

Price Cap on Russian Crude Oil Becomes Effective

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On December 5, 2022, the price cap on Russian crude oil that was announced by the G7 Finance Ministers in September 2022 went into effect at a level of \$60 per barrel. The price cap is implemented by prohibiting the provision of certain services that enable maritime transportation of Russian crude oil unless the oil is purchased at or below the price cap. The price cap is intended to minimize disruptions to global markets while limiting Russia's ability to generate revenue from crude oil production. The European Union, members of the G7 (Canada, France, Germany, Italy, Japan, the United Kingdom and the United States) and Australia are acting as a coalition to implement the price cap.

On November 22, 2022, the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) announced that Secretary of the Treasury Janet Yellen issued a determination pursuant to Section 1(a)(ii) of Executive Order 14071 that effectively prohibits the exportation, reimportation, sale or supply, directly or indirectly, from the United States or by a U.S. person, wherever located, of certain "Covered Services," as they relate to the maritime transportation of Russian-origin crude oil, to any person located in Russia. The Covered Services are trading/commodities brokering; financing; shipping; insurance, including reinsurance and protection and indemnity; flagging; and customs brokering. The provision of Covered Services that would otherwise be prohibited, however, is authorized when the price of the Russian-origin crude oil does not exceed the relevant price cap.¹

Compliance Framework: Safe Harbor and Enforcement Priorities

In a much-anticipated guidance document issued to accompany the determination, OFAC set forth a framework that provides a safe harbor from OFAC enforcement for U.S. service providers that comply in good faith with the guidance's recordkeeping and attestation process. Such a safe harbor construct is a departure from OFAC's traditional strict liability approach to sanctions. Under the safe harbor process, each party in the supply chain of Russian oil shipped via maritime transport is positioned to demonstrate or confirm that the Russian oil was purchased at or below the price cap. U.S. persons providing Covered Services must ensure that refiners or other purchasers in third countries that have not prohibited the import of Russian oil provide documentation showing that the Russian oil was purchased at or below the relevant price cap.

OFAC described three tiers of persons and set forth requirements for members of each tier to be afforded the safe harbor:

- Tier 1 consists of actors that have direct access to price information, such as commodities brokers or traders. They must retain price information and provide information or attestations to Tier 2 and Tier 3 actors, as needed. Examples of information or documentation include invoices, contracts, receipts and other proof of payment.
- Tier 2 consists of actors that are sometimes able to request price information, such as financial institutions providing trade finance, customs brokers and ship/vessel agents. Examples of information or documentation include invoices, contracts, receipts, other proof of payment and price cap attestations. To avail themselves of the safe harbor,

¹ This client alert is for informational purposes only and does not constitute legal advice. Complex assessments often have to be made as to which sanctions regime applies in any given instance, given the multinational touch points of many entities and individuals. In that regard, given the complex and dynamic nature of these sanctions regimes, there may be developments not captured in this summary. Moreover, while the summary was accurate when written, it may become inaccurate over time given developments. For all of these reasons, you should consult with a qualified attorney before making any judgments relating to sanctions, as there are potentially severe consequences of failing to adhere fully to sanctions restrictions

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Tier 2 parties must, to the extent practicable, request and retain relevant information or documentation showing that the Russian oil was purchased at or below the price cap. If that is not feasible, the Tier 2 actor must obtain and retain attestations from its customers confirming that the oil was, or will be, purchased at or below the price cap.

- Tier 3 consists of actors that do not have direct access to price information, such as insurers, reinsurers, P&I clubs, ship owners/carriers and flagging registries. Examples of information or documentation that Tier 3 actors may rely on include sanctions exclusion clauses within policies, clauses within policies that exclude coverage for activities related to the maritime transport of Russian oil purchased above the price cap and price cap attestations.

To be afforded safe harbor, U.S. service providers must retain relevant records for five years, consistent with 31 C.F.R. § 501.601. OFAC explained that service providers are not required to use a particular form of attestation to be afforded the safe harbor.

In the guidance document, OFAC said that it would not pursue a penalty against a U.S. service provider that reasonably relies on the documentation or attestations described in the guidance document, unless the U.S. provider knew or had reason to know that such documentation was falsified or erroneous or that the Russian oil was purchased above the relevant price cap. OFAC said that as part of the safe harbor, it expects that U.S. service providers will continue to perform standard due diligence customary for their industry and for their role in a particular transaction. OFAC noted that a customer's or counterparty's refusal or reluctance to provide the necessary documentation or attestation should be considered a red flag that may indicate the entity has purchased Russian oil above the relevant price cap.

OFAC emphasized that it intends to focus its enforcement responses on those actors who willfully violate or evade the price cap and that U.S. persons are required to reject and report evasive transactions or transactions that violate the determination.

Scope of Relevant Prohibitions

OFAC also used the guidance document to clarify the contours of the relevant restrictions. For example, OFAC explained that the processing, clearing or sending of payments by banks is not included in the definition of "financing" for the purposes of the determination, where the bank (1) is operating solely as an intermediary and (2) does not have any direct relationship with the person providing services related to the maritime transport of the Russian oil (*i.e.*, the person is a non-account party) as it relates

to the transaction. OFAC also noted that services with respect to foreign exchange transactions and the clearing of commodities futures contracts are outside the scope of "financing."

OFAC also explained that the price cap applies from the embarkment of maritime transport of Russian oil (*e.g.*, when the crude oil is sold by a Russian entity for maritime transport) through the first landed sale in a jurisdiction other than Russia, through customs clearance. In other words, once the Russian oil has cleared customs in a jurisdiction other than Russia, the price cap does not apply to any further onshore sale. However, if after clearing customs, the Russian oil is taken back out on the water using maritime transport without being substantially transformed outside of Russia, the price cap still applies. The oil is only considered no longer of Russian origin once it has been substantially transformed (*e.g.*, it is refined or undergoes other substantial transformation such that the product loses its original identity and is transformed into a new product having a new name, character and use) in a jurisdiction other than Russia. OFAC noted that it does not consider blending of crude oil alone to be substantial transformation for the purpose of the determination.

Under the terms of Secretary Yellen's determination, Russian-origin crude oil that is loaded onto a vessel at the port of loading prior to 12:01 a.m. EST on December 5, 2022, and unloaded at the port of destination prior to 12:01 a.m. EST on January 19, 2023, is excluded from the prohibition and therefore not subject to the price cap.

General Licenses

At the same time that OFAC announced the determination and issued the guidance document, OFAC also issued three general licenses to accompany the determination:

- General License No. 55 authorizes through 12:01 a.m. EDT on September 30, 2023, transactions prohibited by the determination related to the maritime transportation of crude oil originating from the Sakhalin-2 project, provided that the crude oil is solely for importation into Japan.
- General License No. 56 authorizes transactions prohibited by the determination related to the importation of crude oil into Bulgaria, Croatia or landlocked EU member states as described in Council Regulation (EU) 2022/879 of June 3, 2022.
- General License No. 57 authorizes certain transactions prohibited by the determination that are ordinarily incident and necessary to addressing vessel emergencies related to the health or safety of the crew or environmental protection, including safe docking or anchoring, emergency repairs or salvage operations.

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Conclusion

The price cap is a novel policy device that will likely raise new compliance challenges for service providers that engage in transactions related to Russian-origin crude oil, particularly given the broad coalition that is implementing the price cap. Service

providers will need to be cognizant not only of the U.S. prohibitions, but also prohibitions connected with the price cap that are issued by the European Union and EU member states, other G7 countries and Australia.