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FOREIGN INVESTMENTS SAFETY ALERT

Overview of limitations of foreign investments and consequences for foreign companies in Russia

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Due to the significant changes of the investment climate in Russia, the Russian Government has introduced a number of extraordinary measures to prevent foreign investors and capital flight, some of them directly targeting multinationals operating in Russia.

On March 4, Russian First Deputy Prime Minister Andrey Belousov, responsible for foreign investment policy in the Government, outlined three options available to foreign investors:

1. Foreign companies should continue their business operations in Russia while securing supply of components and materials and fully complying with their obligations to employers.
2. Foreign companies should transfer ownership of their Russian assets to the management of their Russian partners and then, when the "political pressure" reduces, may look to return to the Russian market.
3. Should a company completely cease business in Russia, close its production facilities and lay off its employees, the Russian Government will consider such moves as equivalent to "premeditated bankruptcy". Such bankruptcy constitutes a criminal offense in accordance with the Russian Criminal Code and could be punished by fine or imprisonment up to 6 years.

Accumulated FDI in Russia constitutes almost 700 billion USD (the majority originating from European Union countries), and their future in Russia represents a significant issue both for the Russian and European economies.

As part of our ongoing efforts to protect and support multinational investments in Russia, Kesarev has prepared a brief guide on the measures introduced by the government of Russia that affect operations of international companies in the country.

Information will be updated in response to major developments throughout the crisis, with the most recent information highlighted.

This brief covers the following:

Assets Freeze

In late February - early March, the Central Bank of Russia banned Russian brokers from fulfilling orders from foreign residents to sell shares of Russian companies. Additionally, foreign individuals and legal entities are prohibited from accruing coupons and dividends of Russian issuers.

A number of restrictions have also been imposed by President Putin's decrees, in particular:

- A ban on the withdrawal of currency by residents of the Russian Federation in favour of non-residents under loan agreements.
- A ban on the export of cash from Russia in excess of the equivalent of $10,000.

These measures are directed not so much against foreign holders of Russian stocks and bonds, but rather to maintain the value of securities of Russian issuers at the time of greatest volatility and support of the ruble.

Over the week, the discussion about a possibility to freeze or even confiscate the Russian assets of companies from the US and EU jurisdictions erupted, with a number of opinions from more moderate to more radical stated by various stakeholders:

- On Sunday Feb. 27, former President of Russia and currently Deputy Head of the Security Council Dmitry Medvedev stated that Russian could confiscate and nationalize assets of companies from jurisdictions which imposed sanctions. Probably, Medvedev voiced the most radical scenario among a number of options being considered.
- On March 3, President Putin's press secretary Dmitry Peskov said that the Presidential administration is not considering the possibility of nationalizing assets of Western companies and individuals in response to sanctions against Russia.

A general framework of the Russian approach to foreign investors and their assets in Russia was stated on March 4 by First Deputy PM Andrey Belousov, who outlined three above-mentioned options. Currently, the most radical scenario of "nationalization" and "confiscation" seems to be removed from active discussion and punitive measures will only be considered to the companies which announced decisions to leave the Russian market.

Capital Flow Prevention

Measures to prevent capital control and ensure financial stability are among the top priorities for the Government and the Central Bank. The measures in this area are among the first ones being imposed over the crisis period.

On **February 28**, President Putin signed an executive order introducing several "response measures" – mainly several capital flow control policies to be enforced since March 1, which will negatively impact Russian investment climate, but may ensure mid-term financial stability, namely:

- Commitment for Russian resident companies to sell 80% of foreign exchange earnings credited from 1 January 2022.
    - The procedure for selling foreign currency will be established by the Central Bank.
- Prohibition for Russian residents to provide foreign loans in foreign currency and credit foreign currency to bank accounts outside of Russia.
- Prohibition of money transfers without opening an electronic payment account provided by foreign suppliers.

Similar measures were previously established by the directive of the Central Bank, however, from a legal point of view, the Presidential Order makes their implementation imperative.

The Central Bank issued clarifications on implementing that order, saying, among other things, that making foreign currency payments from residents to non-residents to pay for goods or services is not prohibited.

On **March 1**, President Putin signed an order on additional temporary measures to ensure financial stability of Russia. Key provisions:

- Starting from **March 2**, the following operations of residents with foreign entities linked to “unfriendly states” can be conducted only under a special procedure, i.e., upon a special authorisation: loans and credit operations in roubles, as well as operations with securities and immovable property.
- Starting from March 2, it is prohibited to export foreign currency cash and foreign currency instruments over 10000 USD.

Investment climate

Since February 24, a steady trend has formed for America, European and some Japanese companies to exit the Russian market and Russian assets. Number of segments are affected: oil and gas (ExxonMobil, Shell, etc.), automotive (BMW, Volkswagen, Honda, etc.), aviation (Boeing, Airbus, Embraer), technology (Intel, AMD, Dell, Apple, Nokia, TSMC, Siemens, etc.), consumer goods segment (Ikea, H&M, Mango, Nike) and many others. At the moment, it is difficult to estimate the size of the capital’s outflow, but it amounts to tens of billions of dollars.

