

US SANCTIONS TARGET VENEZUELA'S PDVSA

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On August 24, 2017, US President Donald Trump issued Executive Order 13808 (the “Executive Order”), which imposes sanctions on the Government of Venezuela and all Venezuelan state-owned companies, including oil company Petroleos de Venezuela, S.A. (“PdVSA”). The sanctions are broadly designed to make it more difficult for the Government of Venezuela to raise funds internationally. Although the sanctions are limited in scope, parties wishing to deal directly or indirectly with the Government of Venezuela or PdVSA should exercise caution, as there are many nuances and uncertainties in the application of the sanctions.

SANCTIONS FRAMEWORK

US sanctions are traditionally “blocking sanctions,” requiring “US persons” to block transactions with prohibited individuals and entities, and seize any property belonging to such individuals and entities. For this purpose, US persons are individual US citizens or permanent residents, entities organized in the US and any other persons in the US. The sanctions imposed by the Executive Order are far more limited, and prohibit only certain types of transactions with prohibited persons. In this respect, the Venezuela sanctions are similar to the “sectoral sanctions” imposed under the Russia-Ukraine sanctions program.

NEW SANCTIONS

The Executive Order imposes the following new sanctions.

Prohibitions on debt and equity. The Executive Order prohibits US persons from providing financing or otherwise dealing in “new” debt of the Government of Venezuela or PdVSA if the debt has a term to maturity of greater than 90 days (for PdVSA) or 30 days (for the Government of Venezuela and all of its other state-owned components). The Executive Order also prohibits US persons from financing or otherwise dealing in new equity of the Government of Venezuela. Presumably, this prohibition applies to the acquisition of a minority interest in a state-owned company, since governments generally cannot issue equity. “New” debt or equity means debt or equity issued on or after August 25, 2017. By its terms, the Executive Order would apply to Citgo, the US oil company that is wholly owned by PdVSA (and therefore indirectly owned by the Government of Venezuela). However, in conjunction with the Executive Order, the US Department of the Treasury’s Office of Foreign Assets Control (“OFAC”) issued a general license permitting transactions with Citgo and its subsidiaries that would otherwise have been prohibited.

Prohibition on dealing in Government of Venezuela bonds. The Executive Order prohibits US persons from dealing in Government of Venezuela bonds issued prior to August 25, 2017. Bonds issued on or after August 25, 2017 are covered by the prohibition on “new debt” described above. In conjunction with the prohibition on trading in Government of Venezuela bonds, OFAC issued a general license permitting US persons to trade in a large number of specified Government of Venezuela bonds, vitiating the impact of the prohibition. Nevertheless, US persons wishing to trade in Government of Venezuela bonds issued prior to August 25, 2017 should ensure that the applicable bond CUSIP is listed in the general license.

Prohibition on dividends paid to Government of Venezuela. The Executive Order prohibits US persons from engaging in transactions related to making dividend payments to the Government of Venezuela (including to PdVSA) from any entity owned or controlled by the Government of Venezuela. This prohibition effectively prevents Citgo from making dividend payments to its parent, PdVSA. The prohibition only applies to companies controlled by the Government of Venezuela, so there is no prohibition on a company whose shares are held by the Government of Venezuela as portfolio stock paying dividends on the stock.

Prohibition on purchasing securities from Government of Venezuela. The Executive Order prohibits US persons from purchasing, directly or indirectly, securities from the Government of Venezuela (including PdVSA). This prohibition does not apply to purchases of Government of Venezuela debt or equity issued on or after August 25, 2017, nor does it apply to new debt or equity in subsidiaries of the Government of Venezuela, which are covered by the prohibitions above. Rather, this prohibition applies to the purchase of portfolio stock, bonds (e.g. US Treasury bonds) and other securities held by the Government of Venezuela.

COMMENTS AND OPEN QUESTIONS

US dollar transactions. The Executive Order prohibits “US persons” from engaging in transactions related to, and otherwise dealing in, new debt or new equity of PdVSA. On its face, this would imply that a non-US bank could make US dollar loans to PdVSA without committing a violation. However, almost all US dollar transactions are cleared through a US correspondent bank account, and any such US bank would arguably be transacting or dealing in the new debt. As a result, it is likely that the provision of US dollar financing to PdVSA by a non-US lender would still constitute a violation of the

sanctions. US correspondent banks may continue to clear non-prohibited US dollar payments made by or to PdVSA, such as ordinary course sales, but given the uncertainty regarding what constitutes a “financing” (as described below), US banks may be reluctant to enter into transactions with PdVSA. Indeed, news reports indicate that PdVSA is winding down its use of US dollars, and is selling oil in exchange for currencies other than the US dollar.

What is a financing? The Executive Order prohibits a US person from providing new financing to PdVSA with a term to maturity of greater than 90 days. Clearly the extension of a bank loan or other loan documented as such would constitute a financing. It is likely, although by no means certain, that other transactions commonly thought of as financings, such as finance leases, would be subject to the prohibitions on new debt.

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Less clear are trade receivables, i.e. deferred payment terms on goods or services provided by a US person to PdVSA. The US sanctions imposed on Russia in response to Russia's alleged intervention in Ukraine contain similar prohibitions. OFAC has issued a "Frequently Asked Question" in respect of the Russia/Ukraine sanctions making clear its position that trade receivables *are* financings subject to that sanctions regime. Pursuant to the Russia/Ukraine Frequently Asked Question, the term of trade receivables is tested by starting the clock at the time that title or ownership is transferred (in the case of a sale of goods) or the time that the final invoice is issued (in the case of services). Therefore, if these rules apply to the Venezuela sanctions, PdVSA's failure to pay a bill for services rendered by a US person within 90 days of the final invoice date would constitute a violation of the sanctions.

It is not clear why OFAC chose to issue this Frequently Asked Question interpreting the Russia/Ukraine sanctions but not the Venezuela sanctions, since the two sanctions regimes are virtually identical in this respect. One could argue that the same interpretation should apply. At the same time, OFAC has argued in the past that each sanctions regime is unique, and advice on one regime is not dispositive with respect to another.

What is a security? The Executive Order prohibits a US person from purchasing securities from PdVSA. Clearly the prohibition would apply to the direct sale between PdVSA and a US person, in an over-the-counter transaction, of portfolio stocks or bonds. It is unclear, however, how this rule operates with respect to stocks or bonds publicly traded on an exchange, where the US person may be unaware of its counterparty. Furthermore, the prohibition applies to the "indirect" sale of securities, which could mean that if PdVSA sells shares of stock to a non-US person, which sells those shares to a US person, the US person has violated sanctions. Arguably this should apply only when there was a prearranged plan to use the non-US person as a strawman, but there is no explicit "intent" requirement in the sanctions. Another unanswered question is whether options, swaps and other derivatives constitute "securities" for this purpose.

CONCLUSION

Given the substantial uncertainty in the application of the Venezuela sanctions, US persons and others with a significant US nexus should exercise caution in dealing with PdVSA and the Government of Venezuela.

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