

Russian counter-sanctions: Temporary procedure for repaying debt to foreign creditors

On March 5, 2022, Russia's Edict No. 95 On Temporary Procedures for Discharging Obligations to Certain Foreign Creditors (**Edict 95**) entered into immediate effect. Russian authorities have thus temporarily changed how Russian debtors may discharge their obligations to creditors.

The changes come in the wake of recently introduced restrictions on capital transfers and other transactions involving non-residents from "unfriendly states". The new requirements temporarily introduce ruble payments for residents' financial obligations instead of the original debt currency. No end date was set for the new payment procedure.

1 Which obligations must be repaid according to the new rules?

Edict 95 establishes a special procedure for Russian residents to discharge their payment obligations to creditors under loans and financial instruments (**financial obligations**). These include obligations under credit facilities, loans, securities and derivatives.¹ The regulatory scope of Edict 95 does not cover payments on non-financial obligations (e.g., for goods and services).

Edict 95 states that the following categories of debtors (**Russian debtors**) should repay their debts to creditors under this new procedure:

- (a) The Russian Federation, its constituent entities and municipalities; and
- (b) Other Russian Federation residents² (including natural persons and legal entities).

Financial obligations also include Russian debtors' obligations related to non-residents' issuance of securities (notes, depositary receipts).

This new applies to financial obligations, which exceed *RUB 10 million* per month or the equivalent in foreign currency.³

The wording of Edict 95 is quite general. We believe therefore that it may cover both foreign-currency and ruble financial obligations. This logic is also implied by the **Central Bank of the Russian Federation (CBR)** guidance of March 6, 2022. The regulator has stated that the special temporary debt service procedure of Edict 95 applies to Russian debtors' financial obligations not only to foreign creditors but also to Russian creditors. It remains an open question whether Edict 95 will be applied in practice to payments to development finance institutions and other supranational organizations.

¹ See section 3.3 of this alert for the effect of Edict 95 on derivatives.

² Similarly to Russian Government Resolution No. 295 of 6 March 2022, we believe the term "resident" is used here with the meaning given in Russian currency

legislation (Federal Law No. 173-FZ On Currency Control and Currency Regulation of 10 December 2003).

³ At the CBR exchange rate on the first day of the month.

2 Creditors from unfriendly states

The new procedure applies to the discharging of financial obligations to:

- (a) Foreign creditors from unfriendly states, including:
 - (i) Persons associated with states which have imposed sanctions or other measures against Russia and its residents, including if those persons hold citizenship, are registered or have their primary place of business in and/or primarily generate profit in those states; and
 - (ii) Persons controlled by them (other than Russian residents); and
- (b) Other foreign creditors that are not from unfriendly states and not controlled by Russian residents (**other foreign creditors**).

On March 5, 2022 Russia's government approved a list of unfriendly states.⁴ The list includes Australia, Albania, Andorra, the United Kingdom (including Jersey, Anguilla, the British Virgin Islands and Gibraltar), the European Union member states, Iceland, Canada, Lichtenstein, Micronesia, Monaco, New Zealand, Norway, the Republic of Korea, San Marino, North Macedonia, Singapore, the United States, Taiwan (China), Ukraine, Montenegro, Switzerland and Japan.

As stated above, Edict 95 does not apply to non-resident creditors whose ultimate beneficiaries are Russian residents (even if they are controlled through foreign legal entities), provided information about control has been properly disclosed to Russian tax authorities. There is a similar exception for the requirements of RF President Edict No. 81 [On Additional Temporary Economic Measures to Ensure Financial Stability in the Russian Federation dated March 1, 2022](#) (alert of March 3, 2022).

3 Discharging financial obligations

3.1 Repaying debt to creditors from unfriendly states

Russian debtors will be able to make payments on financial obligations with creditors from unfriendly states only in rubles through special limited-use type "S" accounts opened (including by the debtor itself) in the relevant creditor's name.

3.2 Repaying debt to other foreign creditors and Russian residents

Financial obligations to other foreign creditors and Russian residents will be considered discharged by the Russian debtor if the creditors receive payments for those obligations in rubles in the ruble equivalent at the CBR exchange rate at the time of payment. Moreover, with special approval from the CBR or the Ministry of Finance (depending on the debtor's category) Russian debtors will be able to discharge foreign-currency denominated financial obligations in the currency of the debt as well.

Russian debtors will also be able to discharge financial obligations to other foreign creditors and Russian residents *without* using type "S" accounts. This will allow creditors who receive funds on their settlement accounts to use the funds without the limitations that apply to type "S" accounts (see section 4 below).

3.3 Special considerations for discharging financial obligations under financial instruments

Edict 95 (subject to the CBR guidance) sets forth the following special considerations for discharging securities financial obligations:

- (a) Obligations to Russian residents and other foreign creditors, whose securities are registered with Russian custodians, are considered discharged by transferring funds in rubles in the ruble equivalent at the CBR exchange rate as of the payment date (these payments are made *without* transferring the funds to type "S" accounts);

⁴ Russian Government Order No. 430-r of 5 March 2022.

