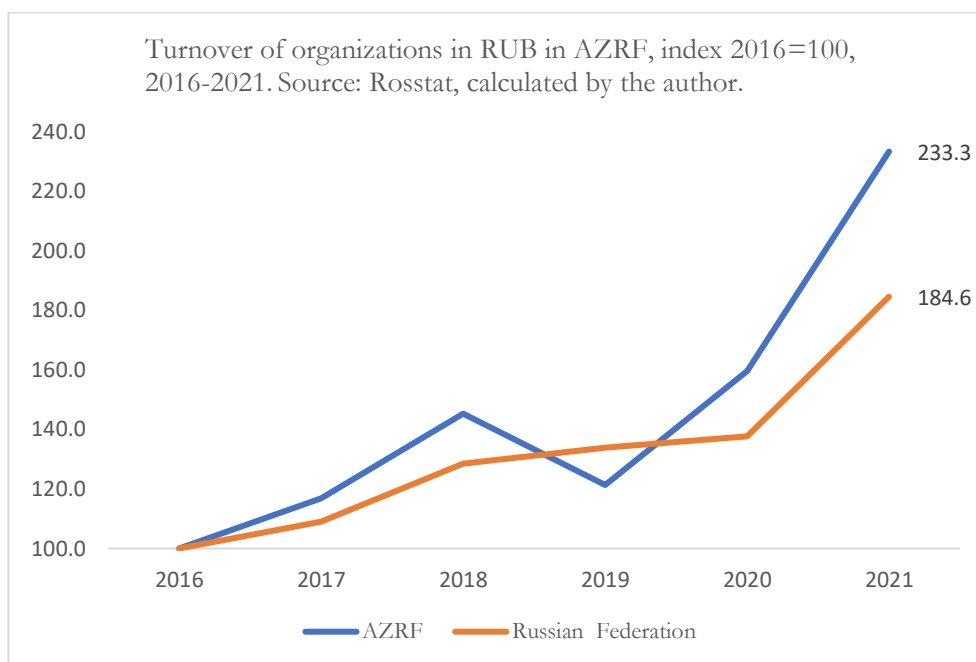
The population is not evenly distributed within the AZRF with the most densely populated regions being Murmansk, Karelia and Arkhangelsk situated in the North-West Federal District contributing to 63% of the AZRF population (see Figure 4). The population in AZRF is highly urbanized with 87% of the population living in urban settlements in 2021.





**Figure 4.** AZRF population distribution by Federal districts, 2022. Source: Rosstat, compiled by the author.

In terms of economic development, the AZRF has been ahead of the average turnover of organizations across Russia. Turnover is the sum of sales and other operating income. Figure 5 demonstrates the turnover of organizations in RUB expressed as an index for the period 2016-2021. The AZRF economy has performed stronger than the rest of Russia with turnover growth of 133% over 2016-2021 while in Russia the growth was 85% over 2016-2021. Note that the index is calculated using current prices.



**Figure 5.** Turnover of organizations in RUB in AZRF, index 2016=100, 2016-2021. Source: Rosstat, calculated by the author.

## Review of the business support programmes in AZRF

Business development in the Russian Arctic is affected by poor transportation accessibility, high energy costs, remoteness from administrative centres, and significant costs for compensation due to Far North employees' benefits, which comprise travel compensation every two years, regional coefficients and allowances (Emelyanova, 2019).

In this article, the focus is on the new Federal Law on state support for entrepreneurial activity in the Arctic zone of the Russian Federation (Federal Law 2020, N-193-FZ). The Federal Law defines the legal status of economic entities of the North as future AZRF residents, mechanisms for regulating AZRF residents' activities, conditions for signing an investment agreement, amendments, and termination. The term "resident" in this context refers to the company or individual entrepreneur acting as an investor, hence, not to be confused with people who live in the Arctic. The state becomes a legal advocate for entrepreneurship in the Arctic, and the Far East Development Corporation is empowered to represent and defend residents' interests in court in disputes with government authorities (Slepcev, 2020). According to some Russian experts, the law largely duplicates the provisions of current federal legislation, which allows for the establishment of various legal regimes: Federal Law 'On Advanced Social and Economic Development

'Territories in the Russian Federation' and Federal Law 'On Special Economic Zones in the Russian Federation' (Koshkin, 2020).

