As Delivered

Thank you all so much for being here today, and to David and the Brookings Institution for hosting me. It has been a little more than six months since Russia began its brutal and unprovoked invasion of Ukraine, the most significant threat in generations to the post-World War II international order. Over those six months, we have worked with our allies and partners to mount an unprecedented global response to help end Russia’s unjustified aggression. As part of our overarching strategy to end Russia’s invasion we have deployed sanctions with two primary objectives in mind: to deny Putin revenue to pursue his war of choice and to erode Russia’s ability to wage war going forward by disrupting the critical supply chains feeding Russia’s military-industrial complex.

According to independent academic analysis at Yale, Russia’s imports have collapsed by as much as half, domestic production has been hammered due to shortages of key inputs, and foreign companies accounting for 40% of Russian GDP have left the country. Moreover, our sanctions and export controls targeting their military industrial complex have denied Russia access to critical equipment and imports, degrading their military capabilities in ways we’re already seeing on the battlefield—with Russia increasingly reliant on outdated, Soviet-era weapons without access to the chips needed to replenish their stocks of modern munitions.

However, there is one part of the Russian economy doing even better than when the war began: their oil industry. This summer, Russia received prices 60 percent higher than last year for its energy exports, more than offsetting the decline in its export volumes. This situation is unacceptable to us, to our allies, and to the people of Ukraine.

But this situation is also complicated. Consumers and businesses in the U.S. and around the world are already facing elevated energy prices. Simply banning or sanctioning purchases of Russian oil might deny Russia some revenue, but it would have the perverse effect of sharply increasing global consumers’ cost of living and increasing the risk of a global recession.
It is important to remember that the United States and a number of our G7 allies have already banned the import of Russian oil into our countries. The impact of further actions to prevent the export of Russian oil to other countries would disproportionately fall on the low- and middle-income countries still buying it. These countries are already facing high energy and food prices due to Russia's unprovoked invasion of Ukraine. We know that economic instability in low-income countries often leads to political instability, and the last thing we want is for additional countries to be destabilized by Russia's actions. And, more broadly, we know that ensuring the continued flow of as much oil as possible onto the global market is critical to reducing prices in our country and around the world.

That is why, last Friday, the G7 Finance Ministers agreed to finalize and implement an innovative policy that puts downward pressure on global energy costs by allowing Russian oil to continue to flow onto the global market while reducing Russian revenue: a price cap on Russian oil. Today, I'd like to share why we think the price cap is so critical, explain how it will work, and dispel a few myths we've heard along the way.

Let's start with how it will work. In June, the EU agreed to a sixth package of sanctions that will ban not only imports of seaborne Russian oil in the EU, but—as of December 5th—will also ban the provision of associated maritime services like insurance, trade finance, banking, brokering, and navigation services by companies in the EU to those associated with Russia's seaborne export of crude oil, regardless of where those shipments are headed. These maritime services are often essential—in many cases, seaborne oil shipments cannot be made without them.

Critically, the providers of some of these services are heavily concentrated in the EU and G7 countries. For example, the EU and G7 provide 90% of global shipping insurance, and they provide the majority of financing and payments services for the oil trade. One potential byproduct of this package could be a substantial shut-in of Russian production of oil and refined product, and associated elevated prices, which could limit or reverse the intentions of the action. This price increase would undermine the well-intentioned goal of limiting Russia's revenue from oil sales while imposing an additional and unintentional burden on global consumers of oil.

The price cap is designed to address this outcome by creating a carveout for services related to the seaborne transport of Russian oil that is sold at or below the cap level—keeping this oil on the market and flowing to consumers who need it but still restricting Russian revenue. Countries outside the G7 can keep buying Russian oil, and companies in the G7 can continue to
offer services to support those sales—as long as the oil these services support is purchased at or below a certain price. And in particular, some of the most vulnerable countries in the world—low- and middle-income oil importers—will benefit most from access to this lower-priced oil.

