

**THE UNCERTAIN FATE OF VENEZUELA’S  
BLACK PEARL: THE PETROSTATE AND ITS  
AMBIGUOUS OIL AND GAS LEGISLATION**

*Luis E. Cuervo\**

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\*Luis Enrique Cuervo practices law in Houston, Texas as the partner heading Fowler, Rodriguez’s Latin American practice. Mr.Cuervo is a member of the Texas, Louisiana, and Colombian Bar Associations. He is a Fulbright scholar and a Tulane Law School graduate. Mr. Cuervo has been an adjunct professor of law at Tulane Law School, the University of Houston, and the University of Texas in Austin. He has served as an advisor to the Colombian Ministry of Justice and to OPEC.

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John Steinbeck tells us that, one day, Kino, a poor fisherman who lived in the brush houses and was a member of the race that had been beaten, starved, and robbed for nearly four hundred years, found a pearl as large as a seagull’s egg and as perfect as the moon; it was the greatest pearl in the world.<sup>1</sup>

Similarly, Venezuelans recently learned that they inhabit a land under which a figurative black pearl lies: the largest hydrocarbon reserves in the Western Hemisphere.<sup>2</sup> Some have

1. JOHN STEINBECK, *THE PEARL* 9, 19 (Penguin Books 1945).

2. See Michael Fox, *Venezuela Begins Process of Certifying Orinoco Reserves*, VENEZUELA ANALYSIS, Aug. 14, 2006, <http://www.venezuelanalysis.com/news/1884>. In 2007, Venezuela’s oil production was 2.6 million barrels per day; it exported nearly 1.9 million barrels per day, and held an estimated eighty-seven billion barrels in its proven reserves. U.S. Energy Info. Admin., *Venezuela Energy Profile*, [http://www.eia.doe.gov/country/country\\_energy\\_data.cfm?fips=VE](http://www.eia.doe.gov/country/country_energy_data.cfm?fips=VE) (last visited Apr. 10, 2010). Venezuela has the world’s seventh largest natural gas reserves calculated at 181 trillion cubic feet. U.S.

called Venezuela's black pearl the greatest in the world.<sup>3</sup> When Venezuela's extra heavy oil reserves are included, the country has the largest oil reserves in the world at an amount that would exceed 310 billion barrels.<sup>4</sup> Additionally, the largest market for the pearl is very close; for oil export purposes, Venezuela is located only five days away from the United States.<sup>5</sup> In 2006, it supplied 11% of U.S. petroleum imports and

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Energy Info. Admin., *World Proven Reserves of Oil and Natural Gas*, <http://www.eia.doe.gov/emeu/international/reserves.html> (last visited Apr. 10, 2010).

3. Stephen C. Webster, USGS Claims Venezuela Sits on Earth's Largest Oil Reserves, RADICALVIEWS.ORG, <http://www.radicalviews.org/index.php/analysis/economics/90-usgs-claims-venezuela-sits-on-earths-largest-oil-reserves.html> (last visited Apr. 10, 2010). According to the Venezuelan Minister of Mines and Petroleum, including production from the Orinoco Belt, Venezuela would have total proven reserves in the amount of 316 billion barrels, the largest in the world. *Presidente Chavez Anuncio Inversiones de Japon en su Pais por unos US\$33.500 Millones en Hidrocarburos*, PORTAFOLIO, (July 4, 2009), [http://www.portafolio.com.com/internacional/vecinos/2009-04-07/ARTICULO-WEB-NOTA\\_INTERIOR\\_PORTA-4954381.html](http://www.portafolio.com.com/internacional/vecinos/2009-04-07/ARTICULO-WEB-NOTA_INTERIOR_PORTA-4954381.html). The Orinoco Belt is an area as large as Massachusetts where the largest oil deposits in the world lie—calculated as 1.3 trillion barrels of oil in place and with 270 billion barrels of recoverable oil—as much as Saudi Arabia. See MANIK TALWANI, THE ORINOCO HEAVY OIL BELT IN VENEZUELA 2 (2002), available at [http://www.bakerinstitute.org/programs/energy-forum/publications/docs/Talwani\\_OrinocoHeavyOilBeltVenezuela.pdf/at\\_download/file](http://www.bakerinstitute.org/programs/energy-forum/publications/docs/Talwani_OrinocoHeavyOilBeltVenezuela.pdf/at_download/file). The United States Geological Survey concluded that “the largest extra-heavy oil accumulation is the Venezuelan Orinoco heavy-oil belt, which contains 90% of the world's extra-heavy oil when measured on an in-place basis.” Richard F. Meyer & Emil D. Attanasi, *Heavy Oil and Natural Bitumen – Strategic Petroleum Resources* (Aug. 2003), available at <http://pubs.usgs.gov/fs/fs070-03/fs070-03.html>. According to BP's statistics, Venezuela holds 7.9% of the world's proven oil reserves. See BP STATISTICAL REVIEW OF WORLD ENERGY 6 (2009), available at <http://www.usaee.org/usaee2009/submissions/presentations/Finley.pdf>.

4. U.S. GOV'T ACCOUNTABILITY OFFICE, ISSUES RELATED TO POTENTIAL REDUCTIONS IN VENEZUELAN OIL PRODUCTION 9 (2006), available at <http://www.gao.gov/new.items/d06668.pdf> [hereinafter ISSUES RELATED TO POTENTIAL REDUCTIONS IN VENEZUELAN OIL PRODUCTION]. In the 1920s, Venezuela was the second largest oil producer in the world after the United States. *Id.*

5. Joanne Shore & John Hackworth, *Energy Info. Admin., Impacts of the Venezuelan Crude Oil Production Loss*, [http://www.eia.doe.gov/pub/oil\\_gas/petroleum/feature\\_articles/2003/venezuelan/vzimpacts.htm](http://www.eia.doe.gov/pub/oil_gas/petroleum/feature_articles/2003/venezuelan/vzimpacts.htm) (last visited Apr. 10, 2010). The United States is the top importer of Venezuelan crude. See MARK SULLIVAN, CRS REPORT FOR CONGRESS, *VENEZUELA: POLITICAL CONDITIONS AND U.S. POLICY* 42 (2008), available at <http://fpc.state.gov/documents/organization/109526.pdf>. In 2006, the U.S. imported 1.42 million barrels per day from Venezuela, that number was reduced to 1.36 million barrels per day in 2007. By 2007, Venezuela was the fourth major provider of foreign oil to the United States, after Canada, México and Saudi Arabia. *Id.* at 42. Ensuring the continued

owned nine refineries in the United States that account for a refining capacity of 750,000 barrels per day.<sup>6</sup> The country owns *Petróleos de Venezuela S.A.* (PDVSA),<sup>7</sup> the fourth-largest oil company after Saudi Aramco, National Iran Oil Company, and Exxon Mobil.<sup>8</sup> Oil gives Venezuela a disproportionate level of international influence, leverage over global oil prices, and the “undue ability to impact U.S. security and economy.”<sup>9</sup> Such is Venezuela’s pearl and many are after it.<sup>10</sup>

Like Kino, Venezuelans must consider what to do with the great pearl, the risks associated with sudden wealth, and the proper people to benefit from it.<sup>11</sup> Some want to share it with the

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flow of Venezuelan oil exports is a key U.S. interest. *Id.* In 2007, Venezuela’s exports to the United States were of \$39.9 billion dollars, 96% of which accounted for oil products. *Id.* at 43.

6. Letter from Richard Lugar, Chairman of U.S. Senate Committee on Foreign Relations, to Condoleezza Rice, Secretary of State (July 20, 2006), *available at* [http://lugar.senate.gov/energy/venezuela/pdf/GAO\\_Letter\\_to\\_Rice.pdf](http://lugar.senate.gov/energy/venezuela/pdf/GAO_Letter_to_Rice.pdf). Venezuela directly owns five U.S. refineries and has partial ownership in another four located in the U.S. Virgin Islands and the United States. *Id.* Its refining activities in the United States are performed through CITGO, a wholly owned subsidiary of the state oil company, *Petróleos de Venezuela S.A.* (PDVSA). *Id.*

7. Petroleos de Venezuela, *Gobierno Bolivariano de Venezuela*, [http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid\\_temas=11](http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid_temas=11) (last visited Apr. 10, 2010).

8. *See Petroleum Intelligence Weekly Ranks World’s Top 50 Oil Companies* (2009), [http://www.energyintel.com/DocumentDetail.asp?document\\_id=245527](http://www.energyintel.com/DocumentDetail.asp?document_id=245527) (last visited Apr. 10, 2010).

9. Lugar, *supra* note 6. In the 2006 Government Accountability Office report, the United States had no contingencies to deal with a decision by the Venezuelan government to shut down CITGO’s refining operations in the United States and the potential higher gasoline prices that such a decision would cause. *Id.* The U.S. Government Accountability Office refers to Venezuela as a “key player in the future energy security of the United States and the world.” *See ISSUES RELATED TO POTENTIAL REDUCTIONS IN VENEZUELAN OIL PRODUCTION*, *supra* note 4, at 1.

10. On November 3, 2009, the Venezuelan Minister of Energy and Petroleum, Rafael Ramirez, referred to investment projects to boost its country’s production. *See* Congreso Mundial de Crudos Pesados (Mar. 11, 2009) *available at* <http://menpet.gob.ve/noticias.php?option=view&idNot=1477>. In doing so, he mentioned Russian, Chinese, and Vietnamese investments in the Junin blocks. *Id.*

11. Moises Naim, *The Venezuelan Story: Revisiting the Conventional Wisdom*, *Vcrisis*, Apr. 2001, <http://vcrisis.com/index.php?content=analysis/moises1001>. Kino’s neighbors talked about what they would do with the pearl. Steinbeck, *supra* note 1, at 43. One would “give it as a present to the Holy Father in Rome. Another said that he would buy Masses for the souls of his family for a thousand years. Another thought he

oil industry's "seven sisters," and others want to distribute it to Venezuela's poor.<sup>12</sup> Venezuelans continue to consider whether such wealth is theirs, should be shared with others, or is reserved for a few in power. Also, as with other countries dependent on petroleum revenue, it is unclear whether such income is a blessing or a curse for Venezuela.<sup>13</sup>

Venezuelan legislation is a model of what to avoid when structuring comprehensive and transparent oil and gas law. Instead of establishing clear guidelines that may be followed objectively, the system is ambiguous and full of loopholes and contradictions. After more than a century of oil and gas exploitation, Venezuela is still a poor country.<sup>14</sup> An analysis of its historical oil and gas legislation is useful to understand the struggle to control power—the eternal struggle between the haves and the have-nots.

At a time when the United States advances the notion of "nation-building,"<sup>15</sup> Venezuela is a country in need of a legal and political system that enables the best use of its extraordinary energy resources to benefit the majority of the population and a true improvement of its people's lives.

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might take the money and distribute it among the poor." *Id.*

12. "The Seven Sisters are Exxon, Mobil, Standard Oil of California, Gulf, Texaco, BP and Shell." Luis E. Cuervo, *OPEC From Myth to Reality*, 30 *HOUS. J. INT'L L.* 433, 464 n.112 (2008).

13. "Just as gold once tainted King Midas' life despite his expectations to the contrary, oil seemed to 'petrolize' the economy and polity of [countries such as Nigeria, Venezuela, Indonesia, and Algeria]." Terry Lynn Karl, *The Perils of the Petro-State: Reflections on the Paradox of Plenty*, 53 *J. INT'L AFFAIRS*, 31–32 (1999) (describing the "paradox of plenty" and the puzzle as to why oil-rich countries often end up in profound economic and political crisis). Juan Pablo Pérez Alfonso, a former Venezuelan Minister of Petroleum and founding father of OPEC, referred to oil as the "devil's excrement." Shawn E. Cantley, *Review: Black Gold or the Devil's Excrement? Hydrocarbons, Geopolitics and the Law in the Caspian Basin*, 54 *EUROPE-ASIA STUDIES* 477 (2002).

14. In 2005, 43.7% of Venezuelans lived below the poverty line. Mark Weisbrot, Luis Sandoval & David Rosnick, *Center for Economic and Policy Research, Poverty Rates in Venezuela: Getting the Numbers Right*, available at <http://www.rethinkvenezuela.com/downloads/ceprpov.htm> (last visited Apr. 10, 2010).

15. See, e.g. Jordan Walerstein, Comment, *Coping with Combat Claims: An Analysis of the Foreign Claims Act's Combat Exclusion*, 11 *CARDOZO J. CONFLICT RESOL.* 319, 351 (2009) ("As U.S. forces focus more on maintaining peace and nation-building . . .").

Ideas about public ownership of oil and gas reserves and the nature and purpose of national oil companies must be revisited and adjusted for 21st-century realities.

More than thirty years have passed since Venezuela's government celebrated assuming full state control of its oil and gas resources.<sup>16</sup> However, oil companies have profited from weak legal systems that create an appearance of state control while making only marginal progress in lifting Venezuela's population out of poverty.<sup>17</sup>

This article reviews the most important changes in Venezuela's oil and gas legislation since 1971. In the intervening four decades, internal politics and legal technicalities have changed, but the true sovereignty of the Venezuelan people over Venezuela's natural resources remains unfulfilled.

### I. WHO OWNS THE PEARL?

On August 21, 1975 Venezuela approved the Ley Orgánica que Reserva al Estado la Industria y el Comercio de los Hidrocarburos [Organic Law<sup>18</sup> Reserving the Oil and Gas Industry for the State] (1975 Reserving Law).<sup>19</sup> The law was

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16. Carlos Andrés Pérez, *Discurso con Motivo de la Ley de Nacionalización del Petróleo* (Aug. 29, 1975), available at [http://www.analitica.com/bitbli/cap/nacionalizacion\\_petroleo.asp](http://www.analitica.com/bitbli/cap/nacionalizacion_petroleo.asp) [hereinafter *President Pérez on 1975 Oil Nationalization*].

17. Many Venezuelans believe their country is the richest in the world, but as much as 85% of them feel cheated out of the benefits of the oil boom. See INT'L REPUBLICAN INST., VENEZUELA'S 1998 PRESIDENTIAL, LEGISLATIVE AND GUBERNATORIAL ELECTIONS, ELECTION OBSERVATION REPORT 9 (1998), available at <http://www.cartercenter.org/documents/1151.pdf>.

18. Under Venezuelan law, "organic laws" hold more weight than ordinary laws and are approved by a two-thirds vote of the National Assembly. Antonio Ramirez, *An Introduction to Venezuelan Governmental Institutions and Primary Legal Sources*, NYU LAW GLOBAL (May 2006), available at <http://www.nyulawglobal.org/globalex/venezuela.htm>. In the country's legal system, organic laws are placed just below constitutional provisions and above ordinary laws. See *id.* Organic laws establish basic principles to be regulated by other, narrower laws. *Id.* "Organic' laws are: 1) those enacted to organize public powers or developing constitutional rights, 2) those which serve as a normative framework for other laws, or 3) those identified as such by the constitution." *Id.*

19. Ley Orgánica que Reserva al Estado la Industria y el Comercio de los Hidrocarburos [Organic Law Reserving the Oil and Gas Industry for the State] [hereinafter 1975 Reserving Law]. This law is also known in Venezuela as "the nationalization law". *Id.*

designed to make ordinary Venezuelans the true owners of their petroleum resources.<sup>20</sup> Venezuelan President Carlos Andrés Pérez understood the challenges before him: the oil and gas industry was not managed by Venezuelan citizens, his state lacked the necessary efficiency to conduct petroleum operations, and “Venezuelan people had no sense of the required public spirit to assume the reins of the national petroleum industry.”<sup>21</sup>

On January 1, 1976, President Pérez, on behalf of the people of his country, celebrated the historic day in which Venezuela assumed full control of its valuable hydrocarbon resources.<sup>22</sup> The flag was raised and the national anthem was played. “The people of Venezuela decided to take control of their natural resources,” and national sovereignty was vindicated.<sup>23</sup> Pérez characterized the nationalization as an act of sovereignty—an act of “creative will.”<sup>24</sup> Pérez proclaimed a democratic and nationalistic revolution.<sup>25</sup> Venezuela’s oil was recognized as an efficient foreign policy tool and an instrument to build a new-world economic order.<sup>26</sup> Pérez declared the end of an economic order that allowed the exploitation of the natural resources of

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20. *President Pérez on 1975 Oil Nationalization*, *supra* note 16. In his inaugural speech, President Pérez promised to implement the Venezuelan people’s aspiration that petroleum be Venezuelan. *Id.* “*Vamos a realizar la vieja aspiración de nuestro pueblo de que el petróleo sea venezolano.*” LUIS JOSÉ SILVA LUONGO, NACIONALIZACIÓN PETROLERA CON MESURA Y ACIERTO (July 9, 2006), available at <http://c3ig.com/webFRBAgosto2006/Confytrabaj/LJSLMerida.pdf>.

21. *President Pérez on 1975 Oil Nationalization*, *supra* note 16 (“*No se trata solo de decisiones del Gobierno. Tampoco del proceso jurídico y práctico para el traspaso de la propiedad de la industria. Más allá nos espera la responsabilidad auténtica para la conducción eficiente de una industria que se mueve en parámetros no manejados jamás por venezolanos, con una estructura estatal que reconocemos ineficiente y pesada; y lamentablemente con escasa conciencia del espíritu público necesario y condicionante para asumir la conducción del destino petrolero nacional.*”).

22. *See id.*

23. *Id.*

24. *Id.* (“*Porque este acto de soberanía, que con unánime emoción realizamos los venezolanos, es también o debe ser un acto de voluntad creadora.*”).

