RUSSIA: Screws tightening on foreign businesses

- The first instances of nationalization since the start of Russia's full-scale invasion of Ukraine are indicative of a further worsening business climate for foreign entities, many of which are continuing operations in Russia or are going through a lengthy and complicated exit process.

- As anticipated, foreign businesses are also facing greater pressure to help the Kremlin finance its wartime economy regardless of whether they stay or leave the Russian market.

- Meanwhile, the sanctions loop is tightening around third-country entities engaged with Russia.

On 11 May, the Finnish energy company Fortum reported a write-down of its Russian assets worth approximately EUR 1.7bn after Russian authorities had transferred the company's shares and management to the Federal Property Management Agency (Rosimushchestvo) in late April. The company's claims that the takeover of its assets was a 'crude violation of international law and of Fortum's rights as a foreign investor' were dismissed by Russian authorities, which stated that their actions were in accordance with domestic legislation and that Fortum was not entitled to any compensation.

Russian officials have been debating the introduction of external management in — or de facto nationalization of — entities belonging to 'unfriendly states' since the spring of 2022, but the corresponding bill was never adopted by parliament. Such debates were cut short by Vladimir Putin's 25 April decree No. 302 on the temporary management of immovable assets. The decree states that this is a retaliatory move against the seizure of Russia's assets by unfriendly states and international organizations. While temporary management can still be called off by the president, it is likely that these assets will be taken over by state-run energy companies. According to the Kremlin, the introduction of external management in other foreign-owned assets will be assessed on a case-by-case basis. The risk is considerable as multiple Western countries are exploring options for leveraging or transferring frozen Russian assets to the benefit of Ukraine.

Besides the threat of nationalization, the yawning budget deficit is forcing Russian authorities to look for new sources of revenue. After changing the calculation of taxes for domestic oil companies earlier in the year, the government is now debating the so-called windfall tax, which is expected to bring the budget around RUB 300bn (USD 3.9bn) according to finance minister Anton Siluanov. While details are still being developed, foreign companies are unlikely to be exempted from the tax. Apart from the financial hit, this would also mean a greater contribution to Russia's war effort.

In addition, the authorities have introduced a mandatory contribution fee for foreign companies selling their assets in Russia, which amounts to 5-10% of the transaction value. Since December, such contributions have reportedly added RUB 20bn (USD 259mn) to the budget. Also, the payment of such a fee might be subject to sanctions and require a special license, depending on the company's origin.

Even those companies that have already pulled out from Russia can be targeted. The Russian auto dealers' association is requesting RUB 8.5bn (USD 110mn) in compensation from Renault for losses linked to the company's exit last year. Unless an agreement is reached, the association intends to launch legal action in Russia, which might complicate the company's option of returning to the Russian market.

Finally, the risk of extra-territorial sanctions for companies engaged with Russia is also on the rise. The European Commission's 11th sanctions proposal focuses on preventing sanctions circumvention via third countries/parties. Recent studies indicate that significant volumes of sanctioned goods, including high-tech products, have been imported to Russia via China, Turkey, and countries in Central Asia and the Caucasus.

Client Portal >>

Andrius Tursa
Central & Eastern Europe Advisor
+370 6792 4910
andrius.tursa@teneo.com