ENERGY AND NATURAL RESOURCES PRACTICE AREA

LEGA ABOGADOS

VENEZUELAN LEGAL CONTEXT: OIL, GAS AND MINING

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CONTENT

EDITORS' NOTE

PRESENTATION

For years, in LEĜA's Energy and Natural Resources Practice Area we have analyzed the most important aspects of Venezuela's current energy and natural resources situation, from a legal perspective. In addition, we have been concerned with outlining some conclusions that may be valid for discussion on the future of these important areas of the national economy.

In 2020 we wanted to prepare these brief essays that we present here, under the common title of Venezuelan legal environment: oil, gas and mining, in order to contribute to the debate of key elements relating to energy and natural resources. These essays go over some topics that we have analyzed from a practical but also theoretical perspective, so while they try to address some important concepts, they also aim at suggesting practical solutions to some problems that we have come across.

Venezuelan legal environment: oil, gas and mining encompasses six essays prepared by members of the Energy and Natural Resources Practice Area of LEĜA:

Simón Herrera Celis, in his essay on Some thoughts on PDVSA's legal regime, in view of a possible reorganization of the hydrocarbons industry, summarizes the legal regime to which PDVSA is subjected and points out some ideas that could help out in the reorganization of the hydrocarbons industry around PDVSA as a central player.

Miguel Rivero Betancourt in his essay on The natural gas industry in Venezuela (Reflections on the general basis for a legal framework of gaseous hydrocarbons in Venezuela) describes the general features of the legal regime of the natural gas industry in Venezuela, and then highlights some ideas that can serve as support for a legal framework for the gaseous hydrocarbons in Venezuela, from both policy and legal perspectives.

Simón Herrera Celis and Miguel Rivero Betancourt sum up in the essay entitled Applicable legislation to oil mixed joint ventures, the key features of the joint ventures as the fundamental vehicle for private participation in the hydrocarbons business in Venezuela.

Elina Pou Ruan in her essay on State equity participation and taxation in hydrocarbons activities in Venezuela (Reflections and ideas for a reform) addresses in an introductory fashion the main aspects of the important issue of taxation in the hydrocarbons sector.

Simón Herrera Celis and José Alberto Ramírez León tackle the relationship between arbitration and the oil activity, as a very important instrument for attracting foreign investments, and as a means of resolving possible disputes, in their essay on International commercial arbitration in the oil industry.

Finally, Carlos García Soto in his essay entitled Public and private initiative in the mining activity in Venezuela: an introduction, describes the ways through which the Venezuelan State and domestic and foreign investors are able to participate in the mining business, under the current Venezuelan legal regime.

We wanted to give to our clients, friends and the public in general, these brief essays, as a sign of our commitment to the country, and as a sign of our passion for these pivotal issues for Venezuela.

Energy and Natural Resources Practice Area of LEĜA

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SOME THOUGHTS ON PDVSA'S LEGAL REGIME, IN VIEW OF A POSSIBLE REORGANIZATION OF THE HYDROCARBONS INDUSTRY

SIMÓN HERRERA CELIS*

I. A plan for PDVSA and the hydrocarbons industry

On February 2020 by means of a Decree, the President in Council of Ministers created a Special Commission with ample powers over the hydrocarbons industry, which task is the reorganization of the industry and the defense and safeguard of Petróleos de Venezuela, S.A. (PDVSA). Said Decree with an initial duration of six months, declared the energy emergency of the industry. Its functioning was extended for an additional period of six months by means of a new Decree issued in August 2020, with the purpose of consolidating the industry's complete recovery, even though its results have not made known to the public as of the date we write this article.

The outcome of the government's plan arising from the work of the Presidential Commission could lean to allowing multinational and national companies the ownership of the assets and the operations of the oil industry, along with the restructuring of PDVSA's debt, notwithstanding the big hurdles that the industry is facing in view of the economic sanctions imposed by the United States in the last three years. With regards to the reorganization of the local oil industry, the international press extensively commented throughout last year indicating that the plan would have been prepared by government circles with the aim of allowing intensive private participation.