25. *Id.* (“*No hemos copiado a nadie métodos o procedimientos para realizar nuestra revolución democrática y nacionalista.*”).

26. *Id.*

poor countries.<sup>27</sup> Like Kino, Venezuela seemed to be ready to rise out of poverty.

The main consequences of the 1975 Reserving Law were:

- All outstanding concession contracts were terminated.<sup>28</sup>
- The state was granted a monopoly of oil and gas operations—both upstream and downstream.<sup>29</sup>
- The formation of a National Oil Company was required.<sup>30</sup>
- The National Oil Company would own and manage all assets reverted to the state upon the termination of the existing concessions.<sup>31</sup> PDVSA was formed in compliance with the law.<sup>32</sup>

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27. *Id.* (“*El orden económico que hizo posible la explotación de los recursos naturales de los países pobres llega a su término.*”).

28. 1975 Reserving Law art. 5. At the same time, the Venezuelan government nationalized the iron industry, terminated all existing concessions in that industry, and transferred to itself all assets and companies owned by the concessionaires; the *Corporación Venezolana de Guayana* was formed to exploit iron in the country. See Carlos Andrés Pérez, *Discurso con Motivo de la Ley Nacionalización del Hierro*, available at [http://www.nuso.org/upload/articulos/164\\_1.pdf](http://www.nuso.org/upload/articulos/164_1.pdf) (last visited Apr. 10, 2010) [hereinafter *President Pérez on 1975 Iron Nationalization*].

29. *President Pérez on 1975 Iron Nationalization*, *supra* note 25. Taking these provisions seriously meant that in the future, the National Oil Company would be the sole upstream operator in a system that would resemble the Mexican Pemex regime. *Id.*

30. 1975 Reserving Law, arts. 5–6. The law required that the government form a state-owned company that would perform oil and gas operations. *Id.* art. 6. The law authorized this company to be formed as a corporation owned by a single shareholder, the Venezuelan State. *Id.* A National Oil and Gas Company under the name of *Corporación Venezolana del Petróleo* (CVP) had been created on April 19, 1960 during a previous administration. ROMÁN DUQUE CORREDOR, EVOLUCIÓN DEL DERECHO PETROLERO EN VENEZUELA, available at [http://www.ulpiano.org/ve/revistas/bases/artic/texto/RDPUB/23/rdpub\\_1985\\_23\\_87-91.pdf](http://www.ulpiano.org/ve/revistas/bases/artic/texto/RDPUB/23/rdpub_1985_23_87-91.pdf) (last visited Apr. 10, 2010). This state-owned company was formed to develop the areas that had boundaries with productive concessions. *Id.* at ¶8.2. CVP was controlled by the Ministry of Mines and Hydrocarbons. *Id.* PDVSA was formed on August 30, 1975 through Presidential Decree 1123 enforcing the provisions of article 6 of the 1975 Reserving Law. *Id.* PDVSA’s sole shareholder is the Republic of Venezuela. *Id.* at ¶8.13. PDVSA became the sole owner of *Corporación Venezolana del Petróleo* on September 2, 1975. See generally, Larry B. Pascal, *Developments in the Venezuelan Hydrocarbon Sector*, 15 L. & BUS. REV. AM. 531, 533 (2009).

31. See 1975 Reserving Law art. 6.

32. *Petroleos de Venezuela, S.A.*, Annular Report (Form 20-F), at 7 (Nov. 17, 2006),



- Expropriation of all assets owned by concessionaries was allowed through prior payment.<sup>33</sup>
- The law required compensation based on the asset's book value, but the 1961 constitution required only "fair compensation" ("*justa indemnización*"), raising questions as to the validity of this provision of the law.<sup>34</sup>
- The state obtained exclusive control of all oil and gas exports.<sup>35</sup>

Notwithstanding the above, the 1975 Reserving Law specifically allowed for "association contracts" with private companies.<sup>36</sup> Such contracts were only possible in special cases and if consistent with the national interest, as long as the state had controlling shares, and the contract included a limited term.<sup>37</sup> Therefore, while a monopoly was formally declared, in practice, the government could still enter into association contracts with private parties.<sup>38</sup>

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available at <http://www.pdvsa.com/interface.sp/database/fichero/free/2856/209.PDF>. Interestingly, the nationalization did not mean significant managerial changes or changes in personnel. *VENEZUELA-PDVSA E&P Background*, APS REV. OIL MARKET TRENDS, Dec. 13, 1999, <http://ww.allbusiness.com/mining/oil-gas-extraction-crude-petroleum-natural/355020-1.html>. Business was conducted as usual, following private company directives until 1997. See *PDVSA E&P background*, <http://www.allbusiness.com/mining/oil-gas-extraction-crude-petroleum-natural/355020-1.html> (last visited Apr. 10, 2010) (noting that "Exxon's culture" was preserved until 1997).

33. 1975 Reserving Law art. 15. Compensation was to be calculated by deducting depreciation from the asset's book value and then deducting further based on several variables. *Id.* Such compensation could be paid over a ten-year term or through public debt instruments. *Id.* art. 16.

34. Compare CONSTITUCIÓN DE LA REPÚBLICA DE VENEZUELA (1961), available at [pdba.georgetown.edu/constitutions/venezuela/venezuela.html](http://pdba.georgetown.edu/constitutions/venezuela/venezuela.html) [hereinafter 1961 CONST.] art. 101 (allowing for expropriation whenever ordered by a court of law, as long as it necessary for public policy, and only after fair compensation), with 1975 Reserving Law art. 15.

35. See 1975 Reserving Law art. 2.

36. *Id.* art. 5.

37. *Id.* Contracts with private parties additionally required congressional approval. *Id.*

38. *Id.* Article 5 was controversial. See John D. Martz, *Policy-Making and the Quest for Consensus: Nationalizing Venezuelan Petroleum*, 19 *J. OF INTERAMERICAN STUD. & WORLD AFF.* 483, 500 (1977).

Interestingly, while the government preached nationalization, the law provided that National Oil Company employees would not be regarded as state employees.<sup>39</sup> Thus, the state is the owner but does not assume full responsibility as employer.<sup>40</sup>

President Pérez spent significant time explaining the acts:

We Venezuelans hope that multinational companies and governments from the large industrialized countries do not view the nationalization of basic resources as hostile acts, but instead as the dynamic expression of a new world and expressions of the country's maturity which recovers what was until now only a theoretical right to manage its natural resources. Within the international legal order, Venezuela will nationalize iron and petroleum pursuant to pre-existing laws, without breaching the laws that insured the continued exploitation of said resources by multinational companies. We want you to understand us, and that the centers of world power, whether governments or board of directors of transnational corporations, or both, value our firm but respectful attitude totally adequate to the national interest.<sup>41</sup>

However, public speeches declaring the law give the false impression of drastic changes.<sup>42</sup> In reality, the law only accelerated the contractual terms agreed to under existing concession contracts, even with some advantages for the concessionaires.<sup>43</sup> Since the 1961 constitution, Venezuelans had

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39. 1975 Reserving Law art. 8.

40. *Id.* ("Los directivos, administradores, empleados y obreros de las empresas a que se refiere el artículo 6 de la presente ley, inclusive los de la Corporación Venezolana del Petróleo una vez convertida en sociedad mercantil, no serán considerados funcionarios o empleados públicos.").

41. *President Pérez on 1975 Oil Nationalization*, *supra* note 16.

42. *See infra* notes 53–59 and accompanying text.

43. *See Martz*, *supra* note 38 at 490 ("Provisions of the negotiations with the corporations provoked relatively little dissent. Compensation was set at \$84,720,930 for Orinoco Mining (U.S. Steel) and \$17,674,418 for Iron Mines (Bethlehem). Payment would take the form of ten-year promissory notes carrying 7% interest. In addition, a one-year contract called for company officials to continue work at the major installations, subject to Venezuelan authority. A smooth and uninterrupted transfer was to be assured through signature of a three-year contract for technical assistance.").

agreed to not grant new concession contracts.<sup>44</sup> Further, the 1961 constitution provided that the concessionaires would not be entitled to any compensation.<sup>45</sup> Thus, since 1971, through the approval of the 1971 Reversion Law, Venezuela was preparing itself for the termination of the existing concessions and the delivery of all their assets to the state.<sup>46</sup>

Article 106 of the 1961 constitution required the adequate exploitation of natural resources for the collective benefit of all Venezuelans.<sup>47</sup>

The 1975 Reserving Law, which appeared to favor indigenous interests and to be detrimental to the concessionaires, actually provided generous compensation to the latter.<sup>48</sup> Pursuant to article 103 of the 1961 constitution, the concessionaires were not entitled to any compensation at all, much less the charitable compensation they received.<sup>49</sup> Further, article 5 of the 1975 Reserving Law opened the door for the negotiation of new contracts with multinational companies.<sup>50</sup>

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44. 1961 CONST. art. 126. Oil concession contracts required legislative approval, could only be granted to Venezuela-based corporations, and had to include a provision submitting all disputes to the jurisdiction of the local courts pursuant to Venezuelan law. *Id.* arts. 126–27.

45. *Id.* art. 103 (“*Las tierras adquiridas con destino a la exploración o explotación de concesiones mineras, comprendidas las de hidrocarburos y demás minerales combustibles, pasarán en plena propiedad a la Nación, sin indemnización alguna, al extinguirse por cualquier causa la concesión respectiva.*”)

46. See *Ley sobre Bienes Afectos A Reversion En Las Concesiones De Hidrocarburos* [Law Concerning the Goods affected by Oil & Gas Concessions] available at <http://www.fundacionempresaspolarg.org/nosotros/educacional/economia/leyhidr.html#intro> (last visited Apr. 10, 2010) [hereinafter 1971 Reversion Law]. In 1971, the Venezuelan legislature enacted a law providing for the reversion of oil and gas assets to the State. *Id.* Under the 1971 Reversion Law, exploration and exploitation areas under concession were to revert to the state, along with all assets, without any compensation whatsoever at the termination of the concession. *Id.* The 1971 Reversion Law declared that these assets were a matter of public policy, and that concessionaires were required to properly maintain the assets that were to be returned to the State. *Id.*

47. 1961 CONST. art. 120. (“*El Estado atenderá a la defensa y conservación de los recursos naturales de su territorio, y la explotación de los mismos estará dirigida primordialmente al beneficio colectivo de los venezolanos.*”)

48. See *supra* note 40 and accompanying text (noting that two iron companies were compensated with more than \$100 million).

49. 1961 CONST. art. 106.

50. 1975 Reserving Law art. 5.

The state that had granted exploration and exploitation concession contracts unilaterally revoked the original terms of those contracts.<sup>51</sup> A crude oil price increase from \$3.71 per barrel in 1973 to \$10.53 per barrel<sup>52</sup> one year later, explains the state's motivation. The President could now claim he was defending the national sovereignty.<sup>53</sup> The companies' rights appeared to be terminated.<sup>54</sup> However, companies were granted a right of compensation, and contracts could still be executed with them.<sup>55</sup>

Several guiding principles of Venezuela's oil and gas regime have been elevated to constitutional status:

- No concession contracts could be executed without congressional approval—to be obtained through a joint session of Congress after the Executive had informed Congress of the relevant details.<sup>56</sup>
- Venezuelan courts had jurisdiction to adjudicate any controversies arising from public interest contracts.<sup>57</sup>
- The Venezuelan people were the true owners of the country's hydrocarbon resources.<sup>58</sup>

However, the 1961 constitution *already* provided that the state was to defend and preserve Venezuela's natural resources to benefit Venezuelan citizens.<sup>59</sup>

Thus, the script seemed clear: populist speeches to comfort the masses while maintaining the status quo in both industry

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51. *Id.* art. 5; 1971 Reversion Law.

52. *See* Luongo, *supra* note 19.

53. *See id.* (arguing that President Pérez's comments were intended to inspire nationalism).

54. 1971 Reversion Law.

55. *See supra* notes 35–43 and accompanying text.

56. 1961 CONST. art. 126.

57. *See id.* art. 127.

58. *Id.* art. 7. Although a specific constitutional provision declaring that hydrocarbon resources belong to the nation was lacking, article 7 of the 1961 constitution included a reference to this matter by regarding resources as part of the territory that is owned by the State. *Id.*

59. *Id.* art. 106 (“*El Estado atenderá a la defensa y conservación de los recursos naturales de su territorio, y la explotación de los mismos estará dirigida primordialmente al beneficio colectivo de los venezolanos.*”).

control and industry partnerships with multinational corporations. But could it really be called “nationalization”?

## II. *APERTURA PETROLERA*: THE SEVEN SISTERS ARE INVITED TO FIND THE PEARL

On December 29, 1989, PDVSA's shareholders approved a plan that would increase production levels to 3.5 million barrels per day through a forty-eight million dollar investment.<sup>60</sup> PDVSA hoped to diversify its business in gas, refining, petrochemical, carbon, and heavy crude projects.<sup>61</sup> To accomplish this, it understood that an “opening to the private sector both local and foreign”<sup>62</sup> was required. The *Apertura Petrolera* [Petroleum Opening]<sup>63</sup> was essentially a PDVSA plan that would accomplish the following objectives:

- (1) Increase hydrocarbon reserves through a selective foreign investment exploration program.<sup>64</sup>
- (2) Use modern technology to boost production from traditional exploitation areas.<sup>65</sup>
- (3) Develop the Orinoco Belt Reservoir.<sup>66</sup>

A Houston-based exhibition titled “Aladdin's Cave of Wonders” was conducted to promote the Petroleum Opening

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60. See Gastón Parra Luzardo, *Análisis de la actividad petrolera en el lapso 1994–1998* (Apr. 1999), available at [http://www.soberania.org/Articulos/articulo\\_289.htm](http://www.soberania.org/Articulos/articulo_289.htm) (last visited Apr. 10, 2010).

61. *Id.*

62. *Id.*

63. This Petroleum Opening enabled joint-ventures between PDVSA and several major oil and gas companies, each for an initial period of thirty-five years. See Talwani, *surpa* note 4, at 4. Four main E&P contracts were executed: Petrozuata (a PDVSA-Conoco joint venture encompassing a \$2.4 billion investment to recover 1.6 billion barrels of crude); Sincor (a PDVSA-Statoil-Totalfinaelf joint venture encompassing a \$4 billion investment to recover 2.6 billion barrels of crude); Hamaca (a PDVSA-Phillips-Texaco joint venture encompassing a \$4 billion investment to recover 2.1 billion barrels of crude); and Cerro Negro (a PDVSA-ExxonMobil joint venture encompassing a \$2 billion dollar investment to recover 1.5 billion barrels of crude). *Id.* at 19–22. To date, more than \$12 billion dollars have been invested in these projects. *Id.* at 22.

64. See Nehisser Betancourt, *La Apertura Petrolera*, available at <http://www.monografias.com/trabajos12/laappet/laappet.shtml>. (last visited Apr. 10, 2010).

65. *Id.*

66. *Id.*

investment rounds.<sup>67</sup> The opening was in line with International Monetary Fund and U.S. Treasury Department guidelines.<sup>68</sup> “[T]he central goal of the policy change was to increase Venezuela’s productive capacity through the rejuvenation of its existing fields, the development of its huge resources of extra-heavy crude oil, and the discovery of new fields of medium and light crude outside of the traditional producing regions.”<sup>69</sup>

Multinational companies were eager to exploit Venezuelan oil and gas resources and reached agreements with PDVSA’s officers and directors.<sup>70</sup> Such agreements enabled traditional multinational exploration and production (E&P) operators to grab a share of Venezuela’s resources and participate in activities theoretically reserved to the state.<sup>71</sup> During the early

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67. See Scott Pendleton, *US Firms See Venezuela’s Oil as Aladdin’s Cave of Wonders*, CHRISTIAN SCIENCE MONITOR (July 25, 1995) at 9.

68. Johan Gindin, *Venezuela’s and Canada’s Very Different Approaches to Oil*, VENEZUELA ANALYSIS, Dec. 14, 2006, <http://venezuelanalysis.com/analysis/2138>.

69. See Energy Information Administration, *Venezuela Offers Full Market Value to Encourage Foreign Investment in Oil*, available at <http://www.eia.doe.gov/emeu/finance/usi&to/upstream/venezuela.html> (last visited Apr. 10, 2010).

70. See Ministerio de Energía y Petróleo, *Plena Soberanía Petrolera: La política de Migración de los Convenios Operativos a Empresas Mixtas* (2006), available at <http://www.menpet.gob.ve/repositorio/imagenes/file/Documentos/varios/conveniosoperativos.pdf> (last visited Apr. 10, 2010) at 7. Three bidding rounds took place. *Id.* The first bidding round between 1992 and 1993 concluded with three operating agreements still in force by 2005 (Guarico Oriental with Teikoku; Monagas Sur with Harvest–Vinccler; and Pedernales with Perenco). *Id.* at 9–10. The second bidding round conducted between 1993 and 1995 resulted in eleven operating agreements still effective by 2005. *Id.* A third round, performed in 1997, concluded with the signature of seventeen operating agreements. *Id.* at 12. The contracts provided for twenty-year terms, included minimum investment obligations, and paid the operator with a fee based on production levels. *Id.* Notably, the contracts signed in each round were progressively more open to international arbitration: The first round of contracts provided for arbitration in Caracas under the Venezuelan Code of Civil Procedure; the second round provided for arbitration in Caracas pursuant to International Chamber of Commerce (ICC) rules; and the third round provided for arbitration in New York pursuant to ICC rules. *Id.* at 9–10, 12, 17. Recently, the Petroleum Minister concluded that these operating agreements were illegal and opposed to the national interest as they reduced taxes, required PDVSA to pay applicable royalties, withdrew some related conflicts from Venezuelan courts, and were opposed to the wording of the 1975 Reserving Law. *Id.* at 20–22.

