

VOLUNTARY CONTRIBUTION TO THE FEDERAL BUDGET (EXIT TAX)

Changes to the procedure for obtaining approval for sale of international companies' Russian assets

5 May 2023

Summary

On 27 March 2023, the Ministry of Finance [published](#) an excerpt from Minutes No. 143/4 of a meeting of the Sub-commission of the Government Commission for Monitoring of Foreign Investment (hereinafter the Sub-commission) held on 2 March 2023. The Sub-commission adjusted the rules for calculating and paying the "exit tax" that entities from "unfriendly" states will have to pay to the Russian federal budget when selling their Russian assets.

Previously, as per the [Excerpt from the Minutes of a meeting of the Sub-commission No. 118/1 of 22 December 2022](#) (published on 30 December 2022), the Sub-commission defined the "exit tax" as an alternative to paying the purchase price in instalments. The current practice of gaining transaction approval evidences that the authorities are beginning to prioritize exit tax over installment plans.

The procedure for calculating the exit tax has also been altered. The Minutes specify that the amount to be paid depends on the discount applied to a given company's appraised value: with a 50-90% discount, the payment totals 10% of half of its appraised value (5% of the appraisal value); with a discount over 90%, the tax will be 10% of its full appraised value.

Generally, the Sub-commission's practices are shaped by a series of precedents (granted and denied approvals) for international companies selling their Russian assets. Tightening of regulatory terms demands that buyers and sellers' project teams pour in additional efforts with a GR component.

Below, we consider in detail the contents and consequences of the changes to the Sub-commission's practices.

Why have the rules for calculating and paying the exit tax changed?

The change in the rules for calculating and paying the exit tax may stem from a complex of factors with different time horizons:

- *short-term*, "exit tax" may be now prioritized over an instalment plan because industry regulators (rapporteurs to the sub-Commission) have developed mechanisms for making targeted use of these payments (financing intra-agency projects and initiatives). These mechanisms prompt regulators, on



the one hand, to maximize the exit tax while, on the other hand, blocking transactions that entail an instalment plan instead of the “exit tax”.

- *medium-term*, the **mounting budgetary deficit** may have prompted the Ministry of Finance to modify the rules and prioritize exit tax¹:
 - currently, discussion is still ongoing on introducing a one-off payment to the federal budget (windfall tax) on big companies’ “super-profit” received in 2021–2022;
 - considered in this context, exit tax as a de facto mandatory requirement appears to be a symmetrical step of sorts in relation to international companies (though it does not cancel out paying the windfall tax).
- *long-term*, tougher terms for exiting the Russian market may also stem from **the authorities’ changing approach to foreign investment as such**:
 - while, in the first months of 2022, the government acted mostly to keep international business in Russia, the paradigm changed in the autumn of 2022;
 - the protracted sanctions war between Russia and the West has left many international companies no alternative but to leave Russia. Accordingly, the procedure for gaining approval for relevant transactions has been reconfigured to give top preferences to asset buyers (*lower costs, tougher requirements for appraisal reports in order to prevent overpricing*) and to the treasury (exit tax).

Changes to the procedure for calculating exit tax

The exit tax is calculated on the basis of the asset’s appraised value:

- with a discount of 50%–90%, the tax will be 5% of the appraisal value;
- with a discount of over 90%, the tax will be 10% of the appraisal value.

The new requirements largely affect how the seller and buyer set up the transaction terms as they now have to account for the following:

- the purchase price agreed by the seller and the buyer is irrelevant for calculating the exit tax. The only thing that matters is the assets’ appraisal value and the discount on it. So, the transaction parties are discouraged from overpricing.
- the exit tax has the greatest effect on transactions involving sale of assets for a symbolic price (1 RUB/USD/EUR), which is, as a rule, typical of MBOs with a buy-back option. Since the discount in such deals is a priori over 90%, the parties pay 10% of the asset’s appraised value;
- the Ministry of Finance still allows instalment plans as an alternative to exit tax, while individual sectoral regulators (including the Ministry of industry and Trade) essentially block submission to the Sub-

¹ At the end of the first quarter of 2023, the budget deficit was RUB 2.4 trillion (with a predicted yearly deficit of RUB 2.9 trillion).



commission of such proposed transactions that do not envisage an exit tax as the regulators are interested in receiving monies into their agencies' treasury accounts.

For the Ministry of Finance (the Sub-commission is chaired by Finance Minister Anton Siluanov), **the new rule helps solve the problem of overpricing of sold assets**. The parties could use overpricing to neutralize the 50% discount requirement.

The regulator believes that the system for appraising the assets of exiting companies could be seriously flawed so independent valuation companies could have "stretched" asset market values to figures that would satisfy both buyer and seller, thereby neutralizing the discount on the agreed purchase price.

In February 2023, the Ministry of Finance [published](#) a List of Valuers recommended for conducting appraisals. The list includes only 42 organizations (out of several thousand valuers in the Russian Federation) and the selection principle was not entirely clear. In particular, it did not feature several large valuers with experience of appraising assets sold by residents of "unfriendly states." On 24 April, the Ministry of Finance also published a [list of SROs recommended to provide expert opinion on appraisal reports](#).