The Russian Far East and Arctic Development Corporation (FEDC) is the management company of the Arctic Zone of the Russian Federation, the Free Port Vladivostok, and the advanced special economic zones in the Far Eastern and Arctic constituent entities of Russia. During a meeting with investors from AZRF the Prime Minister of the Russian Federation Mikhail Mishustin said:

The Arctic is now becoming a favourable region for investment. Today, the largest special free zone in the world has been created in our northern regions. It should become an attractive place for businesses from completely different industries and different scales, and attract, among other things - why not - foreign investors. It's definitely a very large number of industries that could be attractive, whether it's a fish processing plant, or a small hotel, or medical care companies. Everyone should get an equal opportunity here. Moreover, this is enshrined in a package of laws on state support for entrepreneurial activity in the Arctic (Government of Russian Federation, 2020).

The reference of the AZRF to the special economic zone concept is not a coincidence because incentivizing measures are targeted at economic development and support for entrepreneurs. Unlike the system of "northern" benefits (northern coefficients of wages depending on the severity of natural living conditions, allowances for the length of service in the regions of the Far North, additional vacation days, payment for the road to the place of vacation once every two years, and some others), benefits that are defined in the new Federal Law are not guaranteed by default (Zamyatina, 2021). Rather these benefits need to be actively sought after and require capital investments from the applicants, with a minimum of 1 million RUB (equivalent to EUR 17,800) of declared investments.

In sum, the benefits include income tax breaks (except for mining projects); compensation of insurance premiums in respect of new jobs (except for mining projects); severance tax benefits for projects in the field of mining and processing of solid minerals; benefits for land and property taxes; obtaining land plots without bidding; the possibility of creating a free customs zone on the site; protection from excessive unscheduled inspections by supervisory authorities; qualified defence in court in case of disputes with authorities; the possibility of obtaining concessional financing of investments from credit institutions; and targeted support and assistance in solving any problems from the federal ministry (Zamyatina, 2020).

Support measures can be classified into three categories (see Figure 6). These comprise a Programme of the resident of the AZRF, subsidies for infrastructure development and territory of advanced development "Capital of the Arctic".



**Figure 6.** Components of support measures available in AZRF in 2022.***Resident of the AZRF***

The programme resident of the AZRF was made possible as a result of Federal Law “On State Support of Business in the Russian Arctic Zone” (Federal Law 2020, N-193-FZ). The Federal Law defines a resident of the AZRF as “an individual entrepreneur or a legal entity that is a commercial organization, the state registration of which is carried out in the Arctic zone of the Russian Federation in accordance with the legislation of the Russian Federation (with the exception of state and municipal unitary enterprises), which have concluded an agreement on the implementation of investment activities in accordance with this Federal Law Arctic zone of the Russian Federation (hereinafter referred to as the investment activity agreement) and included in the register of residents of the Arctic zone of the Russian Federation” (clause 2 of article 2 Federal Law 2020, N-193-FZ). The focus of the programme is to assist business development in the AZRF by providing business support and taxpayer incentives. Beneficiaries of the programme are project developers in the Arctic Region of the Russian Federation who are planning to invest more than 1 million rubles in their ventures. The Russian Federation strictly regulates and simplifies the registration process for Arctic residents. The deadline for registration of residents from the date of submission application is 37 days. A resident of the Arctic zone is an individual entrepreneur or a commercial legal entity, registered on the territory of the Arctic zone.

