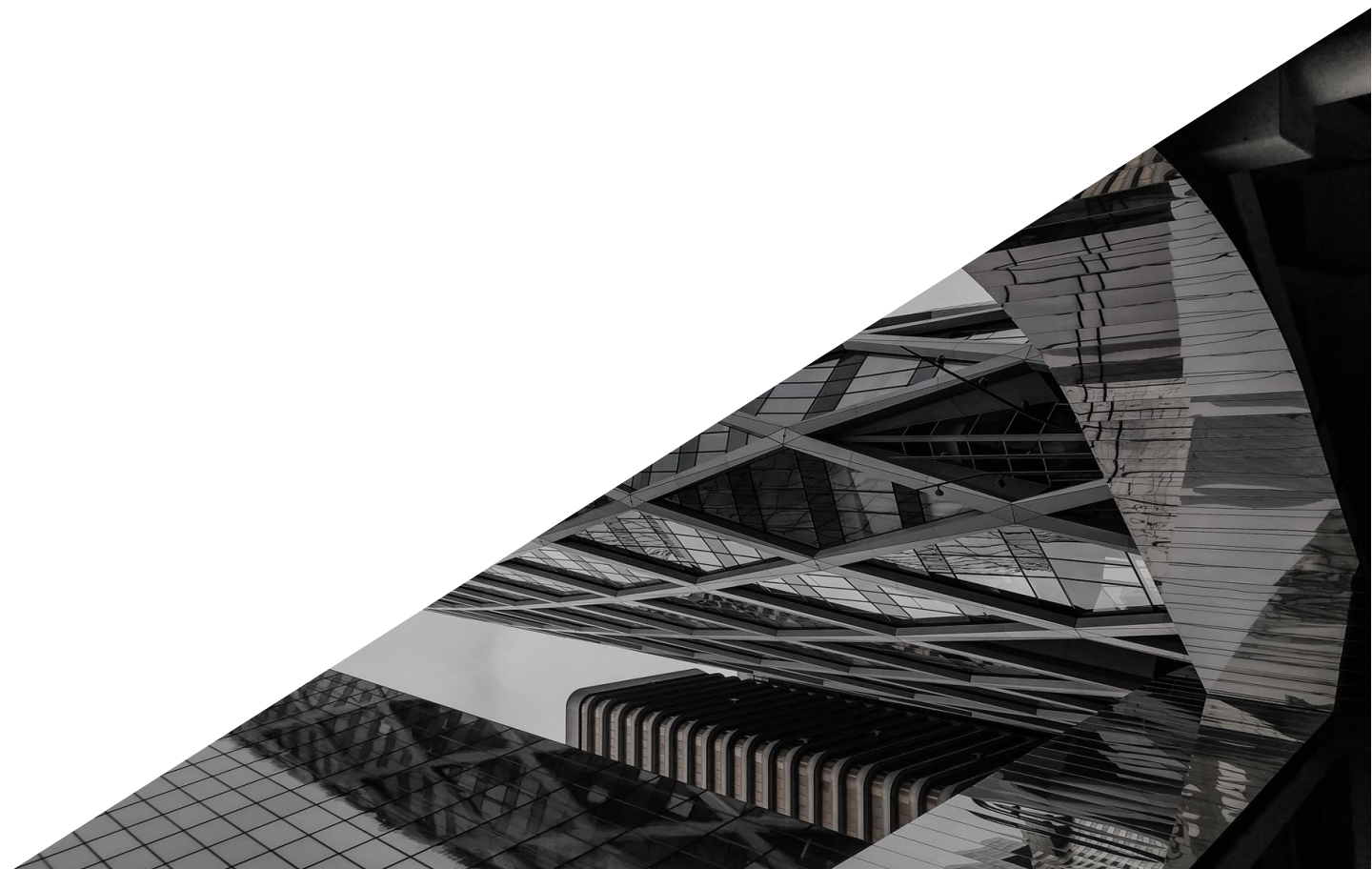


Triangle, But Not the Bermuda:

Blockchain, Digital Rouble and BRICS Bridge in Sanction Setting

Relevant as at 07.11.2024



On 31 October 2024, the Bank for International Settlements announced it was backing out of mBridge, a scheme for digital settlements using digital currencies of central banks. Led by Russia as the initiator, the BRICS states most interested in this new-generation project of settlement technologies are set to carry on by themselves.