On the other hand, some analyses have recently pointed out that the main objective of the Anti-Blockade Constitutional Law would be the call for massive involvement of the private sector in certain economic economic sectors, but particularly in the oil sector, all of which we will briefly mention in this essay.

Below we will refer to the constitutional and legal framework governing PDVSA and the hydrocarbons industry which will serve as grounds to a restructuring and reorganization process. Furthermore, we will look into possible legal reforms.

II. The constitutional framework over the state-owned company PDVSA, the reserve of the oil activity and the ownership of hydrocarbons reservoirs

There are three constitutional provisions in Venezuela integrating the legal cornerstone according to which all legal and sub-legal regulations for hydrocarbons activities must follow.

1. Article 303 of the 1999 Constitution regarding PDVSA expressly sets out the following:

"Article 303. For reasons of economic, political and national strategic sovereignty, the State shall keep the totality of the shares in Petróleos de Venezuela, S.A., or of the entity created for the handling of the oil industry, with the exception of those of the affiliates, strategic associations, companies and any other that has been incorporated or that is incorporated in view of the business development of Petróleos de Venezuela, S.A.".

2. Article 302 of the Venezuelan Magna Carta in its relevant paragraph establishes the possibility of reserving certain activities and industries:

"Article 302. The State reserves to itself, through the corresponding organic law, and due to reasons of national convenience, the oil activity and other industries, exploitations, services, goods of public interests and of strategic character. (...)".

* Simón Herrera Celis is a consultant at LEĜA Abogados. Lawyer graduated from Universidad Católica Andrés Bello, (1991). Master of Laws at American University, (2013). Diploma in Hydrocarbons and Mining at Universidad Monteávila, (2007). Admitted to practice law in Venezuela and New York. Member of the Venezuelan Association of Arbitration (AVA).

3. Article 12 of the Constitution sets out that the hydrocarbons reservoirs belong to the Republic, whichever their nature, are public domain goods, and, as such, inalienable and indefeasible. Mining reservoirs have the same constitutional treatment.

The first thing that we have to stress in connection with the constitutional provisions referred to above, is that the holding and controlling corporation, known as PDVSA, or the entity created for the handling of the hydrocarbons industry, must be owned by the Venezuelan state. Let us remember that PDVSA is a commercial enterprise in the form of a stock corporation, which shares are totally owned by the Bolivarian Republic of Venezuela, represented by the Ministry of the Popular Power of Petroleum. As a holding corporation is in charge of coordinating, supervising and controlling the hydrocarbons industry in the country, with assets and interests abroad as well. In our view, the definition of the oil industry, as far as article 303 of the Constitution is concerned, encompasses the whole hydrocarbons industry, notwithstanding its drafting, even though it could lead to some misconstruction in the sense that a restricted interpretation of this provision would leave out the natural gas industry.

Article 303 in fact does allow for affiliated companies, strategic associations and other companies and projects, to be controlled or owned by the private sector, which in reality is seriously limited today by the *Organic Hydrocarbons Law* of 2001 in respect of upstream activities of liquid, solid, semi-solid and associated natural gas, notwithstanding, the recent enactment of the *Anti-Lock Constitutional Law*.

The second thing to emphasize, that comes as corollary of the legal limitations in the upstream businesses, is that the activities related to the liquid, solid, semi-solid and associated natural gas, as well as the works necessary for its handling, were effectively reserved to the Venezuelan State in accordance with said *Organic Hydrocarbons Law* that abrogated the Nationalization Law of 1975. This reservation is of a legal nature and not a constitutional one.

By virtue of the above, the Venezuelan State would not have, at first, a legal framework to allow the direct private participation in the exploration and exploitation of oil resources. In the past, Venezuela and its state agencies executed an important number of service contracts, exploration at risk and profit sharing agreements, strategic associations, licenses and concessions with private international and national oil companies. In fact, there is a recent experience dating back to 2017 where PDVSA executed various service contracts with private parties, although the legality of such contracts has come under scrutiny in view of the provisions of the *Organic Hydrocarbons Law (LOH)*.

