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Digital Financial Assets as a Tool for International Payments

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ABSTRACT

The relevance of the research topic is due to the need to develop alternative methods of international settlements for Russia in the context of increasing sanctions pressure. Over the past few years, countries have been actively implementing new tools that have emerged due to digitalization and have been called “digital financial assets”, the potential of which can be realized, including in the field of international settlements, ensuring a reduction in sanctions pressure on the Russian economy. **The purpose** of this article is to identify the possibilities of using digital financial assets as a tool for international settlements. **Methods.** The study was carried out using up-to-date data and sources, as well as an analysis of the principles, methodological approaches and practices of using digital financial assets in international settlements. **The scientific novelty** of the work is that it presents the mechanism of Russia's use of digital financial assets for international settlements and highlights its key risks. **The results of the study.** The article examines the essence of digital financial assets, reveals the features and mechanisms of their application in international settlements, presents the approaches of various countries to regulate them, and examines the possibilities and risks of their introduction in Russia. **Practical significance.** The results and conclusions of the article can be useful both for the scientific community and for participants in foreign economic activity and other organizations working with digital financial assets, as well as for the Bank of Russia.

Keywords: digital financial assets; international settlements; digitalization; blockchain; token; digital financial asset issuance operator

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INTRODUCTION

In the last decade, both in the world and in Russia, one of the most notable development trends has been digitalisation — the gradual digitisation of data and work processes. It has also affected the financial sector, where new instruments — digital financial assets (DFAs) — are being developed [1, p. 7].

It is estimated that by 2030, trading in digital financial assets linked to securities alone will be between \$ 4 trillion and \$ 5 trillion.¹ The Russian market of digital financial assets will increase from the current RUB 70 billion to RUB 5–10 trillion by 2027–2028²

Digital assets are designed not only to increase the efficiency of the financial market and the economic system as a whole [2, p. 84]: the participants of transactions with them — investors and issuers — receive a less risky and costly, but faster way of conducting transactions. In addition, investors can split into shares those assets, the acquisition of which is too costly and risky. Market participants also have access to less liquid but more profitable financial instruments: for example, surrogates whose securities are not authorised for trading on the stock exchange, cultural and artistic objects, and other financial instruments.

The development of the digital financial assets market is expected to save on transaction costs, overheads, and administrative expenses [3]. In addition, companies will be able to quickly tokenise assets, attract financing for them, and gain access to a new liquidity market. Distributed registry technology in the use of digital financial assets allows to reduce the number of intermediaries, which should reduce costs³ [4, p. 202]. Banks, on the other hand, are interested in digital financial assets to expand their investment product lines [5, p. 124].

Over the past few years, many sanctions have been imposed on the Russian Federation by un-

friendly states, which has complicated the mechanisms of foreign trade settlements. Therefore, the use of digital financial assets in our country is one of the promising directions that will help speed up foreign trade operations and reduce the impact of sanctions. This topic is not sufficiently studied in the world, and most countries do not have such experience. For Russia, however, the emergence of new mechanisms is now more relevant and in demand than ever before.

CHARACTERISATION OF THE STATE OF THE RUSSIAN DIGITAL FINANCIAL ASSETS MARKET

Digital financial assets are digital rights that exist and are traded in an information system by means of a blockchain-based distributed ledger technology. The advantage of this technology is the possibility to automate the process of execution of transactions with digital financial assets through the use of smart contracts,⁴ which are actually a programme that allows to automatically track and ensure the execution of all obligations under the transaction [6, p. 62].

Digital financial assets are characterised by the following features: the absence of a centre or subject of issuance, as well as intermediaries; simplicity of the mechanism of issuance and registration of a digital wallet; reduction of transaction costs; the ability to make payments and transactions around the clock; openness for third-party developers to study them [7, p. 144; 8, p. 143].