State support for SMEs in the Arctic zone of the Russian Federation is necessary since it contributes to the creation of new jobs, reduces unemployment and develops a regional market for goods and services (Kirillova, 2021). Any interested person who fulfils the criteria from the Federal Law to become a resident and has prepared a set of documents, including the investment project’s business plan, can receive Arctic resident status. After business plan approval, the company management company Far East Development Corporation seals the contract.

The tax preferences are summarized in Table 1. They include tax benefits, subsidies and insurance premium rates.

**Table 1.** Types of taxes and benefits for residents of AZRF (Source: Russian Far East and Arctic Development Corporation).

<i>Type of tax/benefit</i>	<i>Description of privileges</i>
Income tax	0% for ten tax periods after the resident receives the first profits
Mineral extraction tax (MET) rate	<ol style="list-style-type: none"> <li>1) 0.5 of the current rate (for solid minerals; only for new deposits. The amount of the benefit may not exceed the amount of private investment in infrastructure, enrichment or processing)</li> <li>2) Zero MET rate on the production of combustible gas used exclusively for the production of liquefied natural gas and/or as a raw material for the production of goods that are petrochemical products produced at new production facilities put into operation after January 1, 2022</li> </ol>
VAT	Zero VAT rate for works (services) involving the carriage of goods outside the Russian Federation by sea transport, and the provision of icebreaker assistance services for sea vessels engaged in the carriage of goods outside the Russian Federation

Subsidy	75% of the amount of insurance premiums (for new jobs only; does not apply to projects in the field of mining)
Insurance premium rate	7.5% for big businesses residents in the AZRF 3.75% insurance premium rate applies for SMEs resident in the AZRF

Apart from tax breaks, the residents receive administrative benefits. Administrative preferences include the ability to apply the free customs zone (FCZ) procedure to built-up and equipped plots used by Arctic Zone residents, as well as the provision of state- or municipal-owned land plots to Arctic Zone residents without a bidding process, the possibility of conducting inspections concerning Arctic Zone residents only with the approval of the Ministry for Development of the Russian Far East and the Arctic, and the simultaneous conduct of environmental expert assessments and state expert assessments of design and estimate documentation in a shorter time frame. In court, residents' interests are protected (the Management Company has the right to defend and represent the interests of the AZRF residents who have applied to it in court). Special regulations for the operation of checkpoints on the Russian Federation's border in the Russian Arctic are applied.

Any investment project over 1 million rubles can become a resident of the Arctic zone and receive tax benefits. Arctic residents have lower tax rates than the rest of Russia and, in some cases, the Far East. In October 2021 the Cabinet of Ministers made it simpler for small businesses to obtain Arctic zone resident status. Previously, organizations seeking resident status were required to invest in the renovation or construction of the real estate. The Government of the Russian Federation approved a list of 58 types of activities for which companies can become residents of the Arctic zone without the requirement for construction or reconstruction of capital facilities. Among these activities are forestry, animal husbandry, furniture production, metal processing, clothing, publishing, paper and leather goods, the provision of educational services, waste collection and disposal, and healthcare. It is hoped that this order will become an incentive for the socio-economic development of the Russian Arctic (TASS, 2021).

### ***Subsidies for infrastructure development***

This element of support mechanism includes provision of government budgetary aid in the form of tax breaks and subsidies for capital investments made in infrastructure facilities. Beneficiaries are initiators of new investment projects in Russia's Arctic Zone, with investments totaling more than 300 million rubles. The project's goals should align with strategic planning documents that guide socioeconomic growth in the Russian Arctic. The project requires new or updated infrastructure and capital construction facilities. The anticipated state support should not exceed 20% of the project's private investments and the project shall create jobs.

### ***Capital of the AZRF***

This support measure applies to separate areas of the city Murmansk, Kola district and closed administrative-territorial entity Vidyaevo. Its first resident was NOVATEK-Murmansk, which had a project involving the construction of large offshore structures. A special legal regime in the "Capital of the Arctic" is extended to 38 types of economic activity. Port activities, construction,

and logistics continue to be the ASEZ's primary specializations. So far, eight residents of the "Capital of the Arctic" have been granted the status of resident.