71. 1971 Reversion Law.

1990s Venezuela was—especially in its hydrocarbon market—a “country ripe for foreign investment.”<sup>72</sup>

Then-PDVSA president, Luis Giusti, believed that the state’s role was to supply the resources and provide infrastructure, but not to act as operator. Rather than creating wealth, a state-run operation would have reduced it.<sup>73</sup> He believed wealth would be created by multinational companies.<sup>74</sup>

“Aladdin’s Cave of Wonders” was appropriately named. U.S. Energy Information Administration (EIA) projections originally contemplated 125,000 barrels per day;<sup>75</sup> however, in 1997, production was already at 260,000 barrels per day and was expected to grow to more than 500,000 barrels per day.<sup>76</sup> The EIA concluded that “these increases can be attributed to the state-owned oil company’s relative inexperience in managing smaller mature fields and its isolation from the recent technological advances in the industry that have made it possible to sustain (and some cases even increase) production from seemingly mature producing properties.”<sup>77</sup>

Although the law provided that the oil and gas industry was reserved to the state, this was an excellent time to invoke article 5 of the 1975 Reserving Law that allowed granting contracts to private parties.<sup>78</sup> The contractual models used to attract foreign investment were operating service agreements (*Convenios Operativos*), association agreements (*Convenios de Asociación*), and strategic associations (*Asociaciones Estratégicas*).<sup>79</sup>

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72. See Jay Martin, *Venezuela as an Opportunity for Investment in the Petroleum Industry*, 20 ENERGY L.J. 325, 328 (1999).

73. See PDVSA AND MINISTRY OF ENERGY AND PETROLEUM, *CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA* (Mar. 2006), available at <http://www.pdvsa.com/interface.sp/database/fichero/publicacion/1411/59.PDF> (last visited Apr. 10, 2010).

74. See *id.*

75. *Venezuela Offers Full Market Value to Encourage Foreign Investment in Oil*, *supra* note 69.

85 *Id.*

77. *Id.*

78. *CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA*, *supra* note 73, at 13.

79. *Recent Developments in Texas, United States, and International Energy Law*, 2 TEX. J. OIL GAS & ENERGY L. 211, 270 (2007). PDVSA executed four strategic associations for the production of extra heavy oil, and eight risk-profit sharing agreements in which PDVSA could have up to a 35% working interest. *Venezuela Offers*

The operating agreements were contracts between a PDVSA subsidiary and a private investor who would perform specific services.<sup>80</sup> These “service contracts” allegedly would not grant any entitlement to hydrocarbon resources, and services to be provided by the private investor were not within those activities reserved to the state.<sup>81</sup> The contracts provided for a twenty-year term for producing marginal fields, at an income tax rate of 34%,<sup>82</sup> and required PDVSA to pay the 30% royalty.<sup>83</sup> These contracts also provided for international arbitration.<sup>84</sup> These terms and conditions were in opposition to the provisions of the 1961 constitution.<sup>85</sup>

Venezuela’s Minister of Mines noted that these contracts impeded Venezuela’s sovereignty in four areas: royalty payments, income tax payments, applicability of local law, and local court jurisdiction.<sup>86</sup> Thus, although existing law required congressional approval of oil and gas E&P instruments and established a 16.66% royalty, some multinational companies executed special agreements—without going through the legislature—that provided only a 1% royalty.<sup>87</sup>

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*Full Market Value to Encourage Foreign Investment in Oil*, *supra* note 69.

80. CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA, *supra* note 73, at 9. PDVSA executed thirty-two operating agreements with twenty-two companies in three licensing rounds and a direct award to Chevron-Texaco of the Boscán field. *Id.* at 10.

81. These were the arguments raised to avoid congressional approval of the granting contracts. *See generally*, John D. Martz, *supra* note 38, at 499–502 (discussing the varying viewpoints of the political parties involved in drafting the 1975 Nationalization Law).

82. *See* CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA, *supra* note 73, at 9. The standard petroleum industry income tax rate was 50%. *Id.* at 27.

83. *Id.* at 33.

84. *Id.* at 31.

85. *See* Stacy Retner, *Venezuela: How a Hydrocarbons Law Crippled An Oil Giant*, 27 HASTINGS INT’L & COMP. L. REV. 351, 355 (2004) (comparing the historical monopoly PDVSA held over every aspect of oil extraction and production in Venezuela under the 1961 constitution with the rights granted to private investors to participate in joint ventures with PDVSA under the 1999 constitution and subsequent Hydrocarbons Law).

86. CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA, *supra* note 73, at 31.

87. Thomas J. Pate, *Evaluating Stabilization Clauses in Venezuela’s Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry*, 40 U. MIAMI INTER-AM. L. REV. 347, 372–73 (2009).



Can multinational companies that entered into those agreements complain years later that the rule of law was not strictly observed? Did they act with clean hands? Further, shouldn't what happened in Venezuela during the 1990s be investigated under the Foreign Corrupt Practices Act (FCPA)?<sup>88</sup>

On April 12, 2005, the Ministry of Energy and Petroleum (MEP) issued a Resolution<sup>89</sup> that required all existing operating agreements to be modified to strictly meet the terms and conditions of the Hydrocarbons Law.<sup>90</sup> This meant that, as provided by the Hydrocarbons Law, PDVSA should be in control.<sup>91</sup>

### III. THE BOLIVARIAN REVOLUTION

Hugo Chávez was elected president of Venezuela in 1998.<sup>92</sup> His campaign promises, ardently opposed by the two traditional parties,<sup>93</sup> included plans to revise the constitution, control PDVSA spending,<sup>94</sup> and fight corruption<sup>95</sup> and poverty.<sup>96</sup>

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88. The FCPA makes it illegal to promise to give anything of value to a foreign official to influence such foreign official's decision. Foreign Corrupt Practices Act, 15 U.S.C. § 78dd-2 (1998). At best, it is difficult to believe that multinational oil and gas companies were not behind the introduction of article 5 of the 1975 Reserving Law and, later, the negotiations with PDVSA to launch the Petroleum Opening. If the U.S. government were truly interested in enforcing the rule of law, this would be a worthwhile investigation for the Justice Department.

89. See CONVENIOS OPERATIVOS UNA PRIVATIZACIÓN DISFRAZADA, *supra* note 73, at 38.

90. *Id.*

91. U.S. Department of State, *Background Note: Venezuela*, Feb. 2010, <http://www.state.gov/r/pa/ei/bgn/35766.htm> [hereinafter *Background Note: Venezuela*].

92. DOUGLAS SCHOEN & MICHAEL ROWAN, *THE THREAT CLOSER TO HOME 2* (2009).

93. Chávez attacked congress as a failed institution controlled by the two traditional parties. See INT'L REPUBLICAN INST., *supra* note 17 at 17.

94. *Id.* at 1. Chávez was elected by a landslide with 54% of the votes and 16 more points than his immediate rival. *Id.* at 1, 21. Chávez was Venezuela's first president in forty years with no ties to traditional parties COPEI and Acción Democrática. Jennifer McCoy, *Chavez and the End of "Partyarchy" in Venezuela*, J. OF DEMOCRACY, 64, 64 (1999).

95. In 1992, Chávez led a military coup against then-President Carlos Andrés Pérez accusing his government of corruption, and opinion polls indicated that many Venezuelans supported the coup. *Id.* at 16. Chávez was imprisoned but later pardoned by president Rafael Caldera. *Id.*

96. Chávez states that during his childhood he was in close contact with poverty.

Chávez also suggested nationalizing foreign oil installations and suspending payments on Venezuela's international debt.<sup>97</sup> The vote that gave Chávez 56% of the electorate confirmed the popular support of his plans.<sup>98</sup> Chávez gained worldwide notoriety by presenting himself as a successor of Fidel Castro, through his anti-American speech<sup>99</sup> and alliances with leaders of countries like Iran and Russia.<sup>100</sup> Chávez has been called the "son of Fidel," a "Perón with Petroleum," and a "Tropical Mussolini."<sup>101</sup>

On December 15, 1999, Venezuelans enacted by referendum a new constitution (currently in effect)<sup>102</sup> in which they renamed their country "The Bolivarian Republic of Venezuela."<sup>103</sup> When proposed and approved in 1999, the new constitution was presented as honoring Simón Bolívar's dreams of a free and sovereign homeland, independent from any foreign power.<sup>104</sup> Bolívar's name is evoked as a symbol of national unity and the

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SCHOEN & ROWAN, *supra* note 92, at 20. "Yes, I saw the pain of poverty. My little brother was called Enso, he was a very beautiful child but he became ill. I remember him lying in a hammock. He was always smiling. But he died. There were no doctors, nothing. We buried him in a bag. He was one of those children who are swallowed by poverty." *Id.* at 21.

97. *Id.* at 17. At the same time Chávez vowed to respect all existing contracts with foreign oil companies. *Id.*

98. *Id.* at 15.

99. SCHOEN & ROWAN, *supra* note 92, at 133. At the United Nations, Chávez referred to U.S. President George W. Bush as the "devil" and a "genocidal maniac." *Id.* at 1, 5. In September 2008, Chávez expelled the U.S. Ambassador to Venezuela and withdrew the Venezuelan ambassador to the United States. CNN International, *Venezuela to expel U.S. ambassador*, <http://edition.cnn.com/2008/WORLD/americas/09/11/venezuela.us/index.html>, (last visited Apr. 10, 2010). Chávez's anti-Americanism is the critical unifier that draws his popular support and international connections. Ray Walser, *What to do about Hugo Chávez*, (Executive Summary Backgrounder 2243) at 4 (Feb. 19, 2009), available at [http://www.heritage.org/Research/LatinAmerica/upload/bg\\_2243.pdf](http://www.heritage.org/Research/LatinAmerica/upload/bg_2243.pdf) [hereinafter *What to do about Hugo Chávez*].

100. See SCHOEN & ROWAN, *supra* note 92, at 104, 154.

101. *What to do about Hugo Chávez*, *supra* note 99, at 4.

102. See SCHOEN & ROWAN, *supra* note 92, at 47. One hour after his swearing in ceremony, Chávez signed a decree ordering a referendum to convene a constitutional assembly to write the new constitution. See *id.*; see also *Chavez Pledges 'Socialism or Death' at Swearing in Ceremony*, FOXNEWS.COM, Jan. 10, 2007, <http://www.foxnews.com/story/0,2933,242780,00.html>.

103. CONSTITUCIÓN DE LA REPÚBLICA DE VENEZUELA, Nov. 16, 1999.

104. See *Id.* PMBL.

fight for liberty, justice, and the people's wellbeing.<sup>105</sup> Interestingly, the founding principles of the 1999 constitution follow the aspirations of the U.S. founding fathers; the 1999 constitution is based on the idea that all men are created equal and endowed by their creator to the rights of life, liberty, and the pursuit of happiness.<sup>106</sup>

"Sovereignty" is one of the favorite words of the Bolivarian Revolution and its constitution.<sup>107</sup> The constitution is enacted on behalf of the "sovereign people of Venezuela."<sup>108</sup> Sovereignty is recognized as a right inalienable to nations, and the Republic's full sovereignty is enforced in its entire territory, including its onshore and offshore subsoil.<sup>109</sup> One of the state's essential obligations is to preserve its sovereignty.<sup>110</sup> The constitution even makes the state responsible for promoting Venezuela's economic sovereignty.<sup>111</sup> This is the justification for requiring the state to own all PDVSA stock.<sup>112</sup>

Oil is obviously essential to Venezuela.<sup>113</sup> Article 12 of the 1999 constitution, one of the document's main provisions, declares that hydrocarbon resources are an asset of the public domain and owned by the Venezuelan Republic, while Article

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105. See *Exposición de Motivos de la Constitución de la República Bolivariana de Venezuela*.

106. See VENEZ. CONST. PMBL.; see also U.S. CONST.

107. VENEZ. CONST. arts. 1, 5; see also Kiraz Janicke, *Venezuela Celebrates 11 Years of Bolivarian Revolution*, VENEZUELAANALYSIS.COM, Feb. 3, 2010, <http://venezuelaanalysis.com/news/5199>.

108. See VENEZ. CONST. PMBL.

109. See *id.* arts. 1, 11.

110. *Id.* art. 15.

111. *Id.* art. 299. "*El Estado, conjuntamente con la iniciativa privada, promoverá el desarrollo armónico de la economía nacional con el fin de generar fuentes de trabajo, alto valor agregado nacional, elevar el nivel de vida de la población y fortalecer la soberanía económica del país.*" *Id.*

112. See *id.* art. 303.

113. See Cesar J. Alvarez & Stephanie Hanson, *Venezuela's oil based economy*, COUNCIL ON FOREIGN RELATIONS, Feb. 9, 2009, <http://www.cfr.org/publication/12089> (noting that "oil generates about 80 percent of the country's total export revenue, contributes about half of the central government's income, and is responsible for about one-third of the country's gross domestic product").

302 openly declares the strategic interest of the oil and gas industry.<sup>114</sup>

Historically, all of Latin America has had a love-hate relationship with the United States.<sup>115</sup> This is particularly true for Venezuela.<sup>116</sup> In terms of policy, it has meant that no clear standards have ever been drawn *vis a vis* foreign capital and investment.<sup>117</sup> Thus, contradictory provisions are abundant in the constitution. For example, public ownership of hydrocarbon resources and reservation for the state of the oil and gas industry<sup>118</sup> are proclaimed while at the same time other provisions prohibit monopolies and allow concessions.<sup>119</sup> Article 113 of the constitution, which provides the basis for antitrust law in Venezuela, specifically includes a provision allowing concessions to exploit state-owned resources.<sup>120</sup>

Congress is supposed to hold the monopoly of approving all contracts for the exploration and exploitation of hydrocarbon resources; however, the very same constitutional provision that grants this power introduces an exception by limiting it to those cases that are specified by law.<sup>121</sup>

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114. VENEZ. CONST. arts. 12, 302.

115. See CARLOS RANGEL, *THE LATIN AMERICANS: THEIR LOVE-HATE RELATIONSHIP WITH THE UNITED STATES* (Transaction Books 1977) (1987) (discussing historical traditions, social structures, religious ethics, and the other distortions associated with the Latin American myth of the hero).

116. See Simon Romero, *For Venezuela, as Distaste for U.S. Grows, So Does Trade*, N.Y. TIMES, Aug. 16, 2006 (discussing how even though Venezuelan hostility towards Washington is growing, trade between the two countries is surging).

117. See *2009 Investment Climate Statement – Venezuela*, U.S. Dep't of State (Feb. 2009) (observing the cooling of foreign investment in Venezuela). Corruption is also widespread, and Venezuela stands as one of the most corrupt countries in the world. *Id.*

118. See VENEZ. CONST. arts. 12, 302.

119. See *id.* art. 113.

120. *Id.* (“*Cuando se trate de explotación de recursos naturales de propiedad de la Nación o de la prestación de servicios de naturaleza pública con exclusividad o si ella, el Estado podrá otorgar concesiones por tiempo determinado, asegurando siempre la existencia de contraprestaciones o contrapartidas adecuadas al interés público.*”)

121. *Id.* The 1999 constitution provides that contracts involving the national interest require congressional approval. *Id.* art. 150. It also provides the legislature with the power to authorize the executive to enter into contracts of national interest. *Id.* art. 187.

Article 151 requires all public interest contracts to incorporate a local Venezuelan court jurisdiction provision.<sup>122</sup> However, the requirement is not as strict as it seems; contracts are exempt from this provision if it is “inconsistent with their nature.”<sup>123</sup>

A constitutional provision declares that PDVSA is wholly owned by the Venezuelan state as a matter of economic and political sovereignty.<sup>124</sup> However, the same provision allows foreign ownership of PDVSA subsidiaries and strategic associations.<sup>125</sup> Significantly, PDVSA does not produce oil and gas; all of the oil and gas is produced by its subsidiaries, which may be partially owned by private interests.<sup>126</sup> The contradictions are such that the National Oil Company, PDVSA, proclaims public policy and nationalization in Venezuela, while abroad, through subsidiaries like CITGO, it conducts business as a capitalist privately owned corporation.<sup>127</sup>

Three basic issues of petroleum policy are not clearly defined by the country's 1999 constitution. Interestingly, as noted previously, these were the three basic principles included under the 1961 constitution<sup>128</sup>:

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122. *See id.* art. 151.

123. *Id.* (“*En los contratos de interés público, si no fuere improcedente de acuerdo con la naturaleza de los mismos . . .*”).

124. *Id.* art. 303.

125. *See id.*

126. *See* Mommer Bernard, *Plena Soberanía Petrolera*, July 9, 2009, available at <http://www.pdvsa.com/interface.sp/database/fichero/free/5005/642.PDF>.

127. *See* PDVSA, *Petróleos de Venezuela*, [http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid\\_temas=29](http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid_temas=29) (discussing the PDVSA's promise to “serve and benefit the Venezuelan people, who deserve their share of the country's national wealth”); CITGO Petroleum Corp., Registration Statement (Form S-3), at 5 (May 7, 1996), available at <http://www.sec.gov/Archives/edgar/data/1011746/0000950129-96-000756.txt> (“CITGO Petroleum Corporation is a privately-held company engaged in the refining, marketing and transportation of petroleum products including gasoline, diesel fuel, jet fuel, petrochemicals, lubricants, asphalt and refined waxes. CITGO is a direct wholly-owned subsidiary of PDV America, Inc., a Delaware corporation (“PDV America”), and an indirect wholly-owned subsidiary of PDVSA.”).