There are quite a large number of different digital financial assets that can be used for international settlements: crypto assets (cryptocurrencies, tokens, cryptographic securities), digital fiat assets (smart contracts and electronic money), other digital financial assets (assets for P2P lending) [9, p. 974].

Many countries are still in the process of forming their legislation on the regulation of digital financial assets. In Russia, Federal Law No. 259-FL dated 31.07.2020 'On Digital Financial Assets,

¹ URL: <https://www.mckinsey.com/industries/financial-services/our-insights/tokenization-a-digital-asset-deja-vu>

² URL: <https://www.vedomosti.ru/investments/articles/2024/03/26/1027931-mosbirzha-ozhidaet-vzrivnogo-rosta-rinka-tsfa>

³ URL: <https://www.vedomosti.ru/business/articles/2022/06/08/925659-zachem-biznesu-tsifrovie-finansovie-aktivi>

⁴ URL: https://www.cbr.ru/find_infrastructure/digital_oper/

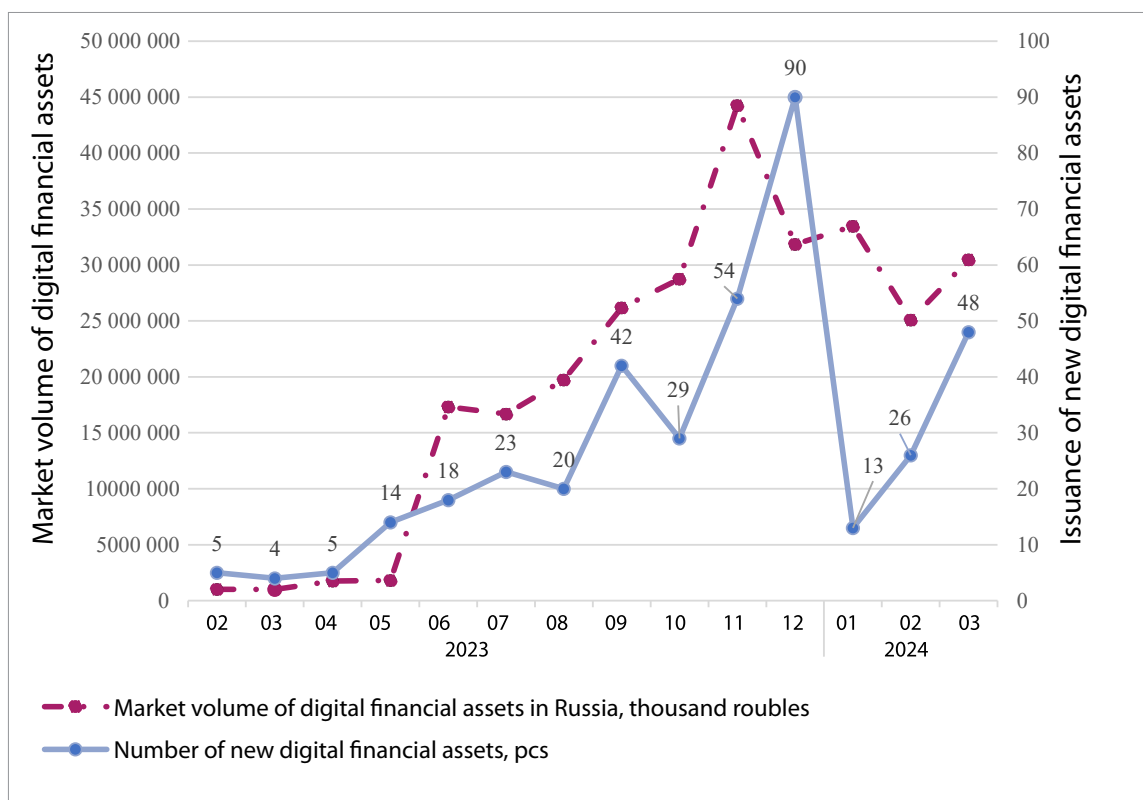


Fig. 1. Market volume of digital financial assets, RUB thousand and issuance of new digital financial assets, pcs

Source: compiled by the authors based on URL: <https://cbonds.ru/dfa/?ysclid=luhfbh35pv703308035>.