In addition, it is convenient to consider that the hydrocarbons industry is a global industry with an aggregated experience of more than one hundred years. Thus, the contractual and association schemes have general features that have suffered transformations with the passing of time, with model documents sometimes hybrid, all of which have their particularities in each jurisdiction, including Venezuela.

The third thing to bear in mind is that the association and contractual schemes with the private sector must always acknowledge that the hydrocarbons are owned by the Republic, and that is the way it has been since its independence as a Nation, in accordance with article 12 of the Magna Carta. Hence, from a constitutional perspective it is only permitted to confer real administrative rights of use over the reservoirs as goods of public domain. That is, the rights conferred are always an administrative granting by the State in favor of third parties.

III. The Organic Hydrocarbons Law, its limitations and the internal market

In accordance with article 9 of LOH, upstream activities (i.e. primary activities) relating to liquid, solid, semi-solid and associated natural gas, are exploration, hydrocarbons' extraction in their natural state, collection, transportation and initial storage, as well as those works necessary for their handling. These primary activities are the ones reserved to the State in an exclusive manner, but LOH allows that the exploration and exploitation rights, and all other primary activities, might be transferred to mixed joint ventures, in which the private sector is entitled to participate in less than fifty percent in the capital stock. Since the year 2006 these joint ventures have been put in place, marking the end of the so-called Venezuelan oil opening. Needless to say, all oil projects in which there is some degree pf private participation nowadays, are controlled by the Venezuelan State through affiliates of PDVSA. As a general non-written rule, PDVSA, through wholly-owned affiliates, holds sixty percent of the shares in the capital stock of the mixed joint ventures, above the legal threshold required under LOH, with only a few exceptions.

In downstream or midstream activities –refining and industrialization- LOH allows for oil projects to be carried out by the private investors without the involvement of the State. This is also true with respect to non-associated gas projects, upstream, midstream and downstream, in accordance with *the Organic Gas Law* of 1999.

With regards to the internal fuels' market, such as gasoline and diesel, such market is reserved to the Venezuelan State, in accordance with the *Organic Law for the Reordering of the Liquid Fuels' Internal Market* of 2008. To date, the private sector is not entitled to participate in the internal market. Further, no mixed joint ventures are allowed in this market.

IV. The need for a legislative reform v. the new Anti-Lock Constitutional Law

It is our opinion that a legislative oil reform through the National Assembly is necessary, being the National Assembly the competent body to enact laws in accordance with the Constitution, in order to allow different contractual and association schemes, and not only mixed upstream joint ventures, or to allow a greater equity share in said mixed joint ventures. In addition, it would be necessary to reform the Organic Law for the Reordering of the Liquid Fuels' Internal Market to consent to the involvement of private parties in this business.

Notwithstanding the above, we cannot discharge that the National Constituent Assembly (ANC) sanctions a new general regulation for the oil business, as done in the past with a series of very important laws, even though the legality and legitimacy of the ANC has been put to question under the contention that it has no legal powers to enact laws. In fact, the ANC sanctioned the *Anti-Lock Constitutional Law for National Development and the Warranty of Humans Rights,* published and with the force of law since October 2020. This new regulation by the ANC would have as its objective the reactivation of the national economy and the opposition to the international sanctions headed by the U.S. government, even though, it would seem to seek the promotion of private investments, as previously noted. Its provisions would be of a temporary nature and would be in force solely until the blockade ceases or until it has lasting effects over the economy. In any event, it seems that the ANC functions came to an end in December.

Constitutional laws do not have legal grounds nor historic tradition in Venezuela. They are basically a legal institution borrowed from other countries in which they are recognized and have tradition. What could be eventually happening here is that by means of a constitutional law an organic law, such as LOH, could be partially and tacitly abrogated. As we already mentioned, this regulation reserved the oil industry to the Venezuelan State in the terms specified therein and in accordance with article 302 of the Constitution.

