

THE VENEZUELAN OIL REGULATION AND THE LICENSES THAT COULD BE GRANTED TO INTERNATIONAL OIL COMPANIES

José Ignacio Hernández G.
Universidad Católica Andrés Bello, Venezuela
Growth Lab, Harvard Kennedy School

INTRODUCTION

1. During the last months, there have been discussions about the licenses that the United States Government (USG) could issue concerning the Venezuelan oil industry. The primary debate is the possibility of granting a license that allows international oil companies (IOCs) to expand their oil operations in the country and for that oil to be traded in the U.S.¹

2. Under the Venezuelan Law, it will be unlawful to transfer the oil production and export activities to IOCs with a reform of general license 8, because only the Government of Venezuela can perform those activities. However, it is possible to relieve the prohibitions introduced in the 2020 reforms of that license to authorize IOCs to renegotiate their debt with PDVSA and, eventually, to export upgraded oil (not crude oil). Those reliefs must accomplish transparency and humanitarian standards, resulting from genuine advances in the Venezuelan transition.

I. THE SANCTIONS AGAINST PDVSA AND THE LICENSE N° 8

3. Two executive orders prevent PDVSA operations in the U.S. and with U.S. persons: (i) executive order N° 13857, dated January 25, 2019, and (ii) executive order n° 13884, dated August 5, 2019. Despite prohibitions against third parties operations (knowns as “secondary sanctions”), those orders apply only to PDVSA and its affiliates (any corporation in which PDVSA has at least 50% of the shares).

4. According to the Venezuelan Law -as is explained in the next section- PDVSA has a monopoly in the oil production and exports activities (but not in natural gas). This is the main reason the executive orders have a greater impact on the Venezuelan oil industry: blocking PDVSA is equivalent to blocking oil exports to the U.S.

5. The constraints resulting from the executive orders could be relieved through licenses or overruling said orders. The current sanctions framework facilitates exceptions based on humanitarian reasons.² Therefore, it is possible to create exceptions that allow PDVSA to conduct operations related to the U.S. by issuing licenses to authorize specific transactions, as is the case of general licenses n° 8 and 40.³ According to U.S. policy, any new license should be conditioned to genuine advances in the Venezuelan transition.⁴

6. License N° 8 applies to several private firms, including Chevron, an IOC that is the minority shareholder in joint ventures, that are corporations in which PDVSA must have more than the 50% of the shares.⁵ Consequently, those joint ventures are also sanctioned subjects. Therefore, Chevron's operations with PDVSA were barred as a U.S. corporation. To avoid the disruption of those operations, license N° 8 was granted on January 28, 2019, to authorize "*all transactions and activities ordinarily incident and necessary to operations in Venezuela involving PdVSA*".⁶

7. This license was renewed -without any change- several times between June 2019 and January 2020.⁷ However, on April 21, 2020, OFAC released License N° 8F, which has been renewed several times until License N° 8J, currently in force (issued on May 27, 2022).⁸ The new licenses introduced -or clarified- several restrictions:

- a) It only authorizes operations that "*are ordinarily incident and necessary to the limited maintenance of essential operations, contracts, or other agreements*" that "*were in effect before July 26, 2019*". Those operations must be necessary "*for safety or the preservation of assets in Venezuela*", and operations that "*are ordinarily incident and necessary to the wind-down of operations, contracts, or other agreements in Venezuela involving PdVSA (...) that were in effect prior to July 26, 2019*".
- b) The license clarified the scope of the prohibited operations, including ***operational prohibitions*** (such as the drilling, lifting, or processing of, purchase or sale of, or transport or shipping of any Venezuelan-origin petroleum or petroleum products); ***new activities*** (such as contracting for additional personnel or services, except as required for safety), and ***financial operations*** (the payment of any dividend, including in kind, to PdVSA, and any loans to, accrual of additional debt by, or subsidization of PdVSA).⁹

8. Whether the license increased the original prohibitions or clarified its scope, the truth is that the content of operations that Chevron can carry with PDVSA was substantially restricted, creating unfair burdens that may impair the continuity of its operations in Venezuela.