Digital Currency and Amendments to Certain Legislative Acts of the Russian Federation⁵ (hereinafter — FL on digital financial assets) was adopted as early as in 2020. According to this regulatory legal act, in our country digital financial assets are understood as ‘digital rights, including monetary claims, the possibility of exercising rights on equity securities, the right to participate in the capital of a non-public joint stock company, the right to demand the transfer of equity securities, which are stipulated by the decision to issue digital financial assets in the manner prescribed by this Federal Law, the issue, accounting and circulation of which are possible only by making (changing) entries in the information system on the basis of the distributed register, as well as in other information systems’.⁶ It is also possible to issue hybrid digital rights, which combine the properties

of digital financial assets and utilitarian digital rights (for example, as provided for in Article 8 of Federal Law No. 259-FL dated 02.08.2019 ‘On Attracting Investments with the Use of Investment Platforms and on Amendments to Certain Legislative Acts of the Russian Federation’).⁷

Russian legislation defines the operator of the information system where digital financial assets are issued (there are 11 such operators in Russia by 2024), whose task is to ensure the functioning of information systems where digital financial assets are issued and recorded; and the operator of digital financial assets exchange (there are 2 such operators in Russia).

By the end of 2023, 10 platforms for issuing digital financial assets were identified in the register of the Central Bank of the Russian Federation: Sberbank, Alfa Bank, Eurofinance Mosnarbank, National Settlement Depository, Spb Exchange,

⁵ URL: https://www.consultant.ru/document/cons_doc_LAW_358753/

⁶ URL: https://www.consultant.ru/document/cons_doc_LAW_358753/

⁷ URL: https://www.consultant.ru/document/cons_doc_LAW_330652/

Atomise, Lighthouse, Distributed Ledger Systems (Masterchain), Tokens (Tokeon) and Blockchain Hub (part of the MTS ecosystem). At the same time, there is only one operator for exchanging and creating a secondary market for digital financial assets — the Moscow Stock Exchange.

The Russian market of digital financial assets is in the stage of active development (*Fig. 1*).

Once the use of digital financial assets in international settlements is authorised, interest in the Russian market will increase — the volume and number of new digital financial assets will increase.

FOREIGN EXPERIENCE IN THE REGULATION OF DIGITAL FINANCIAL ASSETS

In foreign sources there is a more general term — ‘digital assets’, which means literally everything that exists in digital format, including cryptocurrencies, NFTs, asset-backed tokens, tokenised real estate and so on. When considering the application of digital financial assets in international settlements, special attention should be paid to the problems related to their legal regulation and circulation (*Fig. 2*).

It should be noted that in some jurisdictions the legal regulatory regime implies prohibitions of the most risky (in the opinion of regulators) types of digital assets for all entities.

Thus, there is a situation in the world where the same digital assets in different jurisdictions may have different legal nature and legal regulatory regimes, which creates risks of invalidation of transactions with them in international settlements. In addition, differences in the requirements of states related to the issuance and circulation of digital financial assets may impose additional obligations on individual participants in the relevant legal relations.

A key step to remove legal uncertainty and minimise legal risks in this area will be the development of international standards and norms for the regulation of digital assets as a means of international settlement. At the moment, individual international organisations⁸ are developing framework regulations. Point solutions include the conclusion of international treaties and agreements by countries involved in settlements.