128. *See* 1961 CONST.

- (1) the extent of the state's monopoly over the oil and gas industry;<sup>129</sup>
- (2) the requirement of congressional approval for oil and gas contracts;<sup>130</sup> and
- (3) the validity of arbitration provisions in those contracts.<sup>131</sup>

These ambiguities offer a broad spectrum for negotiation by the executive. To the extent that the law is not absolutely clear, deals may be structured, and such deals mean power and money.

#### IV. THE 2001 HYDROCARBON LAW

On November 2, 2001, Hugo Chávez issued decree 1510 enacting the new Organic Hydrocarbon Law (2001 Hydrocarbon Law).<sup>132</sup> Almost a year earlier, on November 13, 2000, the National Assembly had granted broad powers to the executive to issue decrees on almost any legal issue, which would have binding force as law.<sup>133</sup> The Ministry of Energy and Mines (MEM) prepared the draft of the bill with the following characteristics:

*A. The law originated in the executive branch, not in the legislative branch.*<sup>134</sup>

Instead of being discussed in congress, the 2001 Hydrocarbon Law, which is essentially the law in force today,<sup>135</sup>

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129. *Id.*

130. *Id.*

131. *Id.*

132. El Decreto No. 1510 [Presidential Decree No. 1510], La Gaceta Oficial No. 37.323 [Official Gazette No. 36.575] (Nov. 2, 2001) (Venez.) [hereinafter 2001 Hydrocarbon Law].

133. Ley que Autoriza al Presidente de la República para Dictar Decretos con Fuerza de Ley en las Materias que se Delegan [*Law Authorizing the President of the Republic to Issue Decrees with the Force of Law*], La Gaceta Oficial No. 37.076 [Official Gazette No. 37.076] (Nov. 13, 2000). Through this decree, congress granted broad legislative powers to the President on multiple matters, including authority to pass a law that would establish the hydrocarbon regime. *Id.*

134. 2001 Hydrocarbon Law.

135. See *Background Note: Venezuela*, supra note 91. In May 2006, Venezuela's legislature approved the Hydrocarbons Organic Law with essentially the same wording

was drafted by the president pursuant to a broad delegation of powers.<sup>136</sup> Thus, it is questionable whether this law is truly representative of the popular will.<sup>137</sup>

*B. The law was meant to universally apply.*

The new hydrocarbon law was meant to include all provisions that govern the entire spectrum of oil and gas activities in Venezuela.<sup>138</sup> The law applies to a broad range of upstream and downstream operations.<sup>139</sup> This universality principle extends the applicability of the organic hydrocarbon law provisions to all oil and gas service related works in Venezuela.<sup>140</sup> However, article 7 of the decree also provides that oil and gas activities also governed by any other laws, decrees, and resolutions that may be applicable.<sup>141</sup>

*C. The Venezuelan public owns Venezuela's oil and gas.*

Article 3 of the decree confirmed that all hydrocarbon resources within the territory of Venezuela belonged to the Venezuelan Republic.<sup>142</sup> This includes reservoirs in the territorial sea, the continental shelf, the exclusive economic zone, and within the country's international boundaries.<sup>143</sup> The law defined gas and petroleum reserves as public domain

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as the 2001 Hydrocarbon Law. Luis Enrique Cuervo, *Venezuela or the Short of Cash Legislator That Did Not Take himself Seriously*, FRC-LAW, Sept. 2009, at 3–4, available at <http://www.frc-law.com/files/Article%20Venezuela.pdf>.

136. See VENEZ. CONST. art. 236(8) (giving the President the power to create law). Some have criticized this for allowing the executive—not the legislative—branch to review and discuss these issues. See, e.g. *Interview with Juan Carlos Sosa: Oil is of the Nation, the Whole Society*, ANALÍTICA, Sept. 24, 2001, *English translation available at* <http://www.analitica.com/va/economia/opinion/3120564.asp>.

137. *Id.*

138. See 2001 Hydrocarbon Law art. 1.

139. *Id.* (providing that the law governs all matters related to the exploration, development, industrialization, transportation, storage, marketing, conservation including refined hydrocarbon products, and any works that these activities may require).

140. See *id.* (utilizing broad language to extend the decree to all matters related to hydrocarbons).

141. See *id.* art. 7.

142. See *id.* art. 3.

143. See *id.*

goods.<sup>144</sup> Public ownership of these reservoirs is absolute in the sense that they may not be lost by prescription nor affected by liens and seizures.<sup>145</sup>

*D. Oil and gas exploitation is a public policy concern.*

Article 4 confirms a well known legal principle applied in oil and gas law, the “public policy” principle, pursuant to which all business covered by this law (all hydrocarbon related activities) are considered to be part of the country’s public policy.<sup>146</sup> This means that expropriations or nationalizations may be ordered.<sup>147</sup> Article 5 determines the main purposes of the hydrocarbon industry in Venezuela: to promote national development and the common good, considering the defense and rational use of the resource as well as the protection of the environment.<sup>148</sup>

One of the consequences of the public policy principle is that servitudes, expropriations, and non-permanent occupation of goods may be requested when necessary for hydrocarbon activities.<sup>149</sup>

Several other consequences follow:

- Mandatory applicable law and jurisdiction clauses are deemed incorporated in to all oil-and-gas-related contracts.<sup>150</sup> Thus, the validity of choice-of-law provisions choosing anything other than Venezuelan law—as well as all arbitration clauses—would be in question.<sup>151</sup>

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144. *See id.*

145. *See id.* This would mean, for example, that a contract that grants title to reserves. *See id.*

146. *Id.* art. 4.

147. *Id.* art. 34–37.

148. *See id.* art. 5 (providing that “the people’s welfare” is the goal of any oil and gas related income).

149. *Id.* art. 34.

150. *See* VENEZ. CONST. art. 151, (stating that, in public interest contracts, “a clause shall be deemed included even if not expressed” and “shall be decided by the competent courts of the Republic”).

151. *See* Emily A. Witten, *Arbitration of Venezuelan Oil Contracts: A Losing Strategy?*, 4 TEX. J. OIL GAS & ENERGY L. 55, 62 (2009) (showing the reemergence of “Calvo clauses” that bind foreign investors to the host country’s laws with no possibility



- Controversies arising from oil and gas contracts are deemed to be matters of public policy, potentially challenging any provision as affecting the interests of the Venezuelan state.<sup>152</sup>
- Expropriation is possible when conducive to oil and gas operations.<sup>153</sup>
- The prices of oil and hydrocarbon derivatives are established by decree by the MEM.<sup>154</sup>
- Adequate compensation must be guaranteed as an essential condition of all oil and concession contracts granted by the state.<sup>155</sup>
- Local national authorities have the power to grant and revoke permits to companies doing business in the oil and gas industry.<sup>156</sup>

*E. Oil and gas activities are reserved to the state.*

The organic hydrocarbon law distinguishes between “primary” and “secondary” oil and gas activities.<sup>157</sup> Primary oil and gas activities are essentially upstream operations and include exploration, development, exploitation, transportation, and storage, and are all reserved to the Venezuelan state.<sup>158</sup> Primary oil and gas activities may only be conducted by the executive or by state-owned companies such as PDVSA.<sup>159</sup> However, the executive may grant its right to conduct primary oil and gas activities to private operators, reserving the ability to revoke that right whenever the operators do not perform their

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of redress in the foreigner's country).

152. See Brandon Marsh, *Preventing the Inevitable: The Benefits of Contractual Risk Engineering in Light of Venezuela's Recent Oil Field Nationalization*, 13 STAN. J.L. BUS. & FIN. 453, 475–76 (2008) (stating that Venezuelan courts may find oil concession contracts public interest contracts, which Article 151 of deems to be the exclusive jurisdiction of local courts, and which the constitution grants broad powers to strike down).

153. 2001 Hydrocarbon Law arts. 38–39.

154. *Id.* art. 8.

155. *Id.* art. 41.

156. *Id.* arts. 12, 17.

157. *Id.* arts. 9–10.

158. *Id.* art. 9.

159. *Id.* art. 22.

obligations.<sup>160</sup> Thus, it has been clear since 2001 that Hugo Chávez does not want to exclude multinational companies from Venezuela's upstream operations.<sup>161</sup>

*F. Greater power for the executive.*

One of the most controversial provisions of the law is article 24. Under this provision the executive may allow, by decree, private operators to perform upstream activities.<sup>162</sup> It may also revoke such rights by decree.<sup>163</sup> The fact that E&P contracts may be awarded and revoked by the executive branch cements the political nature—and related unpredictability—of E&P contracts in Venezuela. Allowing the government to control these decisions prevents a stable hydrocarbon legal regime and makes unilateral decisions possible in settings that should be controlled by contract.

Under the law, the government may insert clauses into agreements with private companies to change conditions in favor of the Venezuelan Republic. This mechanism allows increasing royalties and the amounts of technology transfer obligations clearly posing a threat to the stability of contracts.

“Secondary activities” are downstream operations related to refining and the sale of refined products.<sup>164</sup> These activities may be performed by private parties through a license from the MEM.<sup>165</sup> Notwithstanding the above, ownership of refineries in Venezuela is reserved to the state.<sup>166</sup>

Some of the main obligations of participants in the Venezuelan oil and gas industry include (1) applying industry

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160. *Id.* art. 24.

161. See B. Seth McNew, “Full Sovereignty Over Oil”: A Discussion of Venezuelan Oil Policy and Possible Consequences of Recent Changes, 14 *LAW & BUS. REV. AM.* 149, 152–56 (2008) (showing that multinational corporations were involved in Venezuela's upstream operations).

162. 2001 Hydrocarbon Law art. 24.

163. *Id.*

164. See *id.* arts. 10–17. Although the term “secondary activities” is never used, it follows that the articles after article 9, which enumerates the primary activities, are secondary. See *id.*

165. *Id.* art. 12.

166. *Id.* art. 10.

standards in safety and environmental protection, (2) providing information regarding operations to the government, and (3) allowing any surplus capacity to be used by others.

*G. International conventions and treaties can affect domestic law.*

Oil and gas treaties entered into by Venezuela will apply to the oil and gas business.<sup>167</sup> As a result, foreign investors must be aware not only of local laws, but also of the oil and gas treaties to which Venezuela is a party and the effect those treaties have on local laws.<sup>168</sup> For example, Venezuela has entered into several bilateral international cooperation agreements to sell crude oil.<sup>169</sup> Bilateral investment treaties and OPEC-related agreements may also be relevant.<sup>170</sup> Thus,

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167. *Id.* art. 6.

168. See generally Thomas J. Pate, *Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry*, 40 U. MIAMI INTER-AM. L. REV. 347 (2009) (showing how investors need to be wary of the interplay between treaties and local laws).

169. By 2000, Venezuela had already executed agreements to sell crude oil to Belize, Costa Rica, Dominican Republic, El Salvador, Guatemala, Haiti, Honduras, Nicaragua, and Panama. *Venezuela Offering Neighbors Oil Deal*, L.A. TIMES, Oct. 19, 2000, available at <http://www.articles.latimes.com/2000/oct/19/business/fi-38725>. An agreement was also executed between Venezuela and Cuba on October 30, 2000 pursuant to which Venezuela agreed to provide Cuba with 53,000 barrels of crude oil a day. *Cuba, Venezuela Sign Oil Deal*, ASSOCIATED PRESS, Oct. 30, 2000, available at <http://www.latinamericanstudies.org/venezuela/oil-deal.htm>.

170. Venezuela is a party to the 1996 Caracas, Inter-American Convention Against Corruption, which condemns the crime of transnational bribery; the 1979 Montevideo Inter-American Convention on General Rules of Private International Law; the 1979 Montevideo Inter-American Convention on Extraterritorial Validity of Foreign Judgments and Arbitral Awards; the 1975 Panama Inter-American Convention on International Commercial Arbitration; and the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Inter-American Convention Against Corruption, Mar. 29, 1996, O.A.S. available at <http://www.oas.org/juridico/english/Sigs/b-58.html>; Inter-American Convention on General Rules of Private International Law, May 8, 1979, O.A.S. T.S. 54, available at <http://www.oas.org/juridico/english/sigs/b-45.html>; Inter-American Convention on Extraterritorial Validity of Foreign Judgments and Arbitral Awards, May, 8, 1979, O.A.S. T.S. 51, available at <http://www.oas.org/juridico/english/sigs/b-41.html>; Inter-American Convention on International Commercial Arbitration, Jan. 30, 1975, O.A.S. 42, available at <http://www.oas.org/juridico/english/sigs/b-35.html>; Convention on the Recognition and

Chávez's meetings with leaders of China, Russia, and Iran may cause practical consequences.

*H. The MEM is the regulatory agency.*

Under the new law there was a power shift from PDVSA to the MEM. The MEM is the Venezuelan Governmental authority that issues all hydrocarbon related regulations, analyzes the market, and establishes applicable prices.<sup>171</sup> The MEM is the main authority on hydrocarbon related matters and has the power to supervise all petroleum operations, payment of taxes, and related accounting records.<sup>172</sup> The MEM determines the sizes and shapes of exploration and exploitation blocks, which by law are limited to one hundred square kilometers.<sup>173</sup> The MEM supervises state-owned entities, supervises production rates, and rules on potential reservoir unitization issues.<sup>174</sup>

The MEM also grants and revokes the necessary licenses and permits, and authorizes any assignment of the rights vested thereof.<sup>175</sup> The MEM authorizes the operation of companies doing business in the oil and gas industry, and it can impose penalties and order the suspension of operations.<sup>176</sup> Among other things, the MEM issues:

- permits for private companies to conduct refining activities,<sup>177</sup>
- licenses to supply, transport, or store hydrocarbon products,<sup>178</sup>
- prices for all oil and gas products,<sup>179</sup> and

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Enforcement of Arbitral Awards, New York, 1958, [http://www.uncitral.org/pdf/07-87406\\_Ebook\\_ALL.pdf](http://www.uncitral.org/pdf/07-87406_Ebook_ALL.pdf) (last visited Apr. 10, 2010). Notably, Venezuela is not a party to the U.N. Convention on Contracts for the International Sale of Goods. CISG Table of Contracting States, <http://www.cisg.law.pace.edu/cisg/countries/entries.html> (last visited Mar. 3, 2010).

171. 2001 Hydrocarbon Law art. 8.

172. *Id.*

173. *Id.*

174. *Id.* arts. 30, 37, 42.

175. *Id.* arts. 61, 63.

176. *Id.* arts. 9, 12, 22–4, 66–68. Fines or penalties may be for up to 50,000 tax units. *Id.* art. 66.

177. *Id.* art. 53.

178. *Id.* art. 61.

- permits related to the installations where oil hydrocarbons are produced.<sup>180</sup>

*I. A mixed bag in terms of access to foreign investment.*

Under the law, while refining in Venezuela is open to private interests, marketing is off limits. Refining, purification, and transformation of natural hydrocarbons, and the marketing of those substances and their products, are all considered industrial and commercial activities that may be performed by both the state and private parties.<sup>181</sup> Refined products should be oriented primarily to exports, but the MEM may require that a minimum percentage be sold in the Venezuelan market.<sup>182</sup> However, Only state-owned companies can armlet Venezuelan oil and gas—for both local demand and exports.<sup>183</sup> Private capital may be involved solely in the marketing of refined products.<sup>184</sup>

*J. The government “take” was substantially increased.*

Royalties, surface taxes, and consumption taxes combine to form the government’s “take.”<sup>185</sup> The law was criticized for raising the government take as a simple means of obtaining—through taxes—additional government revenue without any technical analysis of its effects upon the industry.<sup>186</sup> The law raised royalties to a flat 30%<sup>187</sup> and the executive may request payment of the royalty in cash (at market value) or in kind.<sup>188</sup>

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179. *Id.* art. 60.

180. *Id.* art. 11. A permit is required in order to build, amend, or destroy any installations or equipment dedicated to hydrocarbon products marketing in Venezuela. *Id.* art. 62.

181. *Id.* arts. 10, 50.

182. *Id.* arts. 10, 59.

183. *Id.* arts. 27, 56–57.

184. *Id.* art. 10.

185. *Id.* arts. 44, 48.

186. Sosa, *supra* note 136 (characterizing the government as treating the oil and gas industry like a “cash cow”).

187. 2001 Hydrocarbon Law art. 44.

188. *Id.* art. 45.

Article 48 establishes the oil and gas related taxes.<sup>189</sup> A rental fee of 100 tax units will be charged for every square kilometer.<sup>190</sup> This fee is meant to increase 5% per year.<sup>191</sup>

Furthermore, hydrocarbons produced and consumed in local operations are taxed at a 10% rate per cubic meter.<sup>192</sup> Each liter of oil or gas sold in the Venezuelan market is taxed 30–50% of the price paid by the final consumer.<sup>193</sup>

## V. FULL PERMANENT SOVEREIGNTY

Venezuela's oil and gas policy is based on the defense of its national sovereignty.<sup>194</sup> Hugo Chávez named his oil and gas policy "*Plena Soberanía Petrolera*" [Full Petroleum Sovereignty] and announced its basic elements on October 10, 2004 during his TV program *Aló Presidente*, which aired from the Puerto La Cruz refinery.<sup>195</sup> Such a petroleum policy confirms state ownership of all hydrocarbon resources in the country's subsoil, and re-grants control of oil and gas operations to the Venezuelan government.<sup>196</sup>

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189. *Id.* art. 48.