- (b) Obligations to creditors from unfriendly states and foreign nominee holders are considered discharged by transferring funds in rubles in the ruble equivalent at the CBR exchange rate as of the payment date (these payments are made through type "S" accounts); and
- (c) Russian residents discharge obligations involving the issuance of notes and depositary receipts as set forth in Edict 95.

Edict 95 does not contain separate rules for discharging financial obligations under derivatives. This has caused the professional community to question whether Edict 95 applies to payment obligations in derivatives.

At the same time, since Edict 95 as it is currently worded applies to "financial instruments" generally (without express exceptions), it seems likely that the temporary procedure also applies to financial obligations in derivatives.

Accordingly, in the absence of separate rules, we believe the general rules described herein should apply to the discharge of financial obligations under derivatives.

3.4 Repayment in the currency of the debt

Approval for a Russian debtor to discharge its financial obligations in foreign currency without following this new procedure under Edict 95 may be granted only by:

- (a) The CBR, if the debtor is a regulated credit institution or non-credit financial institution; and
- (b) The Ministry of Finance of the Russian Federation by agreement with the CBR for all other Russian debtors.

The RF President has authorized these bodies to determine a different procedure for discharging financial obligations. The CBR is also authorized to give official guidance on how to apply Edict 95, and that guidance is binding throughout Russia.

4 Type "S" accounts

As stated above, so-called type "S" accounts are used for payments under financial obligations with creditors from unfriendly states. We note that such accounts were already used in Russia to control capital transfers decades ago (before currency control laws were relaxed). The regulator has revised them in light of recent events.

A Russian debtor may submit:

- (a) To a credit institution; or
- (b) To the central depository (the National Settlement Depository non-bank financial institution), if a debt for securities (including notes) is being repaid,

an application to open a type "S" account intended for payments on financial obligations in the name of a creditor from an unfriendly state (or other foreign nominee holder). And, from a practical standpoint, as foreign justice systems have a number of restrictions on interacting with some Russian credit institutions, the debtor and the creditor must agree on which credit institution will be used to open the type "S" account.

Under Edict 95, all security accounts opened for a non-resident or foreign nominee holder prior to March 5, 2022 are also type "S" accounts.

When funds are received on type "S" accounts the creditors from unfriendly states may submit a request to use the funds to the credit institution where the account is held.

Critically, the regime for using type "S" accounts is set forth in the [CBR Board of Directors Decision On Establishing the Type "S" Account Regime for Discharge by a Resident to a Non-Resident of the Obligations Set Forth in Edict 95 of 8 March 2022](#).

A foreign creditor will be able to make only a limited number of transactions on such accounts.

For example, only the following funds may be credited to a type "S" bank account:

- (a) From Russian Debtors to discharge financial obligations;
- (b) From other type "S" accounts; and
- (c) Funds debited from the account in error.

Funds may be debited from such a special account only:

- (a) To pay taxes, duties, fees and other mandatory payments in Russia;
- (b) To purchase federal loan bonds from Russia's Finance Ministry;⁵
- (c) For transfers to non-residents' ruble settlement accounts or for other transactions *if provided by a special approval*;
- (d) To pay account maintenance fees;
- (e) For transfers to a resident when paying a penalty;
- (f) For transfers to other type "S" accounts; and
- (g) To debit funds credited in error.

So, it is evident that a creditor from an unfriendly state *will be limited in how it can use funds received to discharge financial obligations in rubles instead of the currency of the debt*. Funds are thus effectively locked in Russia. The foreign creditor may export them to its settlement bank account only with special approval.

5 Non-circumvention rules

Edict 95 also includes non-circumvention rules. It stipulates that Russian debtors follow the new procedure when discharging financial obligations *assigned* by an initial creditor from an unfriendly state to a new Russian resident creditor or other foreign creditor after March 1, 2022. This essentially means that a type "S"

account must be used to discharge debts to new creditor as if the debtor were repaying the debt to the initial creditor from an unfriendly state.

Neither Edict 95 nor any other Russian law provisions specifically regulate the consequences of failing to comply with the new requirements for discharging financial obligations. However, we believe Russian debtors will simply be unable to pay financial obligations as they did before, because clearing banks will strictly comply with the Edict 95 requirements.

It is also likely that Russian debtors will face administrative liability for currency law violation if payments made without following the new procedure for discharging financial obligations are declared illegal currency transactions. This would involve a fine of 75-100% of the amount of the currency transaction. The question remains open of whether Edict 95 will be deemed an act of currency legislation establishing requirements for making currency transactions (hence triggering such a fine).

⁵ In many cases there are already restrictions on Creditors from a number of Unfriendly States purchasing such bonds under the sanctions on them. Therefore, this

exception clearly would not work for a number of foreign creditors.

Contacts



Tim Stubbs
Partner, Head of Banking & Finance
practice

T: +7 495 644 05 00
E: timothy.stubbs@dentons.com



Filipp Petyukov
Counsel

T: +7 495 644 05 00
E: filipp.petyukov@dentons.com



Konstantin Nazarov
Counsel

T: +7 495 644 05 00
E: konstantin.nazarov@dentons.com