⁸ URL: <https://documents.un.org/doc/undoc/gen/v20/025/50/pdf/v2002550.pdf?token=g1pkDP35WSrWTRgKP8&fe=true>; URL: <https://www.unidroit.org/work-in-progress/digital-assets-and-private-law/>

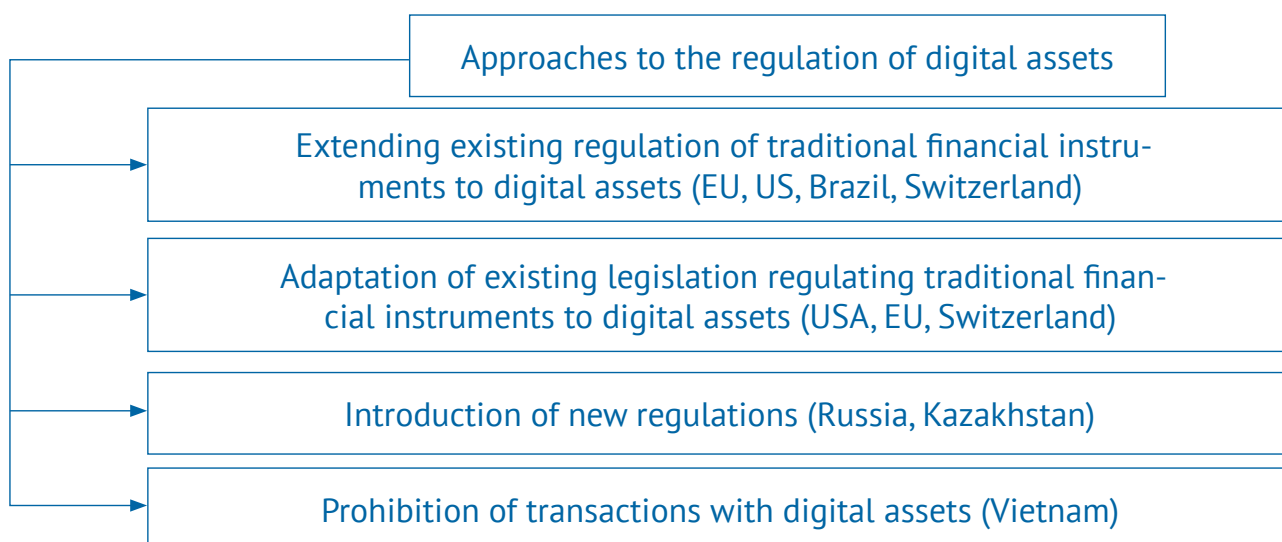


Fig. 2. Approaches to the regulation of digital assets by different countries

Source: compiled by the authors based on URL: <https://www.nasdaq.com/solutions/marketplace-technology/about-digital-assets>



Russian practice of using digital financial assets and international settlements: opportunities, peculiarities, and risks

To understand the level of Russia's preparation for international settlements using digital financial assets, it is necessary to consider the issues of their legal regulation and collision regulation of cross-border transfers.

Digital assets in Russia are singled out as a separate object of regulation with a special legal status (direct regulation model). The Civil Code enshrines the concept of digital rights (Article 141.1 of the Civil Code of the Russian Federation) and stipulates the need for special regulation of rights recognised as digital rights. The Federal Law on Digital Financial Assets in Russia defines certain types of digital rights, specifies their content, and sets out the requirements for their issuance, accounting, and circulation. Thanks to the use of information technologies (e.g., a unique code for digital financial assets), holders have direct access to their digital rights without the involvement of intermediaries. The law includes operators of information systems and digital financial assets exchanges among the main participants in the infrastructure of the digital rights market. The law also effectively regulates the use of smart contracts: 'The terms of a transaction may provide for the fulfilment by its parties of obligations arising therefrom upon the occurrence of certain circumstances without a separately expressed additional volition of its parties aimed at the fulfilment of the obligation. This may be done by means of information technologies specified in the terms of the transaction'.⁹

The Federal Law on Digital Financial Assets contains norms aimed at regulating the participation of foreign persons in legal relations with digital financial assets in Russia, determining the application of Russian law to such legal relations. It also provides for the possibility of performing transactions with digital financial assets issued in foreign information systems through a Rus-

sian digital financial assets exchange operator. However, the detailed procedure of such turnover is not regulated by the legislation: there are no rules for admission of foreign digital financial assets to circulation in the Russian market [10, p. 27], the mechanism of interaction between Russian operators of digital financial assets exchange and foreign operators of digital financial assets exchange is not defined.

