

# Implementing the new Russian Currency Control Law

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Ever since 1992, when the first Russian Currency Control Law was introduced, currency regulation has been a powerful legal instrument in the hands of the country's Central Bank. The Law has allowed the Central Bank to control foreign currency inflow and outflow, national currency exchange rates, as well as to build up its own currency reserves.

Summer 2004 has become a time of major overhaul for the Russian currency control system, with a new Currency Control Law (the Law) coming into effect on June 18, 2004 and most of the numerous regulations of the Central Bank supporting the preceding system subsequently repealed or replaced.

It is generally viewed that the changes have been introduced in response to market demand for the currency control system to become less restrictive and more transparent and flexible, particularly as the final effects of the 1998 Government default and subsequent financial crisis are gradually washed away. Having met the requirements of transparency and flexibility, the new Law has also introduced certain new mechanisms of currency control that appear to be capable, if applied in full, of producing an even more restrictive system of currency regulation than the one that existed until June 18, 2004.

This article is intended to address the most important aspects of the Russian currency control system as the same applies to certain financial transactions performed by non-residents. For the purposes of this article little or no reference is made to the system's requirements with respect to residents' transactions.

## SCOPE OF CONTROL

As was previously the case, the Russian currency control remains targeted at any transactions (referred to as "currency transactions") that would result in:

- residents acquiring foreign currency or title to and interest in "non-domestic" securities (i.e. any securities that are either (i) denominated in a currency other than Russian roubles, or (ii) have not been issued and registered in Russia, or (iii) convey to their holders a right to receive any currency other than Russian roubles);
- non-residents acquiring Russian roubles or title to and interest in "domestic" securities (i.e. any securities that are either (i)

denominated in Russian roubles, or (ii) have been properly issued and registered in Russia, or (iii) convey to their holders a right to receive Russian roubles), particularly, government debt securities; or

- use of Russian roubles, foreign currency, domestic or non-domestic securities as means of settlements between residents and non-residents (and vice versa).

One of the significant positive developments introduced by the new Law is withdrawal of restrictions on conversion by non-residents of roubles into foreign currency for the purpose of subsequent repatriation.

## METHODS OF CONTROL

The new Law has abolished the previous system of individual permits and authorisations. Moreover, the Law expressly forbade currency regulation authorities – of which only the Government and the Central Bank are vested with appropriate power – to impose any additional restrictions not directly provided for by the Law.

Instead, a new requirement of funds depositing ("reservation") was introduced. This is supported by a renewed requirement for certain currency transactions (of both residents and non-residents) to be performed through Special Accounts (Special Rouble Accounts for non-residents and Special Foreign Currency Accounts for residents).

Specific categories of currency transactions with respect to which either or both of the requirements – use of special accounts and/or funds reservation – may be applied, are exclusively regulated by the Law. However, the Russian Government and Central Bank (as the only currency regulation authorities) are vested with power to decide whether such requirements shall be actually imposed or withdrawn with respect to certain categories of currency transactions recognised by the Law as being potentially subject to such requirements.

## SPECIAL ACCOUNTS

Non-residents' currency transactions to be performed solely through their Special Rouble Accounts (Type C, Type A, Type O, Type B1 or Type B2, as appropriate) include the following categories:

- purchase from residents and sale to residents of government debt securities;

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- purchase from residents and sale to residents of domestic securities (including shares, bonds, promissory notes and bills of exchange, etc.);
  - receipt from residents and disbursement to residents of rouble loans; and
  - collection of consideration paid by residents in roubles for domestic securities issued by such non-residents, at the time of placement.

In addition, the Central Bank may demand that Special Rouble Accounts shall also be used for the purposes of:

- sale and purchase of domestic securities between non-residents;
- sale and purchase by non-residents of foreign currency (except where such foreign currency is sold to or is purchased from a Russian bank);
- purchase from residents and sale to residents of non-domestic securities;
- performance by non-residents of obligations under non-domestic securities; and
- performance by residents of obligations under domestic securities.