190. *Id.*

191. *Id.*

192. *Id.*

193. *Id.*

194. PDVSA, *True Nationalization* (2005), <http://www.pdvsa.com> (follow "Full Sovereignty" hyperlink; then follow "True Nationalization" hyperlink) (last visited Apr. 10, 2010) [hereinafter *True Nationalization*] (declaring that the defense of the national sovereignty is one of the pillars of the National Petroleum Policy of the Venezuelan government. *Id.*

195. Programa No. 207 Aló Presidente, Oct. 10, 2004, *transcript available at* [http://www.alopresidente.gob.ve/materia\\_alo/25/1266/?desc=Alo\\_Presidente\\_207.pdf](http://www.alopresidente.gob.ve/materia_alo/25/1266/?desc=Alo_Presidente_207.pdf). Representative Tarek William Saab who was present during the program, along with the Minister of Energy, PDVSA's president and the company's entire board, referred to Oct. 10, 2004 as the date in which Venezuela declared its new Petroleum Independence ("hoy cuando se relanza la nueva independencia petrolera venezolana"). *Id.* at 2, 5–6.

196. PDVSA, *Petroleos Venezuela* (2005), <http://www.pdvsa.com> (follow "About PDVSA" hyperlink; then follow "Petroleos de Venezuela" hyperlink) (last visited Apr. 10, 2010). Control of oil and gas operations encompasses (1) taxes applied to the industry and (2) actual operational control of all on-site work. *See True Nationalization, supra* note 196.

The Full Petroleum Sovereignty policy has the following cornerstones:

- (1) recovering management and benefits of the national oil company PDVSA for the state,<sup>197</sup>
- (2) enforcing royalty payments and effectively applying them to all oil and gas operators,<sup>198</sup>
- (3) allowing the state to recover control of the country's oil and gas policy,<sup>199</sup>
- (4) determining that the main purpose of Venezuela's oil is to provide food, health, and education to its people,<sup>200</sup> and
- (5) having local courts decide any disputes arising from Venezuelan based oil and gas contracts.<sup>201</sup>

Control of Venezuela's hydrocarbon resources does seem to involve true issues of sovereignty. Chávez was elected president of Venezuela through popular vote in a country the U.S. Department of State considers a democracy.<sup>202</sup> Chávez has won popular majority votes for president three times.<sup>203</sup> Therefore, foreign interference to oust Chávez from office would not only violate international law but would be contrary to the apparent will of the Venezuelan people.<sup>204</sup> Significantly, Chávez's rise to power was attributed to his accusations that a small elite class dominated congress and that PDVSA revenues had been

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197. Rafael Ramírez Carreno, Minister of Energy and Petroleum and PDVSA President, *Plena Soberanía Petrolera: Una política popular, nacional y revolucionaria* [Full Oil Sovereignty: A National, Popular and Revolutionary Policy], in *SERIE DISCURSOS* [SPEECH SERIES], Oct. 20, 2005, at 10.

198. *Id.* at 9.

199. Programa No. 207 Aló Presidente, *supra* note 197, at 16.

200. *Id.* at 33; *see also* 2001 Hydrocarbon Law art. 5.

201. *Id.* at 34 (stating that any controversy arising from the contract shall be decided by Venezuelan courts).

202. BUREAU OF DEMOCRACY, HUMAN RIGHTS & LABOR, U.S. DEP'T OF STATE, 2008 HUMAN RIGHTS REPORT: VENEZUELA (Feb. 25, 2009), <http://www.state.gov/g/drl/rls/hrrpt/2008/wha/119177.htm>.

203. Sullivan, *supra* note 5, at 2–3, 9.

204. *See* U.N. Charter art. 2, para. 4.

wasted.<sup>205</sup> He railed against corruption and the politicians who had squandered the country's oil wealth.<sup>206</sup>

Chávez described the recovery of PDVSA for its employees—and away from multinational interests—as the first phase of the reclamation of Venezuelan sovereignty.<sup>207</sup> According to Chávez, the individuals who were in control of PDVSA in 2002 used a strike by oil and gas employees as a means of deposing him from office.<sup>208</sup> Further, the country's Minister of Defense denounced CIA involvement in the 2002 PDVSA strike and attempted coup.<sup>209</sup> CIA officers were clearly aware that disgruntled Venezuelan officers were planning a coup to take advantage of strong opposition to Chávez from the private sector, the media, the Catholic Church, and opposing political parties.<sup>210</sup> The

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205. Sullivan, *supra* note 5, at 3.

206. *Id.*

207. Programa No. 207 Aló Presidente, *supra* note 197, at 9–10. For Chávez, although PDVSA was the National Oil and Gas Company, its officers and directors protected not the national interests but the interests of multinational companies when they sabotaged the company's infrastructure. *Id.* at 9.

208. The “Plan Colina” focused on attacking the PDVSA employees who were responsible for the strike and restoring PDVSA to the Venezuelan workers. *Id.* at 10. On December 2, 2002 an important group of then PDVSA employees and directors started a national strike. PDVSA, *The Sabotage Against the National Industry*, <http://www.pdvsa.com> (follow “About PDVSA” hyperlink; then follow “History” hyperlink; then follow “The Sabotage Against the National Industry” hyperlink) (last visited Apr. 10, 2010) [hereinafter *The Sabotage Against the National Industry*]. The Chávez government claims the following acts were performed by the individuals who, at the time, controlled PDVSA: suspending fuel supply to the Maiquetía Airport affecting all air carriage; suspending supply of fuel to the Carenero, Guatire and Catia La Mar plants; closing service stations in the States of Aragua, Guarico, Apure and Carabobo; suspending all activities in the Yagua, Barquisimeto, Guaraguao and Maturín plants; stopping M.V. Pilín León and twelve other tankers; reducing crude production by 68%; stopping refinery production at the El Palito, Puerto La Cruz and Paraguaná refineries. *Id.* The Minister of Energy and Petroleum stated that the 2002 coup was financed by PDVSA and that PDVSA officers at the time were involved. Ramírez Carreno, *supra* note 199, at 12. The strike caused losses of \$17,400 million. *Id.* at 13.

209. *García Carneiro: CIA Tuvo Papel Fundamental en Golpe de Estado de 2002*, EL UNIVERSAL, Apr. 12, 2009, [http://www.eluniversal.com/2009/04/12/pol\\_ava\\_garcia-carneiro:-cia\\_12A2289295.shtml](http://www.eluniversal.com/2009/04/12/pol_ava_garcia-carneiro:-cia_12A2289295.shtml).

210. A CIA document dated April 6, 2002 provided that in Venezuela “conditions were ripening for Coup Attempt” and stated: “Dissident military factions, including some disgruntled senior officers and a group of radical junior officers, are stepping up efforts to organize a coup against President Chávez, possibly as early as this month . . . To



paralysis of the oil and gas industry caused a 15.8% and 24.9% decline of Venezuela's gross domestic product for the last quarter of 2002 and the first quarter of 2003, respectively.<sup>211</sup> Chávez explained that, in 2002, PDVSA's officers and directors had transformed the national oil and gas company into a "state within the state"—a corporation that was serving the personal interests of those executives at the top instead of the interests of the country and the company.<sup>212</sup> In this sense, the 2002 strike and Chávez's subsequent actions raise legitimate questions:

- What is the purpose of a National Oil Company?
- Who benefits from its operations?
- Who controls the company?
- What is its contribution to the country and its economy?

On October 10, 2004, Chávez set royalties at 16.6% for multinational companies that had executed strategic association agreements and those then paying a 1% royalty.<sup>213</sup>

The policy of Full Petroleum Sovereignty has been described as a national, popular, and revolutionary policy.<sup>214</sup> One may disagree with the Venezuelan government and the manners of its current president; however, the idea that oil and gas resources should primarily benefit the people of Venezuela,

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provoke military action, the plotters may try to exploit unrest stemming from opposition demonstrations staled for later this month or ongoing strikes at the state-owned oil company PDVSA. White-collar oil workers began striking on Thursday . . . . Protracted strikes, particularly if they have the support of the blue-collar oil worker's union could trigger a confrontation . . . ." DCI Strategic Warning Committee, *Senior Executive Intelligence Brief* (Apr. 6, 2002).

211. *The Sabotage Against the National Industry*, *supra* note 210. The strike also prevented the company from selling crude oil and derivatives, resulting in a loss of \$14,430 million. *Id.*

212. *Id.*

213. Programa No. 207 Aló Presidente, *supra* note 197, at 14. Chávez argued that the Venezuelan 1943 Hydrocarbon law provided for a 16.6% royalty and that the Petroleum Opening improperly deviated from such royalty, establishing an exception for new projects against the specific wording of the 1943 law. *Id.* at 11–13.

214. Ramírez Carreno, *supra* note 199, at 8. Venezuelan Ministry of Mines and Petroleum, Rafael Ramírez, explained that this meant recovering control of oil and gas operations by the country, involving the people as a key player, and allowing that petroleum profits are enjoyed by the people of Venezuela. *Id.* at 9–10.

instead of a small elite or a few international companies, is similar to the idea of true sovereignty.

## VI. THE 2006 HYDROCARBON LAW

On May 16, 2006, Venezuela's federal legislature enacted yet another "*Ley Orgánica de Hidrocarburos*" [2006 Hydrocarbon Law].<sup>215</sup> This law is another example of the ambiguity with which the Venezuelan legislator deals with oil and gas issues. Instead of providing clear and comprehensive guidelines, the law is full of loopholes and opportunities for exceptions and exclusive regimes. The central message conveyed by the law is a power shift, meaning that multinational investors who previously dealt with PDVSA directors will now need to deal with officers from the MEP.<sup>216</sup>

### A. A "comprehensive legal regime" that is not so.

The 2006 Hydrocarbon Law is supposed to be the comprehensive legal regime for oil and gas operations in Venezuela.<sup>217</sup> Therefore, the law applies to any and all upstream and downstream activities in Venezuela.<sup>218</sup>

However, the law explicitly excludes all operations relating to gas hydrocarbons.<sup>219</sup> The Hydrocarbons Law applies to all crude petroleum operations and operations related to associated

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215. See *Ley Orgánica Hidrocarburos* [Organic Hydrocarbon Law] (May, 24 2006) [hereinafter 2006 Hydrocarbon Law].

216. See PDVSA, *La Nueva Política Petrolera*, <http://www.pdvsa.com> (follow "Acerca de PDVSA" hyperlink; then follow "Historia" hyperlink; then follow "La Nueva Política Petrolera" hyperlink) (last visited Apr. 10, 2010).

217. See 2006 Hydrocarbon Law art. 1.

218. Thomas J. Pate, *Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry*, 40 U. MIAMI INTER-AM. L. REV. 347, 367–77 (2009).

219. 2006 Hydrocarbon Law art. 2. Gas hydrocarbons are governed by a special law known as the Gas Hydrocarbons Law. See A. Lezcano & G. Rachadell de Delgado, *The Impact of the Organic Hydrocarbons Law on the Venezuelan Natural Gas Industry*, OIL, GAS & ENERGY LAW INTELLIGENCE, April 2008, at 3.

gas.<sup>220</sup> Non-associated gas activities fall under the special Gas Hydrocarbons Law.<sup>221</sup>

Further, oil and gas activities are also ruled by other laws, whether those laws were issued in the past or have yet to be issued.<sup>222</sup> Thus, not only does the regime fail to be truly universal, but also it clearly lacks stability.

The law allows operators to enter into those contracts provided under the Hydrocarbons Law or “any other applicable provisions.”<sup>223</sup> On its own, this provision renders meaningless the idea of a comprehensive law applicable to all hydrocarbon related contracts and operations. It is conducive to special treatment for some companies and deviates from the idea of a transparent legal regime that is universally applied. Thus, the “comprehensive regime” allows for exceptions in a significant portion of oil and gas operations.<sup>224</sup>

*B. Public ownership of hydrocarbon resources.*

Consistent with the provisions of the 1999 constitution, the 2006 Hydrocarbon Law confirms public ownership of all hydrocarbon resources.<sup>225</sup> These provisions declare that any hydrocarbon reserves existing within the boundaries of the Venezuelan Republic are owned by the state.<sup>226</sup> A basic consequence is to exclude private ownership of oil and gas reserves.<sup>227</sup> Through these provisions the Venezuelan state claims ownership of all hydrocarbon reserves found in the territorial sea, the exclusive economic zone, and the continental

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220. See 2006 Hydrocarbon Law art. 2.

221. See *id.*

222. *Id.* art. 7 (“*Las actividades señaladas en esta Ley están sujetas tanto a las disposiciones de la misma, como a las contenidas en otras leyes, decretos o resoluciones, dictadas o que se dicten, en todo cuanto les fuera aplicable.*”). This provision opens the door for any future legislation, lower decrees, or even resolutions affecting the oil and gas industry notwithstanding any of the provisions of the 2006 Hydrocarbon Law.

223. See *id.* art. 25.

224. See *id.*

225. *Id.* art. 3.

226. *Id.*

227. See *id.*

shelf.<sup>228</sup> A claim of ownership of resources located in the continental shelf, but beyond the limits of the exclusive economic zone is controversial and inconsistent with the U.N. Convention on the Law of the Sea.<sup>229</sup> The same provision makes a reference to “national boundaries” and could be used to reconcile the wording with provisions of the Law of the Sea Convention.<sup>230</sup>

Several consequences follow from the state’s ownership of oil and gas resources:

- The state is entitled to receive royalty payments for a third party’s exploitation of those resources.<sup>231</sup>
- The state has a right to rental and production bonuses.<sup>232</sup>
- The state has a right to determine and award exploration and exploitation areas.<sup>233</sup>

Venezuela needs a state-controlled entity that manages the hydrocarbon resources.<sup>234</sup> Pursuant to the Hydrocarbons Law, the MEP fills that role.<sup>235</sup>

Venezuela needs a national oil company. Amazingly, the 2006 Hydrocarbon Law does not mention the National Oil Company PDVSA even once.<sup>236</sup> The law does, however, give the executive power to create state-owned companies to perform oil and gas operations.<sup>237</sup> Further, the law refers to several state-owned companies.<sup>238</sup> It makes no sense whatsoever that PDVSA

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228. *See id.*

229. U.N. Convention on the Law of the Sea art. 76, Dec. 10, 1982, 1833 U.N.T.S. 396 (defining the seabed, ocean floor, and subsoil thereof beyond the limits of national jurisdiction as an area owned by all humanity and subject to international control).

230. *See* 2006 Hydrocarbon Law art. 3.

231. *See id.* art. 44. The law establishes a 30% royalty for the State. *Id.* The same provision introduces exceptions to the 30% royalty if the reservoir is located in the Orinoco Belt. *Id.*

232. *See id.* art. 48.

233. *See id.* art. 23 (limiting the areas to 100 square kilometers).

234. *See id.* art. 8.

235. *Id.*

236. *See generally* 2006 Hydrocarbon Law (refraining from the mention of PDVSA).

237. *See id.* art. 27.

238. *See id.* art. 29. “*Las empresas petroleras estatales se registrarán por esta ley y su reglamento, por sus propios estatutos . . .*” *Id.* (using the plural form).

is Venezuela's national oil company but the country's essential oil and gas law makes no reference at all to PDVSA, its entitlements, or its role.

Disputes arising from Venezuelan oil and gas operations must be submitted to Venezuelan courts.<sup>239</sup>

*C. The internal struggle to control Venezuela's pearl.*

By failing to mention PDVSA, the 2006 Hydrocarbon Law shifts power away from PDVSA and to the MEP.<sup>240</sup> The MEP is vested with the authority to establish and implement the hydrocarbon policy.<sup>241</sup> Exploration and production operations in Venezuela may only be conducted by the executive, either directly or through state-owned or -controlled companies.<sup>242</sup> Therefore, under the law, management of the country's hydrocarbons will no longer be a PDVSA responsibility, but will be controlled by the MEP.<sup>243</sup>

The law provides that national oil companies may be created through an executive decree.<sup>244</sup> PDVSA will no longer have direct authority to conduct E&P operations, requiring a specific executive decree that transfers operations to the national oil company.<sup>245</sup>

Under the law, the MEP may control state oil companies and their subsidiaries, both regarding their domestic Venezuelan and international operations.<sup>246</sup> Though the purpose of the law is to subject PDVSA and its subsidiaries to the MEP, the wording of the law provides a clear extraterritorial reach

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239. *See id.* art. 34(3)(b) (providing that local Venezuelan courts have jurisdiction to solve any disputes arising from any hydrocarbon operations).

240. *See id.* arts. 8, 12, 14.

241. *See* 2006 Hydrocarbon Law art. 8.

242. *Id.* art. 22.

243. *See id.* art. 8.

244. *Id.* art. 27.

245. *See id.* art. 24. Under this provision, the authorization to conduct operations may be revoked by the executive. *Id.* Thus, while foreign investors may enter into contracts with PDVSA, if they act as operators they would do so pursuant to a revocable license issued by the government. *Id.* This provision gives the executive great discretion and power to terminate operational licenses. *See id.*

246. *Id.* art. 30.

that could be used to affect international operations of any PDVSA subsidiary.<sup>247</sup>

The law was enacted with the mindset of a National Oil Company that was not responsive to the national interests.<sup>248</sup> Thus, no reference is made to PDVSA while several of the law's provisions contemplate the creation of new national oil companies.<sup>249</sup> These provisions reflect internal power struggles to control the country's hydrocarbon resources.<sup>250</sup>

From a strictly legal perspective, it makes no sense for the 1999 constitution to raise PDVSA to a constitutional level by including a provision that mentions the National Oil and Gas company,<sup>251</sup> and provides that it is exclusively owned by the state for reasons of economic and political sovereignty, while the Hydrocarbons Law does not even mention PDVSA and opens the door for creating other state companies and for private ownership of upstream activities.<sup>252</sup> The message is simple: multinational investors are still welcome as long as they

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247. *See id.* PDV America, CITGO, Hovensa (a joint venture with Hess Corporation) and Ruhr Oel GMBH (ROG), a German joint venture with BP, are some of the subsidiaries with international operations that would be under MEP control. *See id.*; *see also* CITGO, *PDVSA Profile*, <http://www.citgo.com/AboutCITGO/PDVSAprofile.jsp> (last visited Apr. 10, 2010); CITGO, *About Citgo*, <http://www.citgo.com/AboutCITGO/CompanyHistory.jsp> (last visited Apr. 10, 2010); Hovensa, *Who We Are*, <http://www.hovensa.com/who.html> (last visited Apr. 10, 2010).