At the same time, we note that on March 3, the South Korean Government announced that it would not stop deliveries of cars and electronics to Russia, since these goods are aimed at the mass segment.

The Coca Cola company, which has production facilities and a distribution network in Russia, as well as the Burger King fast food restaurant chain, have officially announced that they have no intention to leave Russia. The French company Total (which owns 19.4% of Novatek's shares) announced that it would not invest in new projects in Russia but does not have immediate plans to withdraw from existing ones.

Economic policy and crisis bailout measures

From late February, along with extraordinary measures in the financial sector, the Government started preparing a package of measures to react to the escalating economic crisis and the US / EU sanctions. Some of these measures represent an economic stimulus while others represent significant risk for foreign investors and represent Russia's reaction to Western sanctions.

On **March 4**, the Federation Council approved an extraordinary legislation to give new powers to the government and change some rules for businesses. Among other things, this includes (mostly for 2022):

The bill to "improve the mechanisms that ensure sustainable economic development in the face of sanctions pressure from foreign states" presumes the following:

- Most importantly, **the Government is authorized to set a list of products to which IP rights protection cannot be applied**. As it was said at the Federation Council meeting to approve the law, the Federation Council proposed the amendment to differentiate approaches to lifting the IP rights protection depending on the country of company's origin (*there is no final text published yet*).

Economy support measures

- A possibility of a moratorium on scheduled inspections of SMEs for 2022. Special conditions for conducting state control (oversight) may be introduced by the Government in 2022.
- The Government by a separate legal act may authorize carrying out activities without renewing a license/permit; obtaining licenses/permits and renewing them without obligatory conformity assessment procedures, without paying state fees, without paying for necessary public services; not undergoing conformity assessment procedures for perpetual licenses/permits.

Healthcare sector measures

- Medical organizations will be able to purchase more products they need according to a simplified procedure (medicines, consumables and medical products).
- Medicines and medical devices that do not have a Russian analogue can be purchased from a single supplier (if the only manufacturer is not from the country that imposed the sanctions).
- A special registration procedure is provided in case of medicines deficit due to economic restrictions imposed by other countries.
- The Government may also ban export of medical devices from Russia, prior imported from the countries that imposed economic restrictions.
- To stimulate medicines and medical devices production in Russia, the Government may approve special procedures for the pharmaceutical activity and production licensing.
- Special procedures may be introduced for conformity assessment with technical regulations.

The bill to amend the Tax Code empowers the Government with granting a deferral for the payment of taxes, social insurance fees, penalties, fines, interest in 2022.

The second and third packages with support measures, drafted by the government, may be considered in the parliament on March 10 and 11.

Tax Policy

On March 3, a draft law was submitted to the State Duma (parliament) that gives additional powers to the Government in terms of tax benefits for the whole of 2022:

- Possibility to suspend, cancel or postpone tax audits.
- Extension of deadlines for payment of taxes, fees and insurance premiums.
- Extension of deadlines for payment of advance payments for regional and local taxes.
- Extension of deadlines for reporting to the tax authorities.
- Etc.

Political Measures

On March 1, Prime Minister Mikhail Mishustin made a statement regarding the prospects for the presence of foreign investors in Russia. He confirmed that the Government "considers foreign businesses as potential partners" and is open to dialogue with constructive investors. "Those who will not curtail their projects will win" in Russia, Mishustin said. Thereby, the Government sends a message that keeping deeply rooted foreign companies in Russia is desirable, especially the companies in the consumer sector (to contain prices and prevent shortages).

Also, the remaining foreign companies will probably be able to rely on state support measures along with Russian businesses (including obtaining preferential loans). A relatively comfortable business can be guaranteed for companies operating in segments outside the focus of the import substitution policy. The main risk for such companies is the need to comply with the sanctions of national Governments against Russia. It should be noted that most of the decisions to withdraw from the Russian market and from Russian assets were not provoked by sanctions by the time and were made under external pressure and in view of the "toxicity" of the Russian market at the moment.

Another direction of counter-activity is limiting any opposition and spread of the information, alternative to the voiced by officials. On March 4, the Federation Council approved the law on criminal liability for calls for sanctions.

The law establishes responsibility for:

- "calls for the introduction of restrictive measures against the Russian Federation, citizens of the Russian Federation or Russian legal entities" (after bringing to administrative responsibility);
- "public actions aimed at discrediting the use of the Armed Forces of the Russian Federation in order to protect the interests of the Russian Federation and its citizens, to maintain international peace and security" (after bringing to administrative responsibility);
- "public dissemination of deliberately false information about the use of the Armed Forces of the Russian Federation".

The law does not provide for responsibility for complying with sanctions (which was one of the risks since the bill was submitted).

We also note that Roskomnadzor (tech regulator) started throttling Facebook and Twitter in Russia for "discrimination of the Russian media" and blocked multiple independent media.

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If you would like to schedule a discussion of this paper and learn more details about the above listed documents, please contact
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