The issues of information security, qualification of foreign digital rights as digital financial assets (by analogy with the qualification of foreign financial instruments as securities of foreign issuers (Article 51.1 of Federal Law No. 39-FL dated 22.04.1996 'On the Securities Market'¹⁰); are currently being worked out; requirements to the financial standing and business reputation of the issuer of foreign digital financial assets and their quality (liquidity, availability of collateral), to the disclosure of information on digital financial assets by the responsible person and to ensuring their fulfilment by the issuer are being established.

It should be noted that when addressing issues of conflict of laws regulation of cross-border transfers of digital assets, the application of classical approaches to determining the legal regime is complicated by their unique characteristics (existence in the form of computer code, cross-border nature). The following rules may be considered as conflict of laws options for determining the applicable law for financial transactions in a decentralised technological environment for participants: the application of the law of the place of the account in which the digital financial assets are held or the location of the intermediary holding the account; choice of law by the operator or users of the distributed registry, subject, for example, to the approval of the chosen law by the financial supervisory authority and public disclosure of the information on the chosen law by the financial registry operator or users of the distributed registry.

⁹ URL: https://www.consultant.ru/document/cons_doc_LAW_5142/1cd43e51fbd4129343b325971a466ec5cd32a425/

¹⁰ URL: https://www.consultant.ru/document/cons_doc_LAW_10148/

Special attention should be paid to the issue related to the legislative prohibition to accept digital financial assets as a means of payment for transferred goods, 'works, rendered services, as well as in any other way that allows assuming payment by a digital financial asset for goods (works, services)' (part 10 of Article 4 of the Federal Law on Digital Financial Assets).

The first steps to mitigate this restriction have been taken. At the beginning of March 2024, the Federation Council of the Federal Assembly of the Russian Federation approved amendments to the Federal Law on Digital Financial Assets, allowing the use of digital financial assets in international settlements: 'Digital financial assets may be used as counterpart under foreign trade agreements (contracts) concluded between residents and non-residents, which provide for the transfer of goods, performance of work, rendering of services, transfer of information and results of intellectual activity, as well as the use of digital financial assets in international settlements including exclusive rights thereto'.¹¹

The creation and recording of digital rights exclusively within Russian systems may be critical for non-residents. The willingness of foreign counterparties to participate in transactions with digital financial assets on Russian platforms will facilitate the introduction of innovations and the development of the digital economy in Russia. A key role for the digital financial assets market in Russia can be played by the availability of market makers and market pricing for digital financial instruments, which increases their liquidity and attractiveness for investors.

The maximum effect of digital assets can be achieved due to their technological advantages, flexible regulatory regime, and the possibility of circulation in the organised market in addition to the already established mechanism. Creating a legal framework for the traditional financial market infrastructure will expand the potential of the digital rights market, including increasing

the scale of their circulation, and will contribute to increasing their liquidity and, consequently, their investment attractiveness.

On 11 March 2023, President of the Russian Federation V.V. Putin signed the long-awaited law on the use of digital financial assets in international settlements.¹² It is assumed that now a counterparty from another state will have to register on platforms in Russia, which may cause some difficulties and affect the liquidity of digital financial assets. In addition, the settlement procedure has not yet been fully worked out, and therefore additional costs may arise, for example, related to the involvement of consultants.

In international settlements using digital financial assets, the Russian and foreign parties to the transaction must be registered on the operator's platform. Then, when paying for any goods under a contract, the Russian party needs to transfer digital financial assets from its wallet to the wallet of its foreign partners. Thus, it will be a transfer within one platform, and it will be realised virtually instantly.