VERBA LEGAL Partner Aleksandr Kuznetsov, Counsel Marat Samarskiy, Senior Lawyer Anna Sidorenko, and Lawyer Ivan Dubrovsky discuss whether the interested parties will be able to pursue the project, and what political and legal barriers they may face.



What Does Russian Business Get from New Settlement Scheme?

Caught in a spiral of countermeasures and sanctions since 2022, the Russian business, including the industries not directly affected by sanctions, has experienced difficulties with international settlements. As most traditional providers of this foreign economic activity segment have been reduced to a limited number of banks from EU, China, Uzbekistan, Turkey, and small Russian banks, the Russian Government now faces many macroeconomic challenges, of which the most critical is development of new settlement options.

The business and the government, which now has to ensure financial sovereignty, are unanimous as to the temporariness of agency solutions. The task is to be solved by full-scale implementation of the digital rouble project supported by the blockchain mechanism, enabling tomorrow's main settlement method, with the correspondent banks totally excluded from the international settlement chains.

Up to 2022, Russia was a leader of the global finance technologies, including implementation of SWIFT analogues (SPFS), introduction of the Fast Payment System functions, and alpha testing of different cross-border payment systems. The Soviet experience vividly demonstrates the role of COMECON and its International Bank for Economic Cooperation (IBEC) in terms of international settlement support (transferable rouble, settlement transactions and clearing in the planned and transition economy settings).

But will Russia and the interested Global South states be able to launch a new-generation settlement scheme?

About Clearing

International settlements between blocks of states count hundreds billion dollars, with the number of companies involved reaching dozens million. Such information volume needs to be carefully processed, administered and distributed. It may be done by a strong clearing centre, preferably with (1) excellent digital expertise and (2) international status.

Up to now, this role could have been played by the Bank for International Settlements (BIS) renowned for its almost 100-year history. Since 2019, BIS had taken part in the development of mBridge, a system for transfer and conversion of central banks' digital currencies, having brought it to the minimal viable product level due to the involvement and participation of Saudi Arabia, UAE, China, Thailand and Hong Kong represented by their national banks.

Nevertheless, by the end of October 2024, having assessed the potential sanction risks and the related real financial problems, the bank quit the project. It will probably also cease providing sites for creation of clearing centres.



In view of the above, such site might be operated by the New Development Bank (NDB) organised by BRICS member-states, or by IBEC which was engaged in this sphere at the time of COMECON.

As the new centre will inevitably work with a large number of involved sanctioned entities, such as Russia's Central Bank restricted for transactions, National Payment Card System MIR, and the country's largest banks, it will without any doubt be spotted by the sanction radar.

The status of an international organisation with its set of privileges and immunities will not help in avoiding the sanction consequences, as the International Investment Bank (1) existing since the COMECON times and (2) located in Hungary became subject to the US blocking sanctions (SDN status) in April 2023.

That said, the clearing centre should, as early as at the creation stage, take into account the risk of becoming sooner or later subject to sanction restrictions.



About Blockchain

Setting aside the sanction aspect of clearing, blockchain would be a real solution for overcoming the biggest hurdle to cross-border settlements, i.e. over-compliance by correspondent banks.

If successfully implemented, mBridge will be able to deploy exclusive interaction between the receiving country and the sending country, by-passing intermediaries with doubtful compliance obligations in the mutual settlement chain. Also on the table is the development of an independent BRICS Bridge system based on the mBridge technologies, intended to make settlements among BRICS member-states more effective.

In the framework of mBridge or BRICS Bridge, digital currencies of central banks, such as digital rouble or yuan, are to be converted within the system, with the banks interacting only with each other within a single country (receiver and sender).

Getting the scheme into shape will require considerable financial resources and political will. Whereas BIS could raise financing from many sources at once, development in the framework of IBEC or NDB may fail to attract comparable financial response.

Legal Regulation

From the legal regulation perspective, neither mBridge with its blockchain nor any potential infrastructure of similar systems, such as BRICS Bridge, is currently covered by the applicable law. Russia's legislators and regulators are yet to design the necessary architecture.

Even with the resources and political will available, the process may take at least a year.

However, the same things were said about crypto-currency mining, which had earlier been in the "grey" regulation zone but had come out on 1 November 2024.



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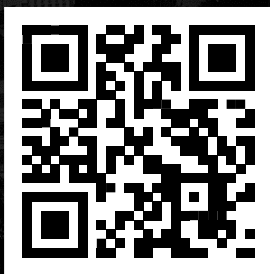
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