248. *See* 2006 Hydrocarbon Law art. 27 (explaining that the law grants companies the legal structure that it deems convenient).

249. *See id.* arts. 27–30 (providing that the executive may create companies owned exclusively by the state and that the MEM shall inspect and supervise such companies).

250. *See* David J. Lynch, *Has Citgo Become a Political Tool for Hugo Chávez?*, Jan. 11, 2006, at A1, *available at* [http://www.usatoday.com/money/industries/energy/2006-01-11-citgo-cover-usat\\_x.htm](http://www.usatoday.com/money/industries/energy/2006-01-11-citgo-cover-usat_x.htm) (discussing the conflict between former Citgo executives and those appointed by Chávez to gain control of Venezuelan oil). This struggle has usually been regarded as a fight between politicians and technicians. *See id.* (noting that Chávez has used his influence to appoint his political allies as executives of Citgo). It is a power struggle between an elite that was in control of PDVSA and Venezuela's oil and the Chávez regime which represents non-elite interests. *Id.* The haves versus the have nots, Marxism at its best.

251. *See* VENEZ CONST. art. 303 (explaining that the State shall retain all shares of the organ created to manage the petroleum industry).

252. *See* 2006 Hydrocarbon Law arts. 27, 50, 53.

understand that they will have new local partners. Politics prevails over the rule of law.<sup>253</sup>

*D. A monopoly that is not such.*

Although the Chávez regime criticized the 1976 nationalization as a fake one<sup>254</sup> and Chávez promised to nationalize everything that was previously privatized, it must be clearly stated: there is no state monopoly of oil and gas activities in Venezuela.<sup>255</sup>

Unlike Mexico, where the constitution clearly provides for exclusively state-controlled upstream operations,<sup>256</sup> Venezuela artificially declared state-controlled operations while simultaneously providing for “mixed companies” that may perform upstream operations.<sup>257</sup> Thus, Venezuela welcomes multinational companies and the Hydrocarbons Law provides the guidelines for such foreign investments.<sup>258</sup>

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253. See *id.* art. 33 (noting that the law shall govern any joint venture companies).

254. See Charles H. Blake, *The Dynamics of Economic Integration in Venezuela and their Implications for the FTAA Process*, 15 L. & Bus. Rev. Am. 81, 95 – 96 (2009) (arguing that the Chávez presidency cannot be viewed separately from widespread criticism of corruption related to previous governments that had acted favorably toward privatization).

255. See 2006 Hydrocarbon Law art. 33.

256. *CONSTITUCIÓN POLÍTICA DE LOS ESTADOS UNIDOS MEXICANOS*, Feb. 5, 1917, as amended, art. 27.

257. See Elisabeth Eljuri & Victorino J. Tejera Perez, *21st-Century Transformation of the Venezuelan Oil Industry*, 26 J. ENERGY & NAT. RESOURCES L. 475, 478 (2008).

258. *But see id.* (opining that although the 2006 Hydrocarbon Law specified how multinational companies could get involved in upstream operations, the effect of the law was to “close[] [Venezuela’s] doors to foreign investors”). In this sense the legal regime established by the 2006 Hydrocarbon Law may be compared to Colombia’s 1974 regime that established association contracts in which any multinational company interested in performing Colombian oil and gas business was required to form a joint venture with Ecopetrol, the national oil company. See *Petroleum Mining and the U’wa Indian Community*, para. 8, <http://www1.american.edu/TED/colspill.htm> (last visited Apr. 10, 2010). When this regime existed no one considered that Colombia was a communist country. See Jonathan Hartlyn, *Producer Associations, the Political Regime, and Policy Processes in Contemporary Colombia*, 20 Latin Am. Research Rev. 111, 118–19 (1985) (explaining that during the presidency of Alfonso Lopez Michelsen (1974–1978), the communist Confederación Sindical de Trabajadores de Colombia was an independent faction that often protested government economic policies). The only difference would be that the multinational investment risk operator would be selected by the Ministry of

Under the law, foreign oil and gas investment contracts in Venezuela will have the following characteristics:

- A twenty-five year term that may be extended for fifteen more years.<sup>259</sup>
- Transfer of title to the state of all equipment and installations when the contract expires.<sup>260</sup>
- Arbitration as a valid clause to be agreed by the parties.<sup>261</sup>

The law does not indicate that Venezuelan courts will have exclusive jurisdiction. Instead, it opens the door for valid arbitration clauses.<sup>262</sup>

#### VII. PRESIDENTIAL DECREE 5200 OF 2007: ENFORCING STATE OWNERSHIP

On February 26, 2007, Chávez issued a presidential decree ordering that existing Orinoco Belt Association Contracts and Production Sharing Agreements be adjusted to abide by applicable oil and gas laws.<sup>263</sup> Pursuant to the decree, such contracts would be replaced by joint ventures<sup>264</sup> in which PDVSA or any of its subsidiaries would have at least a 60% ownership.<sup>265</sup> Private companies with interests in these

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Mines in Venezuela as opposed to directly by the National Oil Company joint venturer. Compare 2006 Hydrocarbon Law art. 33, with Luis Enrique Cuervo, *Colombia 2025—Heaven or Hell?*, 77 TUL. L. REV. 1033, 1043 (2003) (noting that, under Colombian law, “[t]he multinational company is usually allowed to act as the operator”).

259. See 2006 Hydrocarbon Law art. 34.1.

260. *Id.* art. 34.3(a).

261. See 2006 Hydrocarbon Law art. 34(3)(b). Interestingly, article 34(3)(b) of the 2006 Hydrocarbon Law does not prohibit arbitration clauses. The law only provides that the validity of the arbitration provision will be determined by a local Venezuelan court. *Id.* If arbitration was to be excluded the law could have clearly stated so providing that the sole jurisdiction to solve any disputes are the local courts. However, consistent with the Venezuelan tradition of establishing ambiguity, arbitration was not entirely excluded. See, e.g., Eduardo A. Wiesner, *ANCOM: A New Attitude Toward Foreign Investment?*, 24 U. MIAMI INTER-AM. L. REV. 435, 463 (1993) (discussing as ambiguous an arbitration provision for foreign investment).

262. See 2006 Hydrocarbon law art. 34(3)(b).

263. El Decreto No. 5200 [Presidential Decree No. 5200], La Gaceta Oficial No. 38.617 [Official Gazette No. 38.617] (Feb. 26, 2007) (Venez.).

264. *Id.*

265. See *id.* art. 2.



contracts had a four-month period to agree on the terms and conditions of their participation in the new joint ventures.<sup>266</sup> Anticipating the arbitration disputes that this measure would trigger, article 13 of the decree provided that any related disputes would be governed by Venezuelan law and be subject to the jurisdiction of Venezuelan courts.<sup>267</sup>

In June 2007, PDVSA signed new Orinoco joint venture agreements with BP, Statoil, Chevron, and Total.<sup>268</sup> ExxonMobil and ConocoPhillips did not reach an agreement and decided to leave Venezuela and commence arbitration proceedings.<sup>269</sup>

In 2009, the MEP declared at an OPEC meeting that twenty-seven multinational companies were working with Venezuela to exploit the Orinoco Belt resources.<sup>270</sup>

#### VIII. PRESIDENTIAL DECREE 5796 OF 2008: CREATING A MACROECONOMIC STABILIZATION FUND

On December 9, 1997, the Venezuelan Central Bank, the World Bank, and the Venezuelan Ministry of Finance organized a seminar<sup>271</sup> to discuss the creation of a Macroeconomic

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266. *See id.* art. 4.

267. *See id.* art. 13.

268. *See Sullivan, supra* note 5, at 4. One month earlier, similar agreements had been reached with PetroCanada, ENI, and Opic. *See* Press Release, Eni, OPIC, and PetroCanada Abide by the Decree-Law for Oil Nationalization, Petroleos de Venezuela, S.A. (May 4, 2007), *available at* <http://www.pdvsa.com> (follow "Press Room" hyperlink; then follow "More News" hyperlink; select "May 2007") (last visited Apr. 10, 2010).

269. Sullivan, *supra* note 5, at 4. Venezuela has challenged jurisdiction in both cases *See Mobil Corp. v. Bolivarian Republic of Venezuela*, No. ARB/07/27 (ICSID) *available at* <http://icsid.worldbank.org> (follow "Cases" hyperlink; then follow "List of Cases" hyperlink; select "Pending Cases" hyperlink; scroll to Case No. 69) (last visited Apr. 10, 2010); *ConocoPhillips Co. v. Bolivarian Republic of Venezuela*, No. ARB/07/30 (ICSID), *available at* <http://icsid.worldbank.org> (follow "Cases" hyperlink; then follow "List of Cases" hyperlink; select "Pending Cases" hyperlink; scroll to Case No. 71) (last visited Apr. 10, 2010).

270. *See* Rafael Ramirez, Discurso pronunciado en el IV Seminario Internacional de la OPEP, March 18, 2009, *available at* <http://www.menpet.gob.ve/repositorio/imagenes/file/Documentos/discursos/Discurso-Ramirez-IV-seminario-OPEP.doc>.

271. BANCO CENTRAL DE VENEZUELA [CENTRAL BANK OF VENEZUELA], FONDOS DE ESTABILIZACIÓN MACROECONOMICA: SEMINARIO INTERNACIONAL [MACROECONOMIC STABILIZATION FUNDS: INTERNATIONAL SEMINAR] (Luis Rivera ed., 2001) [hereinafter INTERNATIONAL SEMINAR]. The seminar reviewed the examples of Colombia, which created a Petroleum Savings and Stabilization Fund in 1995 to adequately manage

Stabilization Fund.<sup>272</sup> The main idea was to establish a fund that would prevent volatility associated with international oil prices and fluctuating oil export revenues.<sup>273</sup> The fund would be created with oil export revenues and would provide stability to the economy during “rainy days.”<sup>274</sup> Participants at the event acknowledged Venezuela’s high dependence on oil revenues and described the country as a single commodity producer and exporter.<sup>275</sup> Oil revenues represent more than two-thirds of Venezuela’s state income over the last forty years.<sup>276</sup> This means drastic revenue losses when prices fall.<sup>277</sup> In order to limit the volatility associated with price fluctuation several options were considered: hedging,<sup>278</sup> implementing a policy to diversify the countries exports, and creating a stabilization fund.<sup>279</sup> Stabilization funds save money when high prices represent unexpected higher income for the purpose of spending it in the future when prices and revenues go down.<sup>280</sup> The Venezuelan

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revenues from the Cupiana, Cupiaga fields; the Norwegian Petroleum Fund; and Indonesia’s stabilizing macroeconomic measures. *See id.* at 13.

272. *Id.* Participants recalled that in 1974 Venezuela created an investment fund to capture the extra revenues from the oil boom. *Id.* at 20–21.

273. *See id.* at 21.

274. *See id.*

275. *Id.* at 18. Venezuela is described as an exporter of oil in the same way Chile is an exporter of copper and Colombia is an exporter of coffee. *Id.* at 17–18. The study suggests that these countries’ revenues depend on prices they do not control. *Id.* at 18.

276. *See id.* at 211 (showing trends from 1970 to 1997).

277. In 1986 Venezuela’s export revenue was reduced by \$5.7 billion or 44%. INTERNATIONAL SEMINAR, *supra* note 272, at 62. The country had a deficit of \$1.4 million. *Id.* at 97.

278. Hedging is described as a risk allocation process whereby through the use of future contracts, forwards and put calls, exporting countries shift to third parties the risk of price fluctuation. *Id.* at 19.

279. *See id.* at 249. One of the examples analyzed by Venezuela when debating the creation of the fund was the Norwegian Petroleum Fund. *Id.* at 214. It was the instrument created by the Norwegian government to manage oil revenue savings and as the tool to save through financial assets. *Id.* at 14. One additional goal of the Fund is to insure transparency in the use of oil revenues. *Id.* at 178. Amounts are saved in the Fund whenever the government has a surplus, and in 2001, the Fund was expected to have \$80 billion. *Id.* at 179. The Fund’s assets are invested in the international market, and the Fund—which is managed by the Norwegian Ministry of Finance and the Central Bank—acts as a financial investor. *Id.* at 193.

280. *See id.* at 179.

government has consistently increased its spending when oil revenues are high.<sup>281</sup> These discussions led to the creation of the *Fondo de Inversión para la Estabilización Económica* [Investment Fund for Economic Stability] through an executive decree in November 1998.<sup>282</sup>

The Fund's main goal was to stabilize the financial, currency exchange, and monetary policies in Venezuela.<sup>283</sup> Its assets would be obtained from two primary sources: payments made by the Republic of Venezuela, and revenues obtained by PDVSA—including oil and gas income tax, dividends, and income tax paid assessed on private companies for income in excess of the average revenue for the previous five years.<sup>284</sup> The Fund is managed by the Venezuelan Central Bank.<sup>285</sup> Article 6 of Decree 2991 required PDVSA to maintain hydrocarbon export revenues in the Fund and any extraordinary oil and gas related revenues.<sup>286</sup> Under the Fund's law, whenever oil revenues are down because of lower prices, the Fund would transfer resources to PDVSA.<sup>287</sup>

On May 20, 1999, the Chávez government introduced amendments to the Fund's law.<sup>288</sup> One of the changes introduced was the creation of a *Fondo Unico Social* [Social Fund] to which up to 40% of Investment Fund resources should be directed.<sup>289</sup> The law also established the previous five-year revenue average for comparing future oil revenues.<sup>290</sup> The

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281. See *infra* note 299 (noting the Venezuelan government's pattern of wasting oil revenues since 1974).

282. El Decreto No. 2991 [Presidential Decree No. 2991], La Gaceta Oficial No. 36.575 [Official Gazette No. 36.575] (Nov. 4, 1998) (Venez.).

283. See *id.* art. 1.

284. See *id.* arts. 3, 4.

285. *Id.* art. 2.

286. *Id.* art. 6. Under the Fund's law, these funds would still be the property of PDVSA and would be kept in a separate account. *Id.* arts. 6, 7.

287. See *id.* art. 11.

288. El Decreto No. 146 [Presidential Decree No. 146], La Gaceta Oficial No. 36.687 [Official Gazette No. 36.687] (May 20, 1999) (Venez.).

289. See *id.* arts. 9, 16.

290. See, e.g., *id.* art. 4(a)–(c). The income tax base from oil and gas activities was calculated at \$420 million, and the average income for oil and gas exploitation tax was calculated at \$967 million. *Id.* art. 24(a)–(b). Dividends to be paid by PDVSA were

amounts to be reimbursed by the Fund to PDVSA would be spent according to the instructions provided by the President.<sup>291</sup> Likewise, the President was given the power to decide what to do with additional oil revenues that exceeded the estimated revenues to be allocated to the Fund.<sup>292</sup> By 2003 the Fund had resources in the amount of \$700,000,000 while in the term between 1999 and 2003 its total asset flow was of \$7,180,000,000.<sup>293</sup> Thus, the President has extraordinary spending power to determine the destination of oil revenues.<sup>294</sup> This is particularly sensitive regarding PDVSA because the company's income should be at least partially oriented toward funding new exploration and development programs and to adequately maintaining existing wells.<sup>295</sup> These amendments introduced by the Chávez administration have been challenged because they provide the executive with excessive discretion through broad spending power without legislative control.<sup>296</sup>

The Fund's law has been amended several times since its creation.<sup>297</sup> On January 8, 2008, the government of Hugo Chávez issued Decree 5796 creating a Macroeconomic Stabilization Fund.<sup>298</sup> The decree was issued under special

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calculated at an average amount of \$1,254 million. *Id.* art. 24(c).

291. *Id.* art. 16(c). Thus, this provision gives the president of the country decision-making power over part of the national oil company's revenues. *Id.*

292. *Id.* art. 26.

293. Recursos del Fondo de Estabilización Macroeconómica, <http://www.bcv.org.ve/fiem/admifiem.htm> (last visited Apr. 10, 2010).

294. El Decreto No. 146 [Presidential Decree No. 146] art. 26. The power vested in the executive under Decree 146 of 1999 is such that he is granted the power to authorize the use of Fund's resources even before the minimum amounts have been reached. *Id.*

295. See Matthew Walter & Daniel Cancel, *Chavez's Oil Seizures May Cause 'Substantial' Output Decline*, BLOOMBERG.COM, May 9, 2009, <http://www.bloomberg.com/apps/news?pid=20601086&sid=aAfcnsWllc8> (explaining that PDVSA no longer has the capacity to undertake exploration and development because of Chávez's seizure of assets at oilfield service companies).