### ***Sustainability in business support programmes in AZRF***

The Federal Law has Article 28 that mentions the standard of responsibility of residents of the Arctic zone in relations with the Indigenous peoples of the Russian Federation living and (or) carrying out traditional economic activities in the Arctic zone (hereinafter referred to as the responsibility standard). The responsibility standard, a list of principles recommended for use by Arctic residents when interacting with Indigenous peoples in their traditional residences and economic activities, was approved by the Order of the Ministry for the Development of the Russian Far East No. 181.

This Responsibility standard includes the following principles:

- promoting the sustainable development of Indigenous peoples, improving their quality of life and preserving their original habitat;
- participation of representatives of Indigenous peoples in decision-making on issues affecting the rights and interests of Indigenous peoples in the development of natural resources in places of traditional residence and traditional economic activity;
- cooperation in improving the socio-economic situation in the places of traditional residence and in the territories of traditional nature management of Indigenous peoples when a resident of the Arctic zone carries out his activities;
- openness of the activities of a resident of the Arctic zone for Indigenous peoples and their organizations, state authorities and local self-government in all environmental and socio-economic issues affecting the interests of Indigenous small peoples;
- minimizing the negative impact of the economic activities of a resident of the Arctic zone, taking into account the social, environmental, and natural vulnerability of Indigenous peoples and the Arctic zone of the Russian Federation as a whole;

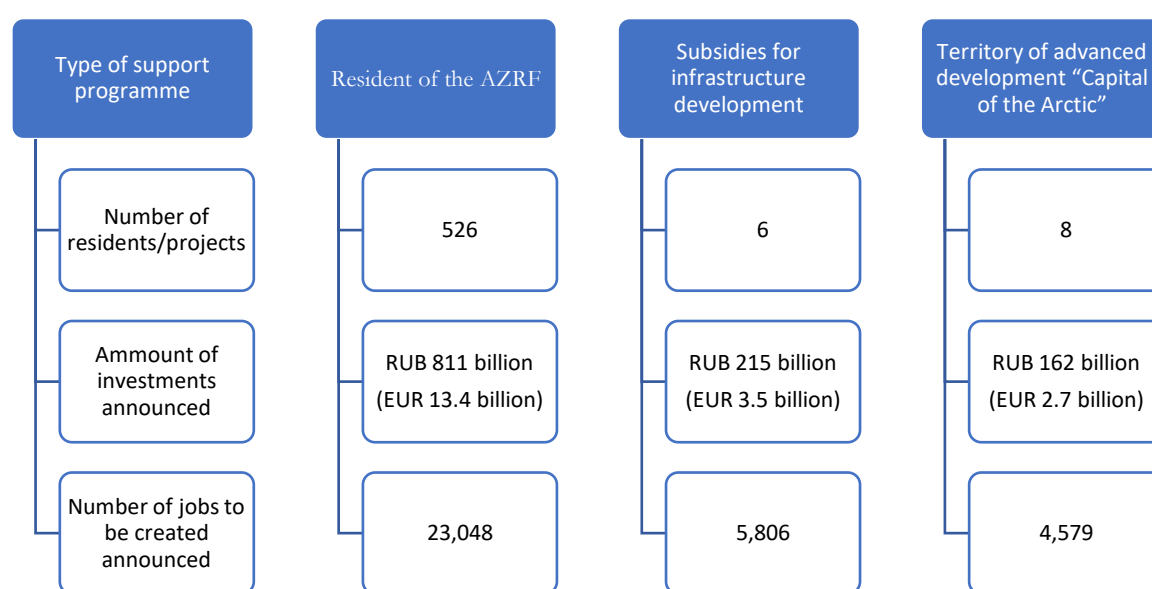
It should be noted that the responsibility standard is advisory. It includes a resident of the AZRF conducting an environmental impact assessment, taking into account the Arctic's vulnerability and Indigenous peoples' traditional use of natural resources; compensation for damage caused by the resident's economic and other activities that affect Indigenous peoples' habitat; etc. Another principle is the participation of Indigenous peoples in decision-making on issues affecting their rights and interest in natural resource development in traditional residences and economic activities. This principle requires preliminary coordination of the resident's project with Indigenous peoples and consultations before starting industrial development projects in places of traditional residence and economic activity.