The steps taken by the Ministry of Finance indirectly evidence the accumulated issues the Ministry has with appraisals of some large assets whose sale had to be approved by the Sub-commission.

Apparently, the new rules for paying the exit tax are, among other things, a way for the regulator to eliminate overpricing.

Who pays the exit tax?

Prior to 2023, the Sub-commission did not, as a rule, specify who was to pay the exit tax (the payer was listed as "transaction parties"). In 2023, however, the Sub-commission's minutes listing the exit tax payment terms generally charged the purchasing company resident in Russia with paying the tax.

At the same time, the tax traditionally may either reduce the buyer's actual purchase price (*the tax is paid "out of" the purchase price*) or may have no effect on it (*in this case, the buyer pays the seller the entire purchase price with a 50% discount and also pays the exit tax*). For the Ministry of Finance, the payment procedure (*paying "out of" the purchase price or without reducing it*) is to be agreed by the parties and to be taken into account in Sub-commission decisions.

These practices may have been adjusted because the US sanctions make it impossible for the seller (either a resident of a "unfriendly state" or a Russian entity controlled by such a resident) to pay the tax. The US Treasury Office of Foreign Assets Control monitors sanctions compliance, while the sanctions directly prohibit US residents from making payments in favour of and with participation by the Bank of Russia or the Ministry of Finance, and secondary sanctions risks might extend to all companies that make payments in dollars.

Exit tax is paid into the treasury account of the ministry that regulates the operations of the Russian asset being sold. Since the Federal Treasury is directly [subordinate](#) to the Ministry of Finance, while treasury accounts are opened with the Central Bank, payment of exit tax constitutes a violation of the US sanctions legislation.



This is confirmed in OFAC's special [commentary](#) on paying the exit tax, which comes down to the following:

- OFAC relies on Directive No. 4 (Russia-related Sovereign Transactions Directive) of executive order 14024, which directly prohibits US individuals and legal entities from participating in transactions involving either the Ministry of Finance or the Central Bank or the Russian National Wealth Fund;
- so, transfer of funds into treasury accounts opened with the Central Bank constitutes a violation of the current sanctions;
- a special license (General License 13D) allows US individuals and legal entities (including subsidiaries in Russia) to pay taxes as part of Russia's regular financial system. Even so, this license applies solely to "regular transactions" critical for current operations and not to asset sales.

Currently, OFAC does not distinguish between exit tax paid by buyer or seller and considers both to be cases requiring a special license.

To whom the tax is paid?

As already shown, exit tax is paid into the treasury account of the regulator in charge of the appropriate area (the Ministry of Industry and Trade, Ministry for Economic Development, Ministry of Construction, Ministry of Agriculture, Ministry for Digital Development, etc.).

Several initiatives were proposed in early April for spending exit tax funds:

- on 8 April, President Putin [instructed](#) the government to ensure that funds obtained from payments made into the treasury pursuant to transactions submitted to the Sub-commission by the Ministry for Economic Development are allocated to the tourism sector (this initiative is likely to have been proposed by the Ministry for Economic Development, which regulates the tourism sector). By 1 July, the government should determine the amount of and procedure for redistributing exit tax funds;
- back then, in early April, Deputy Prime Minister and Minister of Industry and Trade Denis Manturov proposed using the exit tax to finance regional Industry Development Funds, industrial R&D and reverse engineering.

Other sectoral regulators may be expected to roll out such initiatives and programs in the near future, too.

Such initiatives are important for determining the key regulators' stance on payment of the exit tax:

- while there will technically be an alternative (to pay exit tax or make payments on an instalment plan), **preferences will be a priori given to payments to the treasury;**
- receiving these funds into ministry treasury accounts allows for funding of each ministry's programs and initiatives to be increased;
- so, **regulators are additionally incentivized to impose exit tax as a condition for approving the given transactions;**



What is the procedure and deadline for paying exit tax?

Since the exit tax is not technically a tax, the procedure and deadline for paying it are to be determined through negotiations with key stakeholders and efforts of GR teams.

The Sub-commission's practices demonstrate varying approaches to the procedure and deadlines for paying the exit tax, including the options of paying the exit tax in instalments over 1–2 years, paying the exit tax after the transaction has been closed, etc.

Structuring exit tax payments in the interests of the transaction parties requires appropriate arguments to be presented to government stakeholders.

Key takeaways

Institutionalizing exit tax on sale of Russian assets by residents of “unfriendly” states may have the following consequences:

- **higher costs for the asset seller and/or buyer.** The relative cost is particularly high for MBO transactions. The previous terms for paying exit tax are essentially retained only when there is a 50% discount on the appraised value;
- **various options for paying exit tax** remain with respect to the procedure and deadline for making payments, which requires the parties to present before government stakeholders’ arguments in support of the parties’ stances;
- **OFAC’s indeterminate stance** and possible changes in the exit tax payment procedure require the regulations in these areas to be constantly monitored.

Changes in the dynamics of granting approvals for sales of international companies’ assets may be result from a significant range of factors. We predict further changes in these practices and in the legal regulations in this area in general.

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If you would like to schedule a discussion of this paper and learn more detail about the documents listed above, please contact
Yury Panasik, Partner, y.panasik@kesarev.com



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