

NEW RUSSIAN LEGISLATION ON FINANCIAL COLLATERAL: IMPACT ON NETTING AND INITIAL MARGIN

*On 9 June 2021 the State Duma (lower chamber of the Russian Parliament) has adopted legislation improving the financial collateral regime ("**Amendments**"). The Amendments are currently pending ratification by the Federation Council (upper chamber of the Parliament) and signing into the law by the President, but these steps are expected to occur in the next few days. Below we summarize the key provisions of the Amendments.*

RECOGNITION OF REGULATORY INITIAL MARGIN IN INSOLVENCY

Historically, there has been a degree of uncertainty as to how Russian courts would treat security interest collateral in insolvency of a Russian collateral provider, and, in particular, whether they would treat such collateral as an equivalent of a pledge and the collateral taker as a secured creditor ranking ahead of other creditors. However, even if the foreign law governed security interest collateral were recognized as an equivalent of a pledge, this would entail a number of significant limitations. In particular, (a) the collateral would need to be enforced by the insolvency administrator and would be subject to any stays/moratoria in connection with insolvency; (b) the collateral taker would be entitled to receive only 70% of the collateral value, whereas 30% would need to be returned to the insolvency estate; and (c) where a collateral provider is a Russian bank with retail banking license, all the secured creditors would rank behind the retail depositors. All of the above made the security interest collateral not effective in insolvency of a Russian collateral provider, and given that, for example, from September 2021 the Article 31 EMIR requirements for taking initial margin will extend also to trading with Russian banks, it could adversely affect the ability of foreign counterparties subject to EMIR requirements to trade with Russian banks.

To address these concerns, the Amendments expressly give recognition to security interest collateral in insolvency of a Russian collateral provider, provided that the following eligibility requirements are cumulatively met:

- posting such security interest collateral is mandatory under the laws of Russia or under the laws of foreign eligible jurisdictions (the list of such jurisdictions is to be approved by the Central Bank of Russia ("**CBR**"));
- collateral is provided by creating security interest in a bank account, cash, securities or other assets that may be eligible under the regulations of the CBR; and

- security interest collateral is held with a third party that meets the eligibility requirements to be established by the CBR.

Therefore, the Amendments give express recognition and protection to regulatory initial margin, and this recognition and protection will become effective once the CBR issues secondary regulations referred to above, which would set out eligible jurisdictions and requirements to third parties holding security interest collateral ("**Eligible Security Interest**").

ENFORCEMENT OF ELIGIBLE SECURITY INTEREST

The Amendments state that Eligible Security Interest may be enforced by the collateral taker to discharge any liability of the collateral provider for the payment of the early termination amount within 15 business days after the early termination amount has been determined. Any collateral that has not been enforced within 15 business days will need to be transferred into the insolvency estate. The enforcement shall be made in accordance with the terms of the documentation governing the provision of that collateral, which shall, inter alia, determine the process of enforcement and valuation of collateral. However, if the early termination has been triggered by the introduction of moratorium on satisfaction of claims of creditors of a Russian bank, the Amendments state that the collateral taker shall be entitled to appropriate the collateral at the valuation as of the date immediately preceding the date of introduction of the moratorium.

AMENDMENTS TO THE ISDA MASTER AGREEMENT WITH RUSSIAN BANK

The Amendments expand the statutory list of grounds for automatic early termination of transactions under a master agreement with a Russian bank. Before the Amendments it was mandatory to provide for automatic early termination of transactions with Russian banks upon the revocation of a banking license. The Amendments provide that it is mandatory to expand this list by adding the introduction of moratorium on satisfaction of claims of creditors as an additional ground for automatic early termination of transactions that may be entered into under a master agreement with a Russian bank.

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