## **Results and Discussion**

The historical analysis of constructing the AZRF concept in the Russian Federation demonstrates that the AZRF definition has been changing over the time with the addition of some territories whose Arctic status could be contested. The expansion of AZRF follows a managerial logic with a strong emphasis on providing support for socio-economic development of these territories.

According to the official state narrative, the Arctic Zone of the Russian Federation (AZRF) is the largest special economic zone in the world where investors enjoy special tax and administrative

regulation regimes. The measures to support entrepreneurial activities in the AZRF are comprehensive and, in many instances, correspond to practices adopted in SEZs worldwide. However, the focus of the support mechanism is on the business registered in the AZRF, not on the attraction of foreign investment per se like it has been the case in the developing countries adopting SEZ programmes. The support measures are driven by economic considerations so far resulting in EUR 13.4 billion of expected investments in Resident of the AZRF alone and their social impact is most visible in job creation. In fact, statistics from the Resident of AZRF website indicate that since 2020 till November 2022, there have been 23,048 new jobs announced to be created as part of the resident of AZRF programme, 5,806 jobs as part of subsidies for infrastructure development and 4,579 as part of the territory of advanced development “Capital of the Arctic” (see Figure 7). This adds up to a total of 33,433 new jobs announced and EUR 19.6 billion of investments announced.



**Figure 7.** Results of business support programmes in AZRF as of November 2022. (Source: Investarctic.com, compiled by the author).

The magnitude of economic and social impact in terms of announced job creation is big, at the same time, the Federal Law text itself and also the website for applying to become a resident do not have references to global sustainability frameworks like the UN SDGs.

### ***Sustainability concerns***

The responsibility standard as part of the Federal Law is of an advisory nature. It has been criticized because some of the provisions of the draft order that meet the interests of the Indigenous peoples of the North, were excluded when the document was adopted in its final form. The draft document included the principle of free, prior and informed consent (FPIC) of the Indigenous peoples of the North of the Russian Federation to make decisions affecting their rights and legitimate interests. Part 2.2 of the current standard includes instead the principle of participation representatives of Indigenous peoples in decision-making on issues affecting the rights and interests of Indigenous peoples regarding the development of natural resources in places of traditional residence and

traditional economic activity, such as the FPIC principle that has been replaced by the principle of participation (Ivanova & Litvinov, 2022). Moreover, the draft document was unique as it introduced signing an agreement on compliance with the standard between a company (resident) and the federal authority in the field of corporate social responsibility (CSR) and approved methods for monitoring compliance with it (Murashko, 2021). The final standard did not include these items either. Some researchers, however, note that the responsibility standard, although advisory, can have a positive impact on balancing business interests in developing Arctic natural resources and Indigenous peoples interested in preserving their original habitat and improving their quality of life (Samonchik, 2022).

Concerns have been raised in the sphere of land allocation to the residents of AZRF according to Federal Law. This concerns Article 15 “Features of the provision of land plots and real estate objects located on them”. A delegation of the management company’s administrative powers carries certain risks since the company is directly interested in expanding business activities in the Arctic zone, which may affect the objectivity of considering the region’s social and environmental characteristics when allocating land plots. Land plots are leased to residents on a preferential basis without bidding for the duration of the investment agreement unless the resident declares a shorter period (clause 39, clause 2, article 39.6). Decree of the Russian Federation dated February 1, 2021 No. 91 approved rules for the provision by the Arctic zone management company of state or municipal land plots (Samonchik, 2021).