Such a transfer does not require a bank account — digital financial assets can be stored in your wallets and freely disposed of. The absence of any intermediaries is also a plus. The foreign recipient can use the digital financial assets for their intended purpose or in subsequent transactions, as well as realise them on the platform. Only digital financial assets issued within the legal framework of the Russian Federation are valid in this scheme.

However, counterparties from other countries that accept as payment Russian digital financial assets that are accounted for exclusively in the Russian jurisdiction run the risk of remaining inside our financial system. This may also affect the liquidity of digital financial assets and limit their widespread use in international settlements.

The market of digital financial assets in Russia today has a rather small liquidity, but the tech-

¹¹ URL: <https://www.consultant.ru/law/hotdocs/84020.html>

¹² URL: <http://publication.pravo.gov.ru/document/0001202403110010?index=1>

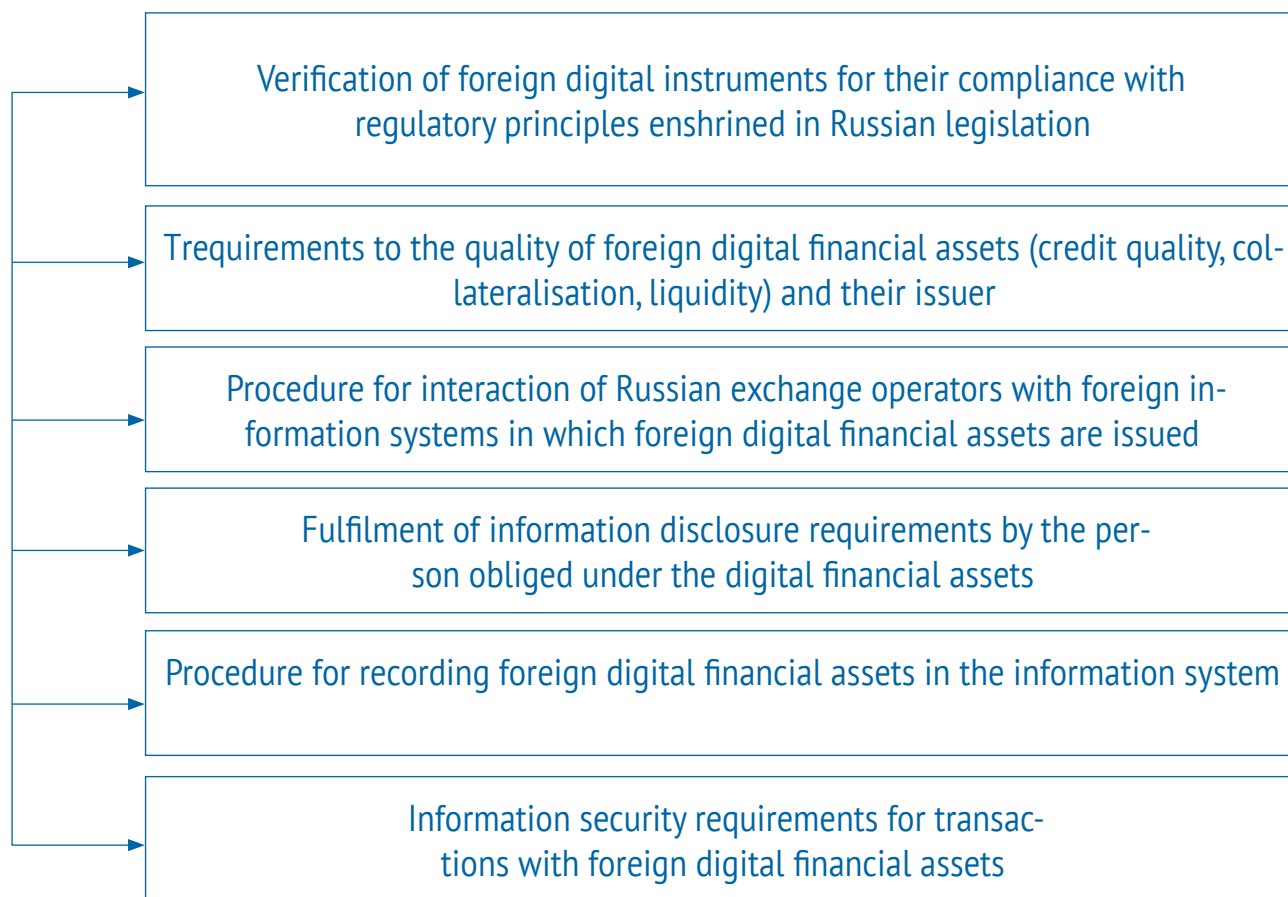


Fig. 3. Issues for joint study in the field of interaction between the Russian and international digital financial assets markets

Source: compiled by the authors.

nological possibilities of its circulation in other countries are limited.

Undoubtedly, international settlements using digital financial assets make it possible to bypass the banking system and make them 'invisible' to unfriendly countries, but the above-mentioned legal risks and those related to liquidity should not be discounted. In addition to these, there are industry, country, systemic, market, inflation, credit, regulatory, operational and — one of the most important — information security and IT-related risks in general.

Today, there is a clear need to create a favourable environment for the use of digital assets in international settlements, overcoming obstacles — both technological and those related to differences in national legal regimes and the lack

of international standards and norms for their regulation. The above-mentioned problems require a comprehensive approach and active participation of states in creating a flexible and adaptive mechanism for international settlements using digital financial assets.

At the same time, the detailed procedure for introducing foreign digital financial assets into circulation on the Russian market is also not regulated. In order to develop this segment, it is necessary to establish a mechanism of interaction between Russian operators of digital financial assets exchange and foreign ones and admission of foreign digital financial assets to circulation in the Russian market.

Figure 3 shows the issues that the Bank of Russia plans to work out together with the participants of the digital financial assets market.