II. THE VENEZUELAN REGULATORY CONSTRAINTS ON THE PRIVATE INVESTMENT IN THE OIL INDUSTRY

9. The scope of rights that IOCs, like Chevron, can exert doesn't depend on the licenses granted by OFAC but on the Venezuela regulatory framework. This means that OFAC shouldn't grant any license that authorizes IOCs to perform operations with PDVSA that are prohibited according to Venezuelan Law.

10. The Organic Hydrocarbons Law prohibits private investment in upstream activities, oil exploration, and production (Art. 9).¹⁰ Only the national oil company, PDVSA, directly or through affiliates, can undertake those activities. Among those

affiliates are the joint ventures, in which PDVSA (through its affiliate, CVP) must have a majority control (Art. 22). Therefore, IOCs can act only as minority shareholders. In addition, private investors cannot export natural hydrocarbons because this activity can only be conducted by PDVSA (Art. 57). The terms and conditions under which IOCs can act as minority shareholders of joint ventures are authorized by a resolution enacted by the National Assembly. The Assembly should also approve any modification (Art. 33).

11. Chevron cannot directly perform exploration and production activities, as well as the natural crude exports, not as a result of sanctions against PDVSA but as a result of the Venezuelan Law. Hence, contrary to some opinion, Chevron cannot undertake exploration, production, and export activities with a license -because those will be unlawful activities under Venezuelan Law.¹¹ Consequently, a necessary condition to even consider reform of License N° 8J is to reform the Venezuela oil framework to authorize private investment to conduct activities that are currently a PDVSA's monopoly.¹²

12. The Maduro regime approved a political document -the "Anti-Blockade Law"- that purportedly grants absolute powers to the Executive to implement any economic policy reform. Due to its lack of legitimacy and violation of international standards of transparency, that political document cannot modify the Venezuela oil regulation.¹³

13. Besides regulatory constraints, other constraints would prevent the recovery of the Venezuelan oil industry, considering its collapse level and the PDVSA's criminal and civil liabilities based on the legacy public debt.¹⁴ The U.S. Department of Justice has concluded that "*fraud and corruption is reportedly common at PDVSA*".¹⁵ This is why not even a regulatory reform and a new license will be enough to recover the Venezuelan oil industry in the short term.

III. DEBT RENEGOTIATION AND THE VENEZUELAN LAW

14. As a result of PDVSA's collapse, the Venezuelan Government adopted some institutional arrangements to increase the role of private shareholders in joint ventures. Particularly, since 2013 PDVSA -through its affiliate, CVP- entered into financial agreements that allowed private investors (including Chevron) to finance the joint venture operations.¹⁶ Based on a textual interpretation of the Art. 57, private investors undertook the export of upgraded crude.¹⁷ In addition, PDVSA also modified the conditions of some joint ventures and signed oil services agreements -transactions that the National Assembly challenged.¹⁸

15. It could be concluded that the license N° 8J prohibited Chevron from participating in those financial agreements, including agreements to renegotiate its debt with payment in kind (considering the literal interpretation that could allow Chevron to export upgraded crude). Accordingly, the prohibitions introduced by license N° 8J created new constraints over the oil production due to the dependence on IOCs due to the destruction of the PDVSA's capacity.

16. Therefore, a license reform could allow Chevron to renegotiate its debt with PDVSA and eventually receive upgraded crude as payment, as long as those operations are consistent with the Venezuelan oil regulation.

17. However, any license reform that allows Chevron to renegotiate its debt with PDVSA must fulfill transparency standards, as well as the constitutional controls over PDVSA’s operations that the National Assembly must perform -controls that Maduro’s regime has barred.¹⁹

18. Finally, according to the general policy of the USG, any license should be conditioned to genuine advances in the democratic transition, including the improvement of the humanitarian conditions of the Venezuelan people. Consequently, any reform on the license must include requirements that facilitate the provision of humanitarian aid. Any license reform that authorizes Maduro to receive oil proceeds will not fulfill humanitarian standards as a result of the lack of capacity of the *de facto* Government of Maduro.²⁰

CONCLUSIONS

19. Beyond the constraint derived from the sanctions and the license N° 8J, the operations of IOCs in Venezuela are bound by several regulatory constraints in Venezuelan Law. Therefore, to increase the scope of Chevron’s rights in Venezuela, it is necessary to reform Venezuelan oil regulation: it is illegal -under Venezuelan Law- to expand those rights through reform of license N° 8J.