296. See *La Reforma del Fondo de Estabilización: Un Aumento de la Discrecionalidad del Gasto*, ANALÍTICA, <http://www.analitica.com/vam/1999.08/reportajes/02.htm> (last visited Apr. 10, 2010) (noting that Venezuelan governments since 1974 have wasted oil revenues and questioning the provisions that enable the executive to use PDVSA revenues indiscriminately).

297. See *Ley de Reforma Parcial del Decreto No. 1478 [Partrial Reform Act of Decree No. 1478]*, Oct. 11, 2002 (Venez.).

298. Decree 5796 of 2008 was published in the Official Gazette on January 9, 2009

powers that allow the executive to legislate with the force of law.<sup>299</sup> The Fund is under the authority of the Minister of Finance, and therefore under direct presidential powers and control.<sup>300</sup> The President appoints the Fund's board of directors, and the Fund is entirely dependent upon the executive to transfer resources to the Fund so it can maintain a level of "social expenses."<sup>301</sup>

The Fund's main purpose is to achieve fiscal macroeconomic stability considering that the state's expenses fluctuate with the price of oil.<sup>302</sup> However, the Fund's legislation lacks the necessary checks and balances to guarantee transparency and to avoid abuse of power by the executive.<sup>303</sup> The difference between revenues and expenses is determined by the Ministry of Finance rather than by an independent entity responsible for the country's monetary policy.<sup>304</sup> In other words, it is entirely discretionary for the executive to determine whether to save or to use additional revenues to increase "social spending."<sup>305</sup> In this sense, the very purpose of having a fund to ensure revenues in the future may be lost.

#### IX. AN OIL-BASED FOREIGN POLICY

The extraordinary wealth associated with oil sold at near \$150 a barrel in July 2008 allowed Hugo Chávez to use oil as a foreign policy tool.<sup>306</sup> Chávez has repeatedly threatened to cut

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under number 38,846. El Decreto No. 5796 [Presidential Decree No. 5796] (2009), available at <http://web.laoriental.com/leyes/L087n/L087nT0Cap1.htm> (last visited Apr. 10, 2010).

299. *Id.*

300. *See id.* art. 2.

301. *See id.* art. 9.

302. *See* Presidential Decree 5796.

303. *See id.* The executive is required to present to the National Assembly an annual report of the Fund's operations. *See id.* art. 2-3. The National Assembly's role is limited to approving or disapproving the report. *See id.* art. 7.

304. *See generally* Presidential Decree 5796 (The overseer of the Fund for Macroeconomic Stabilization, the Ministry of Finance, is responsible for carrying out the duties of the fund, including achieving stability in spending and in fluctuations of revenue).

305. *See id.* arts. 8-9.

306. James Leigh, *Crude Oil Price Retreat: Sunrise or a Lull Before the Storm?*,

oil exports to the United States.<sup>307</sup> He has used oil to form strong alliances with Bolivia, China, Cuba, Iran, Nicaragua, and Russia,<sup>308</sup> and to establish an integration model that opposes and challenges the U.S.-based and -promoted Free Trade Area of the Americas.<sup>309</sup> Members of the U.S. Congress have proposed that the government designate Venezuela as a state sponsor of terrorism because of the country's close relationships with FARC, Hamas, and Hezbollah.<sup>310</sup>

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ENERGY BULLETIN, Aug. 12, 2008, <http://www.energybulletin.net/node/46199>.

307. See *Venezuela Threatens to Cut US Oil*, BBC NEWS, Feb. 11, 2008, <http://news.bbc.co.uk/2/hi/americas/7238214.stm>. These verbal threats have never been accompanied by any relevant action. See *id.* Venezuela's crude oil is primarily refined in U.S. CITGO refineries, and the United States is Venezuela's prime customer. *Id.* Thus, not selling its crude oil to the United States would produce serious adverse economic consequences for the Venezuelan government. *Id.* In 2006 the Chairman of the U.S. Senate Committee on Foreign Relations, Richard Lugar, dismissed those threats as "unrealistic." See Lugar, *supra* note 6. But see SCHOEN & ROWAN, *supra* note 92, at 2 (quoting Otto Reich, the former U.S. ambassador to Venezuela as saying "America is very naïve about the threat Chávez poses. Today, Chávez is at least as dangerous as bin Laden; he's preparing his attack; he's even implementing the attack, but too many of America's leaders are still ignoring him. This could be a tragedy bigger than 9/11.").

308. See, e.g. *Putin Signs Energy Deals with Chavez on Venezuela Visit*, BBC News, Apr. 3, 2010, <http://news.bbc.co.uk/2/hi/8601388.stm> (stating that such an agreement was outside the view of the United States, so as to increase the Venezuela space and nuclear power industries in exchange for oil to Russia); Tyler Bridges, *Raul Castro's Visit with Chavez Shows Cuba's Need for Oil*, CHRISTIAN SCI. MONITOR, Dec. 15, 2008, <http://www.csmonitor.com/World/Americas/2008/1214/p07s01-woam.html> (describing how Cuban dependence on oil from Venezuela creates a close relationship between Chávez and Raul Castro); Warren Bull, *Venezuela Signs Chinese Oil Deal*, BBC NEWS, Sept. 25, 2008, <http://news.bbc.co.uk/2/hi/americas/7634871.stm> (describing how Chávez is using his vast oil reserves to forge alliances away from the influence of the United States, including the agreement with China); *Chavez, Ahmadinejad Claim Dominance over U.S.*, Associated Press, Nov. 19, 2007, available at <http://www.foxnews.com/story/0,2933,312161,00.html> (describing how the President of Iran has bonded with Chávez over their joint oil fund); Helen Popper, *Chavez Spreads His Oil Wealth in Bolivia*, REUTERS, May 27, 2006, <http://www.commondreams.org/headlines06/0527-04.htm> (describing Chávez's pledge of \$1.5 billion in energy investments, including oil, has created a close relationship with Bolivia); Tim Rogers, *Chavez Plays Oil Card in Nicaragua*, CHRISTIAN SCI. MONITOR, May 5, 2006, <http://www.csmonitor.com/2006/0505/p01s04-woam.html> (attributing the sale of oil on credit by Chávez to Nicaragua for the election of the like-minded Daniel Ortega as president).

309. See James Suggett, *Venezuelan Trade Declines with U.S., Increases with Brazil, Russia, China, Japan*, VENEZUELANALYSIS.COM, Aug. 21, 2009, <http://www.venezuelanalysis.com/news/4738>.

310. See H.R. Res. 1049, 110th Cong. (2008), available at <http://www.fas.org/>

The Chávez Administration promotes a foreign policy based on hostile relations with the United States, which Chávez calls “the empire,” while the United States remains Venezuela’s most important economic partner.<sup>311</sup> Venezuela profited from its 2008 \$51.4 billion dollar international trade with the United States,<sup>312</sup> however, the country’s foreign policy is inconsistent with its main trade alliances.<sup>313</sup>

Venezuela’s foreign policy is focused on regional integration and on reducing its economic dependence on the United States.<sup>314</sup> Such foreign policy is structured on four main pillars:

- (1) A new model for international integration, through the *Alianza Bolivariana de Nuestra America* [Bolivarian Alternative for the Americas] (ALBA);
- (2) Promoting the creation of a regional currency, the *Sucre*;<sup>315</sup>

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programs/ssp/asmp/documents/H.%20Res.%201049.pdf (considering the Venezuelan government’s ties to the Colombian guerrilla organization FARC and its close cooperation with Iran).

311. *See id.* at 4. However, the Chávez government has made efforts to divert more of Venezuela’s exports to countries like China and Vietnam. *Id.* at 7.

312. Office of the United States Trade Representative, Venezuela, <http://www.ustr.gov/countries-regions/americas/venezuela> (last visited Apr. 10, 2010). Top U.S. imports from Venezuela in 2008 were mineral fuel and crude oil (\$49 billion), iron and steel (\$584 million), aluminum (\$566 million) and organic chemicals (\$412 million). *Id.* Venezuela was the 8th-largest supplier of imports to the U.S. in 2008. *Id.* U.S. foreign direct investment in Venezuela was \$10 billion. *Id.*

313. David Schreiner, *Colombia and Venezuela: Tensions and Trade Relations*, COUNCIL OF THE AMERICAS, July 31, 2009, available at <http://www.as-coa.org/article.php?id=1826> (noting that Venezuela has been in constant tension with both Colombia and the United States, its top trading partners, over the past several years).

314. *Background Note: Venezuela*, *supra* note 91.

315. *Presidentes del ALBA Acuerdan Crear el Sucre como Moneda Unica*, MPRE, June 22, 2009, [http://www.mre.gob.ve/union/index.php?option=com\\_content&view=article&id=2047:presidentes-del-alba-acuerdan-crear-el-sucre-como-moneda-unica&catid=99:acta-fundacional&Itemid=64](http://www.mre.gob.ve/union/index.php?option=com_content&view=article&id=2047:presidentes-del-alba-acuerdan-crear-el-sucre-como-moneda-unica&catid=99:acta-fundacional&Itemid=64) (noting on June 22, 2009, the ALBA members agreed to establish the *Sucre* as a regional currency). Although the *Sucre* is not contemplated as a currency that will replace each country’s local currency, its purpose is to challenge the dollar as a common currency for international business transactions. *Id.* Initially the *Sucre* will be used virtually since 2010 to register trade exchanges between the ALBA members instead of the dollar. *Id.*

- (3) Venezuela's membership in the *Unión de Naciones Sur-Americanas* [Union of South American Nations] (UNASUR);<sup>316</sup> and
- (4) A regional Energy Cooperation Agreement (Petroamérica)<sup>317</sup>

This foreign policy is directly opposed to Venezuela's trade balance with the United States, which remains the most important source of revenue for the Venezuelan government.<sup>318</sup>

As an oil producer and exporter, Venezuela's role in OPEC is particularly relevant.<sup>319</sup> However, such role is at odds with its commercial relations with the United States and its regional Latin American integration model.<sup>320</sup>

Venezuela's foreign policy challenges U.S. world leadership, promotes the replacement of the dollar in energy transactions, establishes new international economic and financial institutions, uses energy as a geopolitical weapon, and increases Chinese and Iranian foreign investment.<sup>321</sup>

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316. See *Tratado Constitutivo de la Union de Naciones Suramericanas (UNASUR)*, MPRE, June 11, 2009, available at [http://www.mre.gob.ve/union/index.php?option=com\\_content&view=article&id=2023:tratado-constitutivo-de-la-union-de-nacionessuramericanas-unasur&catid=101:acta-fundacional&Itemid=66](http://www.mre.gob.ve/union/index.php?option=com_content&view=article&id=2023:tratado-constitutivo-de-la-union-de-nacionessuramericanas-unasur&catid=101:acta-fundacional&Itemid=66) (noting that the treaty establishing UNASUR aimed to promote integration between South American countries, the notion of a South American citizenship, create a South American Parliament, and to strengthen its member countries' independence and sovereignty). One of UNASUR's objectives is to achieve energy integration in the region. *Id.* UNASUR members include Argentina, Bolivia, Brasil, Chile, Colombia, Ecuador, Guyana, Paraguay, Perú, Suriname, Uruguay, and Venezuela. *Id.*

317. When referring to Petroamérica as an energy integration project Chávez has included North America. See PDVSA – Petróleos de Venezuela, *Petroamérica*, <http://www.pdvsa.com/> (follow “Unión energética” hyperlink; then follow “Petroamérica” hyperlink) (last visited Apr. 10, 2010) [hereinafter *Petroamérica*] (including the entire area between Alaska and Tierra del Fuego).

318. See *Background Note: Venezuela*, supra note 91.

319. See Matthew Robinson, *Analysis–Venezuela's OPEC Role Limited by Output, Politics*, REUTERS, May 26, 2004, available at [http://www.americasnet.net/news/Venezuela\\_OPEC.pdf](http://www.americasnet.net/news/Venezuela_OPEC.pdf).

320. See *id.*

321. See Ariel Cohen & Ray Walser, *The Russia-Venezuela Axis: Using Energy for Geopolitical Advantage*, THE HERITAGE FOUNDATION, July 21, 2008, at 1, available at <http://www.heritage.org/Research/Reports/2008/07/The-Russia-Venezuela-Axis-Using-Energy-for-Geopolitical-Advantage>; see also *What to do about Hugo Chávez*, supra note 113, at 15–18 (illustrating that China and Iran are the top foreign investors in



Thus, there is an inconsistency between the trade policy that economically sustains the Chávez regime, and a foreign policy that essentially alienates its rapport with its most important economic partner.<sup>322</sup>

#### X. ALBA<sup>323</sup>

In 2004, Venezuela promoted an integration of American countries that would constitute an alternative to the U.S. proposed Free Trade Area of the Americas (FTAA).<sup>324</sup> In a joint declaration, Cuba and Venezuela admitted that integration is necessary in an era of great blocs, but described the FTAA as the expression of neo-liberalism, an appetite for domination, and as exclusively focused on the interest for profit that perpetuates economic relations that favor certain countries to the detriment of others.<sup>325</sup> The ALBA confirms the importance of integration between American countries based on the principles of solidarity and social justice.<sup>326</sup> One of the main principles of ALBA is integrating energy of Latin American countries and promoting Latin American investment in the region to replace foreign investments.<sup>327</sup> Under ALBA, agriculture and its products are not conceived as merchandise but as a lifestyle that enables

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Venezuela).

322. See *Background Note: Venezuela*, supra note 91.

323. See *ALBA pasa a ser Alianza Bolivariana de los Pueblos de America*, VENEZOLANA DE TELEVISION, June 24, 2009, <http://www.vtv.gob.ve/noticias-nacionales/19957> (noting the Bolivarian Alternative for the Americas was renamed as the Bolivarian Alliance for the Americas on June 24, 2009). On that date, Ecuador, St. Vincent, and Antigua joined what was now perceived as an economic and political alliance. *Id.*

324. See *Declaración Conjunta [Joint Declaration]*, Venez.-Cuba, Dec. 14, 2004, available at <http://www.cuba.cu/gobierno/discursos/2004/esp/d141204e.html>. The first two members of ALBA were Venezuela and Cuba. *Id.* Today, ALBA has eleven members including Bolivia (which joined in 2006), Nicaragua (2007), Dominique (2008), Honduras (2008), Antigua (2009), Barbuda (2009), Ecuador (2009), the Granadines (2009), and St. Vincent (2009).

325. See *Declaración Conjunta*, supra note 326.

326. See Portal del ALBA, *Formación y Ampliación*, MPPRE, [http://www.mre.gob.ve/union/index.php?option=com\\_content&view=article&id=2042:formacion-y-ampliacion&catid=94:acta-fundacional&Itemid=59](http://www.mre.gob.ve/union/index.php?option=com_content&view=article&id=2042:formacion-y-ampliacion&catid=94:acta-fundacional&Itemid=59) (last visited Apr. 10, 2010).

327. See *Declaración Conjunta*, supra note 326.

preserving cultural values.<sup>328</sup> Bolivian President Evo Morales's proposal of a Commercial Treaty for the People,<sup>329</sup> if integrated into ALBA, would prioritize the people's benefits and introduce limits on foreign investment.<sup>330</sup>

The Venezuela energy-based integration proposal is known as Petroamérica<sup>331</sup> and includes three regional agreements: Petrosur<sup>332</sup> (an agreement between Argentina, Brazil, Venezuela, and Uruguay); Petroandina<sup>333</sup> (which includes Bolivia, Ecuador, Colombia, Perú, and Venezuela) and Petrocaribe (which is formed by fourteen Caribbean countries and Venezuela).<sup>334</sup>

Petroamérica's scope includes: supply of oil and oil products, infrastructure projects including the design and operation of refineries, joint marketing of crude and lubricants, joint oil and gas exploration and exploitation projects, and transportation

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328. See Portal del ALBA, *supra* note 328.

329. See La Propuesta Boliviana para un Comercio Justo entre los Pueblos, [http://www.boliviasoberana.org/blog/\\_archives/2006/4/13/1884087.html](http://www.boliviasoberana.org/blog/_archives/2006/4/13/1884087.html) (last visited Apr. 10, 2010) (noting Morales's declaration of the invalidity of a global economy in which a handful of nations establish the economic model for other countries, and that the economic models imposed by the World Bank have increased the gap between rich and poor countries).

330. See *id.*

331. See *Petroamérica*, *supra* note 317).

332. PETROSUR contemplates joint venture, cooperation, and integration agreements between Ancap (Uruguay), Enarsa (Argentina), PDVSA, and Petrobras (Brazil). See PDVSA – Petróleos de Venezuela, *Petroamérica*, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/readmenuprinc.tpl.html&newsid\\_temas=47](http://www.pdvsa.com/index.php?tpl=interface.sp/design/readmenuprinc.tpl.html&newsid_temas=47) (last visited Apr. 10, 2010). When launched, Petrosur's idea was to become the South American OPEC and the fifth largest oil and gas company in the world. See Raul Vasquez, *An OPEC for South America?*, NEW AMERICA MEDIA, Sept. 6, 2004, [http://news.ncmonline.com/news/view\\_article.html?article\\_id=9236d57cbfc02433d9e228245826048d](http://news.ncmonline.com/news/view_article.html?article_id=9236d57cbfc02433d9e228245826048d).

333. During a presidential meeting in 2005, Venezuela proposed the formation of Petroandina. See Petroandina, Petroleos de Venezuela, S.A., [http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid\\_obj\\_id=5006&newsid\\_temas=86](http://www.pdvsa.com/index.php?tpl=interface.en/design/readmenuprinc.tpl.html&newsid_obj_id=5006&newsid_temas=86) (last visited Apr. 10, 2010). Through the *Acta de Lima* [Lima Act], the presidents of the Andean countries—Bolivia, Colombia, Ecuador, Perú, and Venezuela—“took note” of Venezuela's initiative to create Petroandina as a vehicle to promote regional energy integration. See Acta Presidencial de Lima, Democracia, Desarrollo y Cohesión Social, XVI Consejo Presidencial Andino, July 18, 2005, available at <http://www.comunidadandina.org/documentos/actas/actalima.htm>.