Article 26 of the *Anti-Lock Constitutional Law* grants the National Executive the power to modify the mechanisms for the incorporation, management and participation of public and mixed companies (mixed joint ventures). This provision could certainly affect and have a deep impact on the affiliated companies of Petróleos de Venezuela, S.A. and mixed joint ventures. This would not be the case for this holding corporation due to the fact that it has constitutional protection with respect to the preservation of its publicly-owned capital. In accordance with article 103 of the Organic Law for the Public Administration, mixed joint ventures in the upstream oil business are qualified as state-owned entities, together with PDVSA's wholly-owned affiliates.

We do believe that the *Anti-Lock Constitutional Law* opens up a novel space for discussion and debate that could ultimately be the starting point for a new oil opening. But what the *Anti-Lock Constitutional Law* does not deal with and we have not seen anywhere else with clarity, is how to restructure PDVSA'S debt-servicing obligations and downsizing plan to reduce costs. It is paramount that the company renegotiates its huge financial and commercial debt with a mechanism allowing it to pay creditors based on actual increased revenues.

Conclusions

For the purpose of the recovery of the Venezuelan oil industry it is required a greater participation of the private capital, along with its greater control over the operations and managerial and technical decisions, which necessarily means contributing with technology and qualified personnel. In our opinion, the reorganization plan for the industry announced by the government has to follow this path, aiming at reducing the burdens over the national public budget, restructuring PDVSA's debt and giving a stellar role to private enterprises with an aggressive investment plan for the short and mid term.

There is a constitutional configuration that would consent to this opening to the private sector, as long as the handling of the hydrocarbons industry

is done through Petróleos de Venezuela, S.A. or the entity created for such purposes. The handling has to be read as the supervision, coordination and control over the industry, in which some of the key features are the power to bid, select and administer projects with private investors in the various contractual and association schemes.

Further, foreign and national investors must assess in detail the involvement in new projects or acquiring stocks in existing mixed joint ventures above the limited contemplated under LOH, in the terms set forth in the *Anti-Lock Constitutional Law*. To this end, it would be advisable the signing of legal stability contracts that are also regulated under this new law, which could serve as a mitigation of risks' tool now that a new oil opening could be around the corner. In any event, we take this opportunity to highlight the importance and pertinence of enacting a new hydrocarbons statute to replace the LOH of 2001, notwithstanding the new *Anti-Lock Constitutional Law.* We are also of the view that it is necessary a new Law for the Internal Market of Fuels.

The Organic Gas Law is a model that could be replicated in the case of liquid hydrocarbons, since it is a law that promotes private investments in a clear and precise manner. Please bear in mind that it is required to develop both oil and natural gas projects, in a moment when all evidence points to an energy transition towards cleaner energy sources, in which natural gas will have a more important role as a lesser contaminant hydrocarbon. The immense hydrocarbon reserves in Venezuela are still waiting to be exploited.

There are countless signals coming from important political, economic and academic voices in recent times evidencing the urgent need for allowing the private international and national sector to assume bigger responsibilities in the hydrocarbons industry with the multimillion investments needed for its recovery and relaunching.

THE NATURAL GAS INDUSTRY IN VENEZUELA (REFLECTIONS ON THE GENERAL BASIS FOR A LEGAL FRAMEWORK FOR GASEOUS HYDROCARBONS IN VENEZUELA)

MIGUEL RIVERO BETANCOURT*

Introduction

The natural gas industry in Venezuela is fundamental for the development of the country and for its economic reactivation[1]. Traditionally, natural gas has been considered a by-product of oil (the ugly duckling that no one looks at). In the Venezuelan case, the situation is more dramatic, because there is a clear oil culture above any other industry, including natural gas.

The present article comprises an analysis of the natural gas industry in Venezuela, in which the structure of its energy matrix is briefly developed, as well as a brief reference to the production and consumption of natural gas in its different modalities: methane gas, natural gas liquids and liquefied petroleum gas. In addition, we briefly discuss the participation of the private sector in the natural gas industry value chain. Next, we elaborate on the current regulations for the development of the industry, and then, provide our reflections on the basis for a legal framework for gaseous hydrocarbons in Venezuela. And finally, our conclusions.