20. We can summarize our analysis by distinguishing, in general terms, the scope of rights of Chevron under Venezuelan Law and the prohibitions adopted by license 8J (in comparison with the original license N° 8).

Operations under the Venezuelan Law	Operations prohibited under license 8J (not established in the original license 8) could be overridden with a new license
<ul style="list-style-type: none"> • Rights as a minority shareholder of joint ventures (only joint ventures can perform exploration, production, and crude oil exports) • Right vested in the financial agreements subscribed with PDVSA • Export upgraded crude 	<ul style="list-style-type: none"> • Any new activities regarding the operations performed before July 26, 2019 • Purchase or sale of, or transport or shipping of any Venezuelan-origin petroleum or petroleum product, including upgraded crude

	<ul style="list-style-type: none"> • Any oil operation that, following the joint venture's agreements, is not necessary for safety • Any debt transactions prohibited by executive order N° 13808
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21. The only improvement in Chevron’s rights that could be derived from a new license is the overruling of the prohibition listed in license N° 8J, as long as the new operations are conducted according to the Venezuelan Law, as well as transparency and humanitarian standards. Under those conditions, Chevron could resume the activities that can perform according to the Venezuelan Law, including renegotiating its debt with agreements of payment in kind with upgraded crude (not natural crude).

22. However, to allow IOCs to undertake oil production and export activities, it will be necessary to reform the Venezuelan oil regulation and fulfill transparency and humanitarian standards. IOCs cannot undertake those activities based on reform on license N° 8.

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¹ For an accurate report on the current situation, see Palacios, Luisa, and Monaldi, Francisco (2022), "Venezuelan oil sanctions: not an easy fix", Columbia Center on Global Energy Policy, March 2022 at: https://www.energypolicy.columbia.edu/sites/default/files/file-uploads/Venezuela_CGEP_Commentary_031822-2.pdf. Particularly, according to news, Chevron could be negotiating with the *de facto* Government of Nicolás Maduro the regulatory reforms that could expand its rights in explorations and productions activities. See “The U.S. renews Chevron's Venezuela license through November under same restrictions”, *Reuters*, May 27, 2022: <https://www.reuters.com/business/energy/us-renews-chevrons-venezuela-license-through-nov-under-same-restrictions-2022-05-27/>, and “Chevron podría ampliar sus operaciones en Venezuela”, *Diario Las Américas*, July 7, 2022: <https://www.diariolasamericas.com/eeuu/chevron-podria-ampliar-sus-operaciones-venezuela-n4252440>

² See the *Guidance Related to the Provision of Humanitarian Assistance and Support to the Venezuelan People*, dated August 6, 2019. Also, see the report by the Venezuelan Working Group at the Atlantic Council (2022), *Exploring humanitarian frameworks for Venezuela*, at <https://www.atlanticcouncil.org/in-depth-research-reports/report/exploring-humanitarian-frameworks-for-venezuela/>

³ The license authorizes “all transactions and activities related to the exportation or reexportation, directly or indirectly, of liquefied petroleum gas to Venezuela, involving the Government of Venezuela, *Petróleos de Venezuela, S.A. (PdVSA)*, or any entity in which PdVSA owns, directly or indirectly, a 50 percent or greater interest”. OFAC issued license N° 40A, dated July 7, 2022.

⁴ For instance, see U.S. State Department, “Readout of the High-Level Coordination Meeting on Venezuela”, February 16, 2022, at: <https://www.state.gov/readout-of-the-high-level-coordination-meeting-on-venezuela/>

⁵ Art. 22, Hydrocarbons Organic Law.

⁶See <https://www.federalregister.gov/documents/2021/10/26/2021-23331/publication-of-venezuela-web-general-license-8-and-subsequent-iterations>

⁷ Licenses N° 8A, 8B, 8C, 8D, and 8E.

⁸ The renewals are 8G (November 17, 2020), 8H (October 21, 2021), 8I (November 24, 2022), and 8J (May 27, 2022).