When it comes to implementation, two critical pieces are compliance and enforcement—how market participants know oil is coming from Russia, and therefore needs to be priced below the cap, and how we deter and punish evasion and knowing violations. On compliance, we’re working with the G7 to develop a robust but simple documentation and attestation system that can give service providers comfort that they are complying appropriately. On enforcement, those that evade the price cap by falsifying documentation or otherwise hiding the true origin or price of the oil would face consequences under the domestic law of jurisdictions implementing the price cap.

Our approach to implementation is guided by the principle that Russian oil should continue to reach the global market, provided purchasers and service providers abide by the price cap in good faith.

That is why today, to offer greater clarity to the market and help achieve this objective, I am announcing that Treasury’s Office of Foreign Assets Control is issuing preliminary guidance on how this compliance system will work. OFAC will follow up with additional, formal guidance in the coming weeks to help ensure these compliance expectations are sufficiently clear to facilitate the flow of Russian oil. This action helps formalize the United States’ commitment to implementing the price cap.

Finally, from a technical perspective, one of the questions I’ve heard most often is how the price will be set. And this relates closely to a common objection I’ve heard, that Russia will not sell oil at or below the cap and instead will simply refuse to export. The way the cap is set is the reason we think that won’t happen. Russia may bluster and say they won’t sell below the capped price, but the economics of holding back oil just don’t make sense: The price cap creates a clear economic incentive to sell under the cap.

We intend to set the price cap above Russia’s marginal cost of production, at a level consistent with prices they have historically accepted. Russia doesn’t have much storage capacity for oil, and many of its wells and equipment are far from state of the art, which makes it hard for them to stop and later restart production without incurring significant costs. And that problem is only going to get worse as our sanctions continue to deny them
access to critical software and drilling equipment. As a result, Russia will be forced to continue selling or risk long-term degradation of its capacity to produce.

That leaves quite a bit of room below both prevailing market prices and the price Russia is receiving today. It means we have an opportunity to deny Russia the revenue to pursue its unconscionable war while lowering some of the economic pressure countries around the world are feeling.

Russia knows that—and it’s why they are already responding to those clear economic incentives. They are already offering long-term contracts to potential buyers at steep discounts—of 30% or more—far in advance of the price cap’s implementation. The fact that they are doing this reveals how worried they are and shows how the price cap is already working to drive down Russia’s revenues. We view this as one of the policy’s key features: that it can achieve its objectives even if some buyers choose not to formally join because they also want to pay lower prices for Russian oil. The price cap gives them greater price transparency and leverage when they negotiate with Russia. So even if Russia tries to get around the cap with buyers outside our coalition, their revenue will still be driven down, as we’re already seeing.

We are clear-eyed that Russia can go find service providers outside the G7 and the other members of our coalition to replace the maritime services blocked by the EU ban. But these alternative services will be expensive and less reliable than the services provided by G7 firms. There is a reason the world relies on EU and G7 firms for the vast majority of these services. Building up a services ecosystem outside the coalition will cost Russia more money, which will help reduce the Kremlin’s revenues even more.

Let me conclude by taking a step back from the details. We are moving forward with this extraordinary proposal because it is essential that the global community take steps to deny the Kremlin the revenue it is using to prop up its economy and fight its unjustifiable war in Ukraine. The price cap seeks to create incentives that reduce Russia’s revenues while its oil continues to flow. The bottom line is that everyone wins but the Kremlin.

This is not an academic conversation. We face the largest ground invasion in Europe since the end of World War II, one being perpetrated by a regime that will not be easily deterred. It is
critical that we take this step to deny Russia the revenue they are using to pursue this brutal invasion while continuing our efforts to disrupt their critical supply chains and degrade their military-industrial complex. We look forward to your advice on implementation as we move forward with this policy. Thank you again for being here. I'll turn it back to David to introduce a panel where you'll hear more on this from my colleague Ben Harris.
