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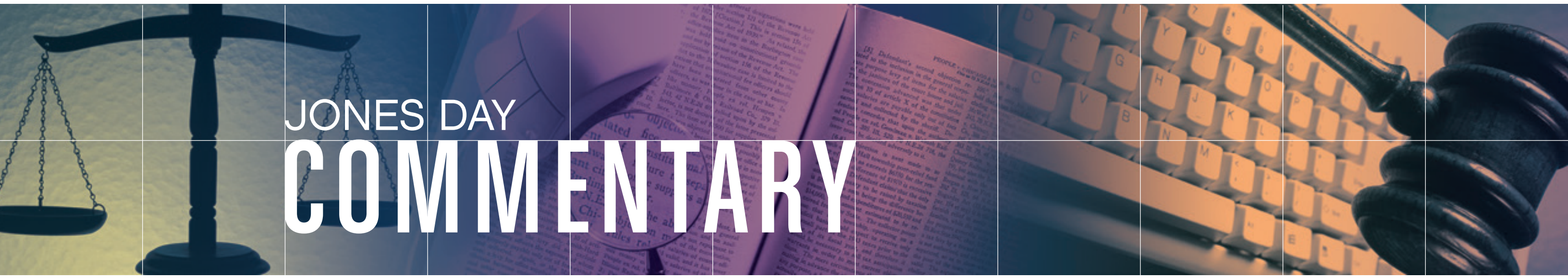

CYPRUS: A RUSSIAN DIMENSION TO THE EUROZONE CRISIS

With the end of summer, Europe's political leaders are intensifying their efforts to address the Eurozone's economic and monetary crisis. For a variety of reasons, including a favorable tax treaty with Russia, Cyprus has become the preferred jurisdiction for many Russian companies and financial institutions to establish holding company structures, joint venture vehicles, and offshore corporate entities. Given Russia's strong business connection to Cyprus, for many companies and financial institutions operating in Russia, the impact of the Eurozone crisis on Cyprus is of particular interest. This Mediterranean island nation joined the European Union in 2004 and adopted the euro as its official currency on January 1, 2008. As a result of the Eurozone financial crisis and inability to tap the international debt markets to finance its deficit, Cyprus has recently appealed to Russia for a €5 billion bailout, which only underscores the island's importance to the Russian economy.

While an assessment of the likelihood of and commercial risks arising from a possible Cyprus exit from the euro is outside the scope of this *Commentary*, Russian companies with Cypriot incorporated affiliates and transactions structured through Cypriot corporate entities should be taking practical steps now to understand and prepare for the risks from a possible escalation of the Eurozone crisis and a Cypriot euro exit, including the potential imposition of currency controls and the redenomination of currency from the euro ("Redenomination").

While the majority of questions and issues set out below may be equally applicable to most Eurozone jurisdictions, the Cypriot analysis needs to take into consideration that Cyprus only adopted the euro in 2008, has recent experience of working through redenomination issues, and until 2004 utilized exchange controls that had only limited effects on Cypriot entities held directly or indirectly by nonresidents.

CONTRACTUAL ISSUES

- Where and how are the payment obligations of the entity to be performed?
- What is the currency of contractual performance? Euros? Dollars? Other?
- If euros, how is the currency of the contract defined?
- What is the governing law of the contract, and which courts and arbitration tribunals have jurisdiction?
- What events of default are specified, and could they be modified by the principle of continuity of contracts, which would generally dictate that contractual provisions continue to be valid in spite of currency controls or a change in currency? What if such provisions are not included?
- Can material adverse change or other termination clauses be relied upon as a pretext for restructuring or as a basis to otherwise improve the contractual position of the parties to the transaction in the event of implementation of currency controls or Redenomination? Or, will these provisions be trumped by force majeure clauses that might excuse a failure to perform by an affected party?
- Is there a likelihood that under the governing law of a relevant contract, additional terms will be implied into it so as to facilitate the continuing efficacy of contractual obligations?

CORPORATE AND ENFORCEMENT ISSUES

- Would a Redenomination affect corporate capital structures?
- Could euro or foreign currency contractual rights and obligations be redenominated into a local currency?
- Could exchange controls be reimplemented, and what would their impact be?
- Could exchange controls or the Redenomination affect the enforcement of foreign proceedings in Cyprus?
- Will a foreign court give judgment in euro or other foreign currency in the event of Redenomination?

SOVEREIGN RISK AND *LEX MONETAE* ISSUES

- Is the sovereignty of a state over its own currency absolute? Can exchange controls be implemented?

PRACTICAL FUNDING, HEDGING, AND TREASURY ISSUES

- If exchange controls were to be implemented, what form are they likely to take?
- If exchange or currency control laws had to be reintroduced in Cyprus, would they:
  - affect payment obligations transiting through the local or offshore accounts of an entity incorporated in Cyprus?
  - affect U.S. dollar payment obligations?
- Will a Redenomination and currency or exchange controls have an impact on hedging contracts, margin arrangements, guarantee obligations, documentary credits, and custodian relationships?

OTHER RISKS

- Will the Eurozone crisis and any impact on contractual rights and obligations be used as a pretext for limiting exposure to Russia?

STEPS TO UNDERSTAND AND MITIGATE THE RISKS

- Have all contracts, assets, and liabilities that may be affected been identified?
- Can termination provisions, indemnities, or any other contractual provisions be relied upon to exit relationships or accelerate payments from counterparties who may become a concern?
- What opportunities can be identified to renegotiate contracts that may be affected?
- Does it make sense to consider contingency plans? If so, what are the legal, timing, and other practical considerations?

Jones Day has significant experience in dealing with all aspects of sovereign defaults, currency redenomination, and the imposition of exchange controls, as well as the consequences of these actions in a wide range of corporate and financing transactions. We have deep experience in cross-border structured transactions involving Cyprus and Russia. With regard to the Eurozone crisis and transactions involving Cyprus, we are advising our clients to prepare and are assisting them with:

- Analyzing their contractual relationships involving joint ventures or affiliated corporate entities organized in Cyprus and how they are documented to identify the exposures within them to payment obligations transiting through or to Cyprus or any other Eurozone member states.
- Considering how contracts would operate in the event of redenomination of payment obligations or the imposition of foreign exchange or other currency controls.
- Pursuing preemptive measures that might be taken now in order to limit the risk when it occurs—for example, amending contract terms to relocate the situs of the transaction, payment obligations, or payment currencies.
- Implementing a contingency plan to consider those relationships that may become contentious or end up in dispute in the event of a Cypriot sovereign default or Eurozone departure.

LAWYER CONTACTS

Jones Day's Moscow Office and the Firm's euro crisis team based in London and other European offices are available to assist clients to address these and other issues arising from the Eurozone crisis. For further information, please contact your principal Firm representative or one of the lawyers listed below. General email messages may be sent using our "Contact Us" form, which can be found at www.jonesday.com.

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