The implementation of this initiative will allow Russian investors to carry out transactions with foreign digital assets that meet established quality criteria (availability of the issuer, collateral, etc.).

The issue of recognition, liquidity and turnover of digital financial assets is of key importance, because these three parameters are the key to success in building a system of international settlements. Winning confidence in new financial instruments (in particular, digital financial assets) on the part of international counterparties requires government agencies to develop a set of measures to create an appropriate system of cross-border payments.

International agreements should recognise digital financial assets as assets that can be used in international settlements. Principles for their cross-border circulation should also be established for digital financial infrastructures involved in settlements.

CONCLUSIONS

In order for the Russian market of digital financial assets to serve foreign trade operations, it needs to reach a fundamentally new level of development and liquidity; it is necessary to ex-

pand the functionality of digital financial assets for foreign trade and qualitatively work out the issues of interaction between Russian operators for issuing digital financial assets with foreign counterparties.

The current Russian market for digital financial assets has good development potential, but the current opportunities for their use for international settlements are limited, which directly affects the market's liquidity.

In many countries, digital financial assets are still poorly regulated, or even banned. For their successful application in international settlements, it is necessary that they be legally authorised not only in Russia, but also in the counterparty's country.

The market for digital financial assets offers new opportunities for both countries and participants, but we should not forget about the risks and potential problems that users may face.

Today, the mass use of digital financial assets in international settlements is complicated by problems related to their regulation and increased volatility. At the same time, their use in international settlements with friendly countries is objectively necessary for Russia and will help to reduce sanctions risks.

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I.A. Kokorev — analyzing the problems of using digital financial assets to ensure international settlements.

K.L. Meletidi — analyzing the risks of using digital financial assets for international settlements, analyzing foreign experience of using digital financial assets for foreign trade settlements.

A.M. Lyukshin — analyzing the Russian market of digital financial assets, its regulation, opportunities for the Russian Federation to use digital financial assets for international settlements.

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