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BRIEFING

TIGHTENING US SANCTIONS ON PDVSA WILL IMPACT SHIPPING

JANUARY 2019

"... THOSE WHO ELECT TO CONTINUE DEALING WITH PDVSA SHOULD DO SO WITH EXTREME CAUTION."

On January 28, 2019, US President Donald Trump issued an Executive Order dramatically ramping up sanctions on Petroleos de Venezuela, S.A. ("PdVSA"), the Venezuelan state-owned oil company. Unlike the 2017 sanctions targeting PdVSA, which were limited in scope, the latest sanctions designate PdVSA for "blocking sanctions," which effectively cuts it off from all direct and indirect US trade, and exposes non-US persons who continue to deal with it to the risk of "secondary sanctions." Subject to limited relief for winding down existing transactions, much of the international shipping community will be required to cut off trade with PdVSA, and those who elect to continue dealing with it should do so with extreme caution.

PdVSA: Specially Designated National

On January 28, 2019, President Trump designated PdVSA as a "specially designated national," or "SDN." An SDN is sometimes referred to as a "blocked person" or "sanctioned person." As a result of the designation, "US persons" (i.e., individual US citizens or permanent residents, entities organized in the US and any other persons in the US) will generally be prohibited from entering into transactions with PdVSA, subject to certain exceptions described below. Furthermore, US banks will generally be required to "block" all payments in US dollars made to or from PdVSA, effectively preventing it from using US dollars to make or receive payments.

In addition, the sanctions *may* target non-US persons who deal with PdVSA with additional sanctions. Pursuant to Executive Order 13850 (released in November 2018, but previously not covering PdVSA) blocking sanctions will also be imposed on any person found "to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services to or in support of" PdVSA. These sanctions are similar to the "secondary sanctions" targeting non-US persons who deal with Iran. The US Department of Treasury's Office of Foreign Assets Control, ("OFAC") is yet to release guidance regarding the application of these sanctions, including how they apply to non-US persons. It is possible that future OFAC guidance will provide comfort regarding the circumstances in which non-US persons can deal with PdVSA without running the risk of becoming subject to blocking sanctions. In the meantime, non-US persons engaging in significant transactions with PdVSA are at risk.

Licenses and Exceptions

OFAC has issued several general licenses, which the international community can rely on in winding down their transactions with PdVSA, subject to special rules described below regarding payments to it. Among the most relevant license exceptions are:

- The US oil company Citgo, which is owned by PdVSA, is broadly exempted from these sanctions until **July 27, 2019**; (Earlier sanctions which generally prohibited Citgo from making dividends up to its parent remain in effect)

- Parties are permitted to engage in transactions and activities ordinarily incident and necessary to the wind-down of operations, contracts or other agreements with PdVSA and its subsidiaries until **February 27, 2019**;

- US person employees and contractors of non-US entities are permitted to engage in transactions and activities ordinarily incident and necessary to the wind-down of operations, contracts or other agreements with PdVSA and its subsidiaries until **March 29, 2019**;

- Parties are permitted to engage in transactions and activities ordinarily incident and necessary to the purchase and importation into the United States of petroleum and petroleum products from PdVSA and its subsidiaries until **April 28, 2019**. This exception applies only to imports into the United States; the transportation of PdVSA oil from Venezuela to a third country would not be subject to this license; and

- Transactions and activities with Nynas AB (a subsidiary of PdVSA) and *its* subsidiaries are broadly permitted until **July 27, 2019**.

"THE NEW SANCTIONS WILL HAVE PROFOUND EFFECTS ON THE SHIPPING COMMUNITY'S INVOLVEMENT WITH PDVSA AND ITS SUBSIDIARIES."

Notwithstanding the foregoing, payments *from* a US person *to* PdVSA or its subsidiaries (including US dollar payments that are routed through the US financial system) generally must be placed into a blocked, interest-bearing account in a US bank. PdVSA will be unable to access this account until sanctions are lifted.

Banks are permitted to refuse (rather than block) payments to or from PdVSA or its subsidiaries until **March 29, 2019**, so long as the funds originate outside the US, and neither the originator nor the beneficiary is a US person. This may help non-US persons who do not yet realize the sanctions are in effect by avoiding the blocking of funds. Once the funds are blocked, they generally cannot be claimed by either the payer or the payee until sanctions are lifted.

Application to Shipping

The new sanctions will have profound effects on the shipping community's involvement with PdVSA and its subsidiaries. Among the most important consequences are:

- US-based shipping companies should begin winding down their operations with PdVSA, including the transportation of PdVSA crude oil and other petroleum products. Voyages made pursuant to charters in effect prior to January 28 can generally continue until February 27 (or April 28, if importing oil into the US) after which point they would be prohibited. Transactions with Nynas (including new transactions) can continue until July 27;
- No payments from a US person, and no payments in US dollars, can be made to PdVSA or its subsidiaries (excluding Nynas);*
- Non-US persons who wish to continue doing business with PdVSA past the applicable wind-down period will be subject to a risk of secondary sanctions; and
- Parties should carefully review the sanctions provisions of their charterparties, loan agreements and insurance clauses. A transaction that would not violate sanctions may still result in a breach of these agreements.

Conclusion

Previous US sanctions imposed roadblocks in dealing with PdVSA, but they still broadly permitted US persons to trade with it. The new sanctions cut off almost all such trade. US persons should take steps to discontinue their relationship with PdVSA and/or apply for specific licenses from OFAC to continue to work with PdVSA. Non-US persons wishing to continue a relationship with PdVSA should proceed with extreme caution. It is possible that future OFAC guidance will limit the scope of secondary sanctions that may apply, but unless and until that guidance is released, substantial risk remains.

*Updated February 13, 2019. An earlier version of this briefing said "including Nynas."

FOR MORE INFORMATION

Should you like to discuss any of the matters raised in this briefing, please speak with the author below or your regular contact at Watson Farley & Williams.

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Publication code number: 60956420v1