334. See *Petroamérica*, *supra* note 333.

agreements.<sup>335</sup> Petroamérica contemplates joint ventures between Latin American National Oil Companies to perform joint investments and E&P operations and marketing.<sup>336</sup>

The Venezuelan government promoted the creation of Petrocaribe in 2005<sup>337</sup> as an international Caribbean Energy Cooperation Agreement,<sup>338</sup> primarily concerned with energy security and the construction of fair social structures<sup>339</sup> to combat poverty. Petrocaribe was established within ALBA.<sup>340</sup> Its creation was based on the basis of the principle of permanent sovereignty over natural resources and was created as the organization<sup>341</sup> that would dictate the energy plans and policies

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335. *Id.*

336. *Id.*

337. PDVSA – Petróleos de Venezuela, Petrocaribe, <http://www.pdvsa.com/> (follow “Unión energética” hyperlink; then follow “Petroamérica” hyperlink; then follow “Petrocaribe” hyperlink) (last visited Apr. 10, 2010) [hereinafter *Petrocaribe*].

338. The *Acuerdo de Cooperación Energética Petrocaribe* [Petrocaribe Energy Cooperation Agreement] was executed by Antigua & Barbados, Bahamas, Belize, Cuba, Dominica, Dominican Republic, Grenada, Guyana, Jamaica, St. Vincent & the Grenadines, St. Lucia, St. Kitts and Nevis, Suriname, and Venezuela. PDVSA – Petróleos de Venezuela, *Acuerdo de Cooperación Energética Petrocaribe*, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/biblioteca/readdoc.tpl.html&newsid\\_obj\\_id=1349&newsid\\_temas=111](http://www.pdvsa.com/index.php?tpl=interface.sp/design/biblioteca/readdoc.tpl.html&newsid_obj_id=1349&newsid_temas=111) (last visited Apr. 10, 2010) [hereinafter *Acuerdo de Cooperación Energética Petrocaribe*]. Several other countries have also joined. *See, e.g.* PDVSA – Petróleos de Venezuela, *Panamá Solicitó Ingreso a Petrocaribe*, Apr. 3, 2009, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid\\_obj\\_id=7293&newsid\\_temas=0](http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid_obj_id=7293&newsid_temas=0); PDVSA – Petróleos de Venezuela, *Declaración de Incorporación de la República de Guatemala al Acuerdo de Cooperación Energética de Petrocaribe*, July 13, 2008, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid\\_obj\\_id=6285&newsid\\_temas=0](http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid_obj_id=6285&newsid_temas=0); PDVSA – Petróleos de Venezuela, *Adhesión de Honduras*, Dec. 21, 2007, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid\\_obj\\_id=5070&newsid\\_temas=0](http://www.pdvsa.com/index.php?tpl=interface.sp/design/readsearch.tpl.html&newsid_obj_id=5070&newsid_temas=0).

339. *Petrocaribe*, *supra* note 339. The Energy Cooperation Agreement promotes the elimination of social inequities. *Id.*

340. *Acuerdo de Cooperación Energética Petrocaribe*, *supra* note 340.

341. Petrocaribe is essentially formed by a Ministerial Council integrated by the Energy and Petroleum Ministers of its member countries. PDVSA – Petróleos de Venezuela, *Estatutos*, <http://www.pdvsa.com/> (follow “Unión energética” hyperlink, then follow “Petroamérica” hyperlink, then follow “PetroCaribe” hyperlink, then follow “Estatutos” hyperlink) (last visited Apr. 10, 2010) [hereinafter *Estatutos*]. Its headquarters, pursuant to article 4 of its bylaws are located in Caracas, Venezuela. *Id.* art. 4. Petrocaribe has two main governing bodies, the Ministerial Council, which ordinarily meets once a year in Venezuela, and a Secretariat, which is part of the Venezuelan Ministry of Energy and Petroleum, as Venezuela is entirely responsible for

for its Caribbean region members.<sup>342</sup> Petrocaribe acknowledges the detrimental effects of high crude oil prices on the economies of small Caribbean oil-importing countries.<sup>343</sup> Among its goals is the promotion of energy conservation and efficient use.<sup>344</sup> Petrocaribe contemplates three basic instruments: an economic development fund, a PDVSA subsidiary to refine and supply oil and oil products to member countries, and financing mechanisms for countries purchases from Venezuela.<sup>345</sup>

The agreement created an economic and social fund (Fondo AlbaCaribe) through Venezuela's contribution of \$50 million, for the economic and social development of Caribbean countries.<sup>346</sup> A company known as PDV Caribe, a PDVSA subsidiary, was formed as an instrument to conduct refining, transportation, and distribution system operations to provide oil products to the Caribbean countries.<sup>347</sup>

Petrocaribe's main purpose is to coordinate the energy policies of its member countries and guarantee stable sources of

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all its costs. *Id.* art. 7, 10, & 14. Under its bylaws, Venezuela holds the organization's permanent presidency. *See id.* art. 10.

342. *See id.* art. 2.

343. *See* Acuerdo de Cooperación Energética Petrocaribe, *supra* note 340.

344. *Id.*

345. *See id.*

346. *Id.* Nine countries have benefitted from the fund: Antigua & Barbados, Belize, Cuba, Dominica, Grenada, Haiti, St. Kitts & Nevis, St. Vincent & the Grenadines, and Nicaragua. PDVSA – Petróleos de Venezuela, Fondo AlbaCaribe, <http://www.pdvsa.com> (follow “Union energética” hyperlink, then follow “Petroamérica” hyperlink, then follow “Petrocaribe” hyperlink, then follow “Fondo AlbaCaribe” hyperlink) (last visited Apr. 10, 2010).

347. *See* PDVSA – Petróleos de Venezuela, *PDV Caribe*, <http://www.pdvsa.com> (follow “Union energética” hyperlink, then follow “Petroamérica” hyperlink, then follow “Petrocaribe” hyperlink, then follow “PDV Caribe” hyperlink) (last visited Apr. 10, 2010). By 2007, PDV Caribe had entered into five mixed companies with its counter-parts of other member countries and had executed eleven oil supply contracts. PDVSA – Petróleos de Venezuela, *Declaración Política de Jefes de Estado y de Gobierno Petrocaribe*, [http://www.pdvsa.com/index.php?tpl=interface.sp/design/eventos/agenda\\_petrocaribe.tpl.html&newsid\\_obj\\_id=5024&newsid\\_temas=333](http://www.pdvsa.com/index.php?tpl=interface.sp/design/eventos/agenda_petrocaribe.tpl.html&newsid_obj_id=5024&newsid_temas=333) (last visited Apr. 10, 2010). PDV Caribe has invested \$552 million in projects such as the St. Vincent GLP plant, the storage and distribution plant in Dominica, and the Camilo Cienfuegos refinery in Cuba. PDVSA – Petróleos de Venezuela, *Petrocaribe: El Escudo Antimiseria*, June 11, 2009, <http://www.pdvsa.com> (input “el escudo antimiseria” into search field) [hereinafter *El Escudo Antimiseria*].

energy.<sup>348</sup> Its members reiterated their sovereign right to manage the rate at which they exploit their nonrenewable natural resources.<sup>349</sup> By providing oil and oil products to Caribbean importing countries, Venezuela attempts to form an international bloc to help advance its global interests.<sup>350</sup>

Petrocaribe reported the supply of fifty-nine million barrels of oil and oil products to its member countries during the first six months of 2008, financing the amount of \$2.007 million to the purchasing countries.<sup>351</sup> By 2009, Cuba received at least 178 million barrels of oil and oil related products and reactivated the Cienfuegos refinery.<sup>352</sup>

For Venezuela, Petrocaribe is clearly a foreign policy tool that improves its relations with its Caribbean neighbors toward a “multiple leadership” world and as an instrument of a broader strategic alliance.<sup>353</sup>

## XI. THE BOTTOM LINE

U.S. estimates show that PDVSA's oil production decreased between 2001 and 2005, dropping from 3.1 million barrels to 2.6 million barrels per day.<sup>354</sup> Such production decline is consistent with lower foreign investment in the same period, a reduction in the number of active drilling rigs, the PDVSA loss of managerial and technical personnel following the strike, and its inability to keep up with maintenance related investments.<sup>355</sup> The natural production decline of its fields, the lack of new E&P investment projects, potential lack of necessary technology to develop heavy oil fields, and the use of an important percentage of its revenues

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348. *Estatutos*, *supra* note 343.

349. *Id.*

350. See Acuerdo de Cooperación Energética Petrocaribe, *supra* note 340.

351. See *El Escudo Antimiseria*, *supra* note 349.

352. Prensa MPPRE, *Resultados Alcanzados por Misiones Sociales en Venezuela no tienen Precedentes*, Dec. 13, 2009, [http://www.mre.gov.ve/index.php?option=com\\_content&view=article&id=3048:resultados-alcanzados-por-misiones-sociales-en-venezuela-no-tienen-precedentes-&catid=127:12-2009-viii-cumbre-del-alba-lahabana&Itemid=264](http://www.mre.gov.ve/index.php?option=com_content&view=article&id=3048:resultados-alcanzados-por-misiones-sociales-en-venezuela-no-tienen-precedentes-&catid=127:12-2009-viii-cumbre-del-alba-lahabana&Itemid=264).

353. See *El Escudo Antimiseria*, *supra* note 349.

354. ISSUES RELATED TO POTENTIAL REDUCTIONS IN VENEZUELAN OIL PRODUCTION, *supra* note 4, at 14.

355. See *id.* at 15–17.

in social problems may create serious problems for the company that supplies the Venezuelan government with most of its revenues.<sup>356</sup> The economic realities that PDVSA may face could in turn question whether the country's foreign policy is consistent with the best interests of its national oil company and with a plan that creates greater revenue.<sup>357</sup>

Caracas is one of the most dangerous cities in the world.<sup>358</sup> Chávez's concentration of power and ties to terrorist groups invite questions as to his adherence to democratic values.<sup>359</sup> Some report that Venezuela has the highest rate of common crime and inflation in the Western Hemisphere and experiences extensive shortages of basic foods.<sup>360</sup> Further, corruption in Venezuela is described as "monumental."<sup>361</sup>

Despite huge oil revenues, the country's financial situation is described as "very poor," and the Central Bank estimates that Venezuela has negative reserves and that the PDVSA borrowed \$16 billion in 2007.<sup>362</sup>

More than a century of oil and gas exploration and exploitation activity in Venezuela justifies several questions:

- Who has really benefitted from oil and gas operations in Venezuela?

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356. *See id.* at 20–21.

357. *See id.* at 22.

358. *See Venezolanos Convertidos en "Policías" en Línea Ante la Creciente Inseguridad*, EL NACIONAL, Dec. 8, 2009, [http://www.el-nacional.com/www/site/p\\_contenido.php?q=nodo/112208/Tecnología/Venezolanos-convertidos-en-policías-en-línea-ante-la-creciente-inseguridad](http://www.el-nacional.com/www/site/p_contenido.php?q=nodo/112208/Tecnología/Venezolanos-convertidos-en-policías-en-línea-ante-la-creciente-inseguridad). Caracas has a murder rate of 100 persons per 100,000 compared to the world's average of nine persons per 100,000. *Id.*

359. *See* Ray Walser, *State Sponsors of Terrorism: Time to Add Venezuela to List*, HERITAGE FOUND., Jan. 20, 2010, <http://www.aipnews.com/talk/forums/thread-view.asp?tid=11791&posts=1>.

360. *See Venezuela: Looking Ahead: Before the Subcomm. on the Western Hemisphere of the Comm. on Foreign Affairs H.R.*, 110th Cong. 59 (2008) (statement of Norman A. Bailey, Adjunct Professor of Statecraft, the Institute of World Politics, President, Institute for Global Economic Growth), available at <http://foreignaffairs.house.gov/110/43520.pdf>.

361. *Id.* ("[B]illions of dollars hav[e] been stolen by government officials and their allies in the private sector over the past [nine] years.")

362. *Id.* at 59, 61 ("Production has been falling for years due to lack of investment and maintenance . . . PDVSA's management is so poor that the company is subject to dozens of lawsuits internationally for non-performance of supply contracts.")

- Are Venezuelans better off today after many decades of oil and gas production?
- What is the meaning—if there is one at all—to declaring that oil and gas resources are owned by the state?
- Does having a National Oil Company guarantee that the nation's population profits from the development of its hydrocarbon resources?
- The shareholders of multinational companies received the specific economic outcomes of E&P work conducted in Venezuela. Has that been the case for the shareholders of PDVSA?
- What should be the purposes of E&P exploration and exploitation contracts?
- Should the foreign investor's obligations vis-a-vis the host country be limited to payment of the government take, or should multinational companies share a vested interest in the improvement of the communities in which they operate?
- Is international arbitration contrary to the very notion of permanent sovereignty over national resources?
- May a multinational company that takes advantage of a controversial interpretation of a hydrocarbon law challenge a future different interpretation of the law that is against its interests?
- Is a multinational company's involvement in the process of drafting and approving hydrocarbon laws in foreign jurisdictions an area that should be investigated under FCPA provisions?

The most recent “nationalization” by the Venezuelan government enforces provisions that have been on the books since 1975, which provide the state has a monopoly of oil and gas activities and hydrocarbons under Venezuelan soil are owned by the Venezuelan state.<sup>363</sup>

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363. See Gregory Wilpert, *The Economics, Culture, and Politics of Oil in Venezuela*, Aug. 30, 2003, <http://www.venezuelanalysis.com/analysis/74>.

Multinational companies violate existing laws when they force their ways into a country, bribe top officers with political power, and obtain granting contracts. Those companies should be barred from complaining when years later someone in such country reminds everyone what the law said in the first place. Venezuela is an example that should be remembered by all those companies that now set their eyes on Mexico.

In 2007, according to the U.N. Development Program, Venezuela, along with China, was one of the top countries to improve its human development index.<sup>364</sup> This means—according to U.N. statistics—improved life expectancy, literacy, per capita gross domestic product, and school enrollment.<sup>365</sup> However, 57% of Venezuelans do not believe Chávez's policies are lifting the population out from poverty.<sup>366</sup> The real test for the Full Petroleum Sovereignty policies may be years from now, when we may look back to determine whether an average Venezuelan is, in fact, better off.<sup>367</sup>

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364. *China and Venezuela Big Gainers on Human Development Index*, EARTHTIMES, Oct. 5, 2009, <http://www.earthtimes.org/articles/show/288726,china-and-venezuela-big-gainers-on-human-development-index.html>. (noting that Venezuela was ranked 58th, up from 54th); see also U.N. DEV. PROGRAMME, HUMAN DEVELOPMENT REPORT 2009: VENEZUELA, [http://hdrstats.undp.org/en/countries/country\\_fact\\_sheets/cty\\_fs\\_VEN.html](http://hdrstats.undp.org/en/countries/country_fact_sheets/cty_fs_VEN.html). Venezuela has heavily invested in social programs reducing poverty rates from 49% to 37%, investing \$3.7 billion of its 2004 \$6.5 billion oil profits in social missions. Jonah Gindin, *Venezuela's and Canada's Very Different Approaches to Oil*, ALBERTA NEWS, Dec. 14, 2006, <http://www.venezuelanalysis.com/print/2138> ("This investment is building a society fundamentally inclusive of the [37%] of Venezuelans who live in poverty, and the much larger number who live within its shadow—the very people who have historically been the victims of a society designed to perpetuate the rights and privileges of a tiny minority." *Id.*

365. See *China and Venezuela Big Gainers on Human Development Index*, *supra* note 366.

366. Katuska Hernández, *Venezolanos Rechazan Intención de Transformar Propiedad Privada en Social*, EL NACIONAL, Oct. 14, 2009, [http://www.el-nacional.com/www/site/p\\_contenido.php?q=nodo/103790/Econom%EDa/57%-no-cree-que-Ch%E1vez-est%E9-acabando-con-la-pobreza](http://www.el-nacional.com/www/site/p_contenido.php?q=nodo/103790/Econom%EDa/57%-no-cree-que-Ch%E1vez-est%E9-acabando-con-la-pobreza).

367. The UN Department for Economic and Social Affairs has concluded that "[m]arkets are powerful mechanisms to promote economic development, but they often fail to produce the economic dynamism and the social justice that a sustainable economic development requires." U.N. Dept. for Econ. & Soc. Affairs [UNDESA], *State-Owned Enterprise Reform*, 6 (2007) (prepared by Ha-Joon Chang), [http://esa.un.org/techcoop/documents/PN\\_SOERreformNote.pdf](http://esa.un.org/techcoop/documents/PN_SOERreformNote.pdf). The study suggests that State Owned Enterprises work very well in countries like Singapore (Singapore Airlines), Brazil



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## VENEZUELA'S BLACK PEARL

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In the John Steinbeck story, Kino's son dies, and Kino is unable to remove himself from poverty, "[a]nd the music of the pearl drifted to a whisper and disappeared."<sup>368</sup>

Venezuelans may still have time to understand how to secure a better future for themselves and their posterity. Only time will tell whether their story resembles Kino's.

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(Embraer), and France (Renault) Norway, and Germany. *See id.* at 8–9.

368. STEINBECK, *supra* note 1, at 90.