Moreover, the recording of title to domestic shares, bonds and government debt securities belonging to non-residents shall be performed at special sub-accounts of their respective depository accounts.

Use of Special Rouble Accounts (or special sub-accounts of depository accounts) does not by itself impose any restrictions on currency transactions performed by non-residents; by default, funds are freely transferable to and from such special accounts or are convertible into foreign currency.

However, in almost all cases where use of special accounts is or may be required (with a few exceptions as discussed below) the Russian Central Bank is allowed to demand that funds reservation shall be made in connection with currency transactions performed through such special accounts.

### **FUNDS RESERVATION**

According to the new Law, funds reservation by non-residents may be imposed by the Central Bank with respect to such categories of currency transactions as are determined by the Law, in particular:

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- crediting of rouble amounts, domestic or non-domestic securities to a non-resident's special account;
- withdrawal of rouble amounts, domestic or non-domestic securities from a non-resident's special account;
- dealing in non-domestic securities;
- acquisition by non-residents of domestic securities;
- granting to residents of rouble loans; and
- sale by non-residents of foreign currency or foreign currency denominated cheques (except for sale to a Russian bank).

The only currency transactions that may potentially be required to be performed through non-residents' Special Rouble Accounts, but are still exempt from potential funds reservation requirement, are (i) sale and purchase of domestic securities between non-residents; and (ii) exchange of roubles into foreign currency.

Generally, funds reservation may be required in an amount of up to 20% of a specific currency transaction value, for a period of up to one calendar year. However, 100% of a transaction value reservation for a period of up to 60 calendar days may be imposed with respect to withdrawal of roubles, domestic or non-domestic securities from a non-resident's special account.

Moreover, dealing in non-domestic securities may be subject to either up to 100% reservation for a period of up to 60 days or up to 20% reservation for a period of up to one year, at the Central Bank discretion.

As a general rule, funds shall be deposited prior to a relevant currency transaction, whereupon such transaction may be proceeded with. However, dealing in non-domestic securities and withdrawal of rouble amounts, domestic or non-domestic securities from a non-resident's special account may only be performed after the relevant reservation period (if applied) shall expire.

As of June 30, 2004, funds reservation requirements are applied with respect to:

- crediting of rouble amounts from a non-resident's normal bank account to Type B2 Special Accounts (used to provide rouble loans to residents, or to purchase from or sell to residents of certain domestic securities) and to Type O Special Accounts (used to purchase from or sell to residents domestic corporate bonds) – 3% of value for 365 days;

- crediting of rouble amounts from a non-resident's normal bank account to Type C Special Accounts (used to deal in government debt securities) – 20% of value for 265 days; and
- withdrawal of rouble amounts from Type B1 Special Account (used to collect rouble loans extended by residents, etc.) to a non-resident's normal bank account – 50% of value for 15 days.

It should however be noted that the Law sets January 1, 2007, as deadline beyond which the funds reservation requirement shall not survive.

## CONCLUSIONS

With the new Law and supporting legislation being in effect for a just short amount of time, the new currency control system operation practice is yet to develop. Nevertheless, certain preliminary conclusions may still be drawn.

Undisputably, the new system features certain positive developments that are evidenced, *inter alia*, by:

- the replacement of the underlying restrictive concept of currency control (i.e. "forbidden unless specifically permitted") by the opposite one (i.e. "permitted unless specifically restricted");
- the curtailing of the Central Bank power to qualify certain currency transactions as being subject to or exempted from restrictions;
- the abolishment of obscure and, largely, ineffective system of case-by-case control of currency transactions through the system of individual permits and authorisations issued by the Central Bank; and
- the intended withdrawal of funds reservation requirements with effect from January 1, 2007.

At the same time, the new system provides the Russian Central Bank with a set of flexible tools that appear to allow it to tune the currency control system to essentially any degree of freedom. To what extent those tools will be used remains to be seen.

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