The simplified procedure for providing land plots established by the Federal Law is not sufficiently justified. According to Samonchik (2021) the law pays little attention to the region’s vulnerable land. No criteria are established for refusing applicants to provide the requested land, which can harm the interests of Arctic Indigenous peoples (Samonchik, 2021). Concerns over land management and relations with the Indigenous peoples in the AZRF mirror challenges in the SEZs in India (Akon, 2018; Sundar 2011; Chaudhuri & Yabuuchi 2010). Lessons learnt from the development of SEZ elsewhere shall be taken into account for the future of AZRF business incentivizing programmes.

Federal Law does not include separate provisions on environmental responsibility. The capital construction projects that require environmental assessments are listed in the Federal Law of November 23, 1995, N 174-FZ “On Environmental Assessment” and the “Town Planning Code” of the Russian Federation. Article 16 of Federal Law states that capital construction projects that are not subject to “On Environmental Assessment” and the “Town Planning Code” of the Russian Federation and do not cause significant harm to the environment and its components, can be carried out from the date of submission of project documentation prepared for capital construction projects.

The universalization and unification of state support measures for conducting business in the harsh Arctic conditions and other Russian SEZs located in other regions of Russia do not take into account the particulars of conducting business in the Arctic (Koshkin, 2020). Various federal and regional legislative acts govern a variety of Arctic Indigenous peoples and land management issues. However, the nature of such regulation is neither consistent nor adequate. Although all territories of the Russian Arctic inhabited by Indigenous peoples are designated as specially protected natural areas, those territories continue to engage in commercial activities (Lipski & Storozhenko, 2019).

The state program of the Russian Federation “Socio-economic development of the Arctic zone of the Russian Federation” (State Program of March 30, 2021, № 484) prescribes indicators regarding the AZRF resident programme and by 2024 it is expected that there will be 320 residents. In November 2022, there were already 526 residents. Depending on their type of activity this will mean a higher impact on the environment. Evidence from China implementing SEZs calls for more considerate action in case of rapid expansion of economic activities (Zheng et al., 2016).

By analyzing the business support measures on the AZRF, it becomes evident that the economic pillar of sustainability prevails. The measures indeed provide residents with strong economic benefits and administrative support. At the same, less attention is paid to social and environmental responsibilities that come with the resident status. Several solutions are possible to raise sustainability on the agenda of support mechanisms. First, responsibility standards can become compulsory. Second, residents of AZRF could be required to provide reporting on their Environmental, Social and Governance (ESG) commitments. Depending on the size of the business requirements for ESG, reporting can be adjusted. The inclusion of the UN SDGs in the planning and execution of the projects and reporting on achieved indicators can be parts of individual projects. Reporting on the progress of the UN SDGs indicators on the municipal level of the AZRF can be potentially included in the Rosstat reporting.

## Conclusions

The article investigated how the AZRF developed into a Special Economic Zone concept with a certain set of economic benefits. In the analysis, I focused on incentivizing programmes for business development and support from the standpoint of sustainability. In doing so, I highlight how economic, social, and environmental concerns are integrated into these projects. In addition, I evaluate the degree to which international sustainability frameworks, such as the Sustainable Development Goals established by the United Nations, are included in these programmes.

The scope and scale of measures introduced in the AZRF are unprecedented. More time will be needed to see the efficiency and effectiveness of the programmes introduced. A managerial approach to the AZRF weighs on economic efficiency. For creating SEZ in the Russian Arctic all aspects of sustainability should be of equal significance. On the other hand, the social and environmental responsibilities that come along with resident status receive less attention. There are a few different approaches that might be taken to accomplish the goal of putting sustainability higher on the list of priorities for support mechanisms. These, for instance, may be raising the status of responsibility standard, requiring ESG commitments as part of granting the resident status and incorporating the UN SDGs principles in the support mechanisms. Lessons learned from SEZ programmes in developing countries can be used to develop more socially, environmentally and economically responsible business support mechanisms in the Arctic context.

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