I. Structure of the country's energy matrix and policy

Venezuela's secondary energy matrix has the following distribution: liquid hydrocarbons, 38%; methane gas, 36%; and hydroelectricity, 26%. As it can be shown, natural gas is predominant in the country's energy matrix. It is used 71% in oil industry and 29% in domestic market (21% for electricity generation, 24% in steel and aluminum sector, 13% in petrochemicals, 5% in commercial and residential use, 5% in cement industry and 32% for other uses).

Therefore, it is essential to have enough free natural gas to satisfy the requirements of the domestic market, before allocating volumes for export. [2]

II. Structure of the gas industry

There are many different uses for the components of natural gas, and there are also many different users of this precious product. In this respect, we must point out that, in general terms, the users of natural gas are composed of residential, commercial, industrial, electricity generation and vehicle fleets.

In case of the residential and commercial sector, gas is used primarily for heating (in countries whith low temperatures) or air conditioning, hot water, cooking and drying clothes .[3]

Regarding the industrial area, gas is mainly used as heating and cooling areas in their industries and factories, constituting its major use in a variety of processes of metal smelting, treatment, forging and casting that take place in furnaces, boilers, foundries, dryers, and other industrial manufacturing equipment[4]. As for the last two sectors, natural gas is used as an alternative for electricity generation and as an alternative fuel to gasoline and diesel[5] .

As can be seen, uses of gas are diverse. The components of gas (Methane, Ethane, Propane, I-Butane, N-Butane, I-Pentane, N-Pentane, Hexane, Heptane, Carbon Dioxide) each have their own value and use. For example, in Venezuela, methane gas is the most frequent component found in the subsoil, in a close average proportion of 80%, being the one that is fundamentally used and exploited in our country. It is followed by ethane, propane, and butane, in an average proportion of about 7%, the last two being the so-called cylinder gases.

Natural gas consumption[6] is considered the world's fastest growing primary energy resource. Venezuela has proven natural gas reserves of 222.4 trillion cubic feet (Tcf) by 2020[7], the second largest in the Western Hemisphere (after the United States) and the eighth largest in the world. The country produced approximately 7.793 Tcf in 2015[8], all of which was consumed domestically.

As we have already pointed out, most of the country's usable natural gas production is consumed by the oil industry which reinjects gas into oil fields, another part is delivered to the domestic market, and another smaller portion is transformed into Natural Gas Liquid. The rest is distributed among gas thrown out, and for other uses such as the generation of electricity;

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* Miguel Rivero Betancourt is a senior partner in LEĜA Abogados. Lawyer, graduated from the Universidad Católica Andres Bello (UCAB), (1991). He holds a Specialization in International Economy and Integration Law from Universidad Central de Venezuela, (1999). He holds a Law Master's Degree (LLM) in Natural Resources and Environmental Law and Policy and a Specialization in Energy Law, both studies having been completed at the University of Denver, Colorado, (2002). Guest professor at the Hydrocarbons Management Diploma (IESA). President of the Venezuelan Association of Gas Processors (AVPG).

[1] Nelson Hernández (November 2020), "El Rol del Gas en la Reactivación Económica de Venezuela": https://venezuelagas.org/wp-content/uploads/2020/11/El-rol-del-gas-en-la-reactivacio%CC%81n-econo%CC%81mica-de-Venezuela.pdf(09-22-2020).

in the petrochemical production, and the rest is used mainly by the industrial or commercial clients in big cities.

It is important to note that Petróleos de Venezuela, S.A. (PDVSA) has traditionally monopolized the production of Venezuelan natural gas. However, on August 1999, the legislation opened the country's natural gas sector to foreign investment in exploration and production, distribution, transmission, or commercialization. Venezuela held its first exploration of non-associated natural gas (free gas) in 2001.