⁹ The corporations listed in license 8 don't pay dividends to PDVSA: those dividends are paid by joint ventures. The IOCs that are minority shareholders can receive dividends from the joint venture. A rational interpretation of this prohibition is that joint ventures can pay dividends to the minority shareholder but not to PDVSA.

¹⁰ The prohibition does not apply to gas (except associated gas). According to the Organic Gas Law, gas production can be conducted directly with private investors. This paper doesn't address the gas industry.

¹¹ According to the news, “Chevron Corp. wants more control over the oil it produces in Venezuela, a move that would help the driller boost output and recover the debt if the U.S. eases sanctions amid a global fuel crunch”. See “Chevron Looks to Revamp Venezuela Oil Pact in Bid to Lift Output”, Bloomberg, July 6, 2022: <https://www.bloomberg.com/news/articles/2022-07-06/chevron-looks-to-revamp-venezuela-oil-pact-in-bid-to-lift-output>

¹² This is necessary to promote the recovery of the Venezuelan oil industry. See our proposal for a new oil regulation in Hernández, José Ignacio and Bellorín, Carlos (2019), “The case for a new Venezuelan Hydrocarbons Law as the basis of a new Hydrocarbons Policy: unlocking the path for recovery, stabilization, and growth,” in *The Journal of World Energy Law & Business, Volume 12, Issue 5*, 394. See also Hernández G., José Ignacio (2017), “La regulación de los hidrocarburos en Venezuela: situación actual y propuestas de reforma”, in *Revista de Direito Econômico e Socioambiental Vol 8, N° 3*. In 2020 the fourth legislature of the National Assembly approved the first draft of the legislative reform to remove the binding regulatory constraints. See Hernández G., José Ignacio (2020), “El nuevo proyecto de la Ley Orgánica de Hidrocarburos presentado por Comisión Permanente de Energía y Minas en septiembre de 2020”, in *Revista de Derecho Público N° 163-164*, 473. From an economic perspective, see Abuelafia, Emmanuel and Saboín, José Luis (2021), *Una mirada a futuro para Venezuela*, Washington D.C.: Inter-American Development Bank, I-23.

¹³ In 2020 the illegitimate national constituency assembly approved the Anti-Blocked Organic Law that authorizes Maduro -in violation of the Venezuela Constitution- to enter into any economic agreement, even to transfer assets to private investors, without fulfilling constitutional and legal requirements. A possible path is to transfer the oil production activities to private investors, a policy that will violate the Constitution and the Organic Hydrocarbons Law. See Hernández G., José Ignacio (2022), *Control de cambio y de precio en Venezuela. Auge y colapso institucional*, Caracas: Editorial Jurídica Venezolana.

¹⁴ Following Palacios and Monaldi's (n.1) conclusions, “while sanctions relief is necessary for improving Venezuela's oil outlook going forward, it is by no means a sufficient condition”. Regarding the oil industry's collapse, see Monaldi, Francisco, and Hernández, Igor (2016), *Weathering Collapse: An Assessment of the Financial and Operational Situation of the Venezuelan Oil Industry*, Center for International Development

Working Paper N° 327. PDVSA's public debt -and the several litigations claims by creditors- will create risks over any activity conducted by IOCs and PDVSA.

¹⁵ Criminal complaint, *U.S. v. Francisco Convit Guruceaga, et al.*, July 23, 2018, at 23

¹⁶ Monaldi, Francisco, and Hernández, Igor (2016), *Weathering Collapse: An Assessment of the Financial and Operational Situation of the Venezuelan Oil Industry*, cit., 29. The first agreement was subscribed with Chevron regarding Petroboscán.

¹⁷ According to an interpretation, this prohibition does not apply to the export of upgraded crude. Therefore, private investors could undertake upgraded crude exports through an agreement with PDVSA. Precisely, and despite the collapse, production of upgraded crude has continued. See *Reuters*, July 8, 2021, at: <https://www.reuters.com/business/energy/venezuela-resorts-upgraded-oil-blends-feeding-refineries-document-sources-2021-07-08/>

¹⁸ Resolutions dated September 25, 2018, and August 1, 2019.

¹⁹ Art. 187,3, Venezuelan Constitution.

²⁰ Venezuelan Working Group at the Atlantic Council (2022), *Exploring humanitarian frameworks for Venezuela*, cit.