In Venezuela, the growth in energy consumption of the primary transformation sector (steel, aluminum, and petrochemicals) and, in general, of its population (electricity and residential fuel), will be supported by natural gas, which makes it necessary to seek effective and long-term solutions. On the other hand, the technology aims at physical and chemical transformation as the new way to expand the natural gas business in international markets.

In this way, the effort of the Venezuelan state is oriented to achieve the most efficient use of a resource with abundant reserves, low cost, compared to other alternatives, and with its own characteristics to preserve in greater degree the environment, and that will present, in the next years, high availability derived from the exploitation of the reserves of non-associated gas and gas associated to the production of the crude oil.

1. Exploration and exploitation (off-shore and on-shore)

In Venezuela, exploration for gas has been very limited. On land, in the 80's, it was explored in Guárico State (Yucal-Placer Area). The discoveries of resources in the area known as Cristobal Colon, now Mariscal Sucre, were in search of oil; the same happened in the Plataforma Deltana.

More recently, gas exploration has taken place in Falcón State: important reserves were discovered in the Cardón IV area, developed by ENI and Repsol[9].

Because of this, the country's natural gas resources are mostly associated with oil. By 2015, the Gas Licenses had produced 364 Million Cubic Feet (MMP/D)[10].

2. Gas consumption: Natural Gas, Natural Gas Liquids (LNG), Natural Gas Vehicles (NGV), Liquefied Petroleum Gas (LPG) and other gases

From a natural gas production of 7,439 mmpc/d of 103.8 Thousands of Barrels per Day (mb/d) of natural gas liquids in 2017, according to figures from the state-owned PDVSA (note that there is a decrease to that reflected in the 2015 Management Report[11]), 2 were injected into the fields for additional recovery.119 mmpc/d; other consumption is of 2,444 mmpc/d of methane gas, of which 959 mmpc/d went to electricity sector, 539 mmpc/d to oil sector, 479 mmpc/d to petrochemical sector, 169 mmpc/d to steel and aluminum sectors, 121 mmpc/d to manufacturing, 129 mmpc/d to domestic and commercial sectors, and only 3 mmpc/d as NGV. To complete the balance, there were 2,730 mmpc/d of unused gas (dumped, flared and waste). With respect to liquefied petroleum gas (LPG), a total of 117 thousand barrels per day (mb/d) were sold, to the domestic sector they were 44 mb/d, to petrochemical sector 28 mb/d, and to PDVSA 17 mb/d. Additionally, 28 mb/d were exported.

3. Free gas licenses

MENPET has granted various Gas Licenses for the exploration and exploitation of non-associated natural gas. In 2001, MENPET granted six licenses[12] for the exploitation of non-associated natural gas, two of which were development licenses over areas of proven reserves (Yucal Placer North and South areas), and the remaining four were exploration licenses (Barrancas, Tiznado, Barbacoas and Tinaco areas). In 2002, the License for the San Carlos Area was granted[13].

In 2003, two licenses were granted for the exploration of non-associated gaseous hydrocarbons, for Block 2[14] and Block 4[15] of the Deltana Platform. In 2004, a license for the exploration of non-associated gaseous hydrocarbons was granted for Block 3[16] of the Plataforma Deltana.

[2] Presentation by Diego González at UNAM: “Oportunidades en Materia de Gas Natural en América Latina”, Mexico City, 2012.
[3] Alfredo Méndez (2006), Aliento de Piedra, Vita Arte Producciones C.A, Chapter 3, pp. 42 - 49.
[4] Alfredo Méndez (2006), Op. Cit., Chapter 3, pp. 49-51.
[5] Alfredo Méndez (2006), Op. cit., Chapter 6, pp. 88-90.
[6] “International Energy Outlook 2019 in Natural Gas”: http://www.eia.doe.gov/oiaf/ieo/nat_gas.html, (02-12- 2019). This page is produced by the Energy Information Administration (EIA) of the Government of the United States of America.
[7] See “Statistical Review of World Energy 2020”, 69th edition: https://venezuelagas.org/wp-content/uploads/2020/06/bp-stats-review-2020-full-report.pdf, (11-16-2020).
[8] PDVSA 2016 Management Report.
[9] Gas License granted to Cardón IV, S.A., Resolution No. 11, 01-27-2006, Official Gazette of the Bolivarian Republic of Venezuela N° 34,319 dated 02-02-2006.
[10] www.pdvsa.com
[11] Report of PDVSA’s commissioner 2016.
[12] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 37,266 dated 08-22- 2001.
[13] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 37,577 dated November 25, 2002.
[14] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 37,645 dated March 7, 2003.
[15] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 37,641 dated February 27, 2003.
[16] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 37,996 dated August 6, 2004.

In 2005, licenses were granted for the exploration of gaseous hydrocarbons not associated with the Urumaco I, Urumaco II, and Cardón III Blocks, corresponding to Phase A of the Rafael Urdaneta Project[17]; and Cardón IV[18] and Moruy III[19] Blocks, corresponding to Phase B of the Rafael Urdaneta Project.[20]

In 2017, the Russian state oil company Rosneft was granted a license for the exploration and exploitation of non-associated gas for the development of the Costa Afuera Patao and Mejillones fields, located in the north of Sucre state, for a period of 30 years for the export of Liquefied Natural Gas.[21]

III. Regulatory framework

In the present time, two important legal instruments related to the natural gas sector are in force in our national legislation: *the Organic Law of Gaseous Hydrocarbons, promulgated as Decree No. 310 of September 12, 1999* (*Gas Law*) [22] and its Regulations promulgated as *Decree No. 840* of May 31, 2000[23]. These legal instruments contain the normative basis for investors to know their rights and obligations to decide to invest in natural gas projects in Venezuela.

The principles that govern all activities regulated in the *Gas Law* (Exploration, Production, Storage, Transportation, Distribution, and Commercialization) (i) are primarily aimed at national development; (ii) which must be carried out through the intensive and efficient use of such substances, such as Fuel for domestic[24] and industrial use[25]; raw material for the purpose of industrialization and eventual export in any of its phases; (iii) they must safeguard the defense and rational use of the resource and the conservation, protection and preservation of the environment; (iv) they will propitiate the formation and the participation of national capital and goods of national origin will concur with transparency and non-disadvantageous conditions[26], that will be carried out by maximum participation of the management and national personnel, goods and services given by local citizens, among others[27]. A genuine purpose of encouraging national development through the process of opening gas is observed from the principles enunciated.

According to the *Gas Law*, the natural gas chain is clearly identified with respect to the following segments: exploration, production, extraction and fractionation of natural gas liquids, transportation, distribution of methane gas, internal commercialization of natural gas products and its exploitation, as well as the liquefaction of natural gas.

The development of methane gas transport and distribution activity is indispensable and will see forms of association for the expansion of existing systems, while the extension of these to new geographical areas may be carried out directly by private companies motivated by the consumer sectors.

The internal commercialization of natural gas products (both liquid and methane gas) will be supported by supply contracts, until the development of a greater level of competition in gas production occurs in the country, through profit-sharing agreements already signed with private companies, or others, derived from the

[17] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 38,304 dated November 1, 2005.
[18] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 38,371 dated February 2, 2006.
[19] Published in Official Gazette of the Bolivarian Republic of Venezuela No. 38,380 dated February 15, 2006.
[21] Published in the Official Gazette of the Bolivarian Republic of Venezuela No. 41,302 of December 18, 2017.
[22] Official Gazette No. 36,793 of September 23, 1999.
[23] Official Gazette No. 5,471 of June 5, 2000.
[24] According to the Regulations of the Gas Law, Domestic Gas is the methane gas used as fuel in appliances and equipment for domestic use, installed in single-family or multi-family homes, which is delivered through a connection to a distribution network.
[25] According to the Regulations of the Gas Law, Industrial Gas is the methane gas used as fuel or raw material in facilities, plants, or factories, where industrial operations are carried out to obtain a product or transform a substance or product, which is delivered through a connection to a network of pipes in a Distribution region or a Transportation System.
[26] Articles 3 and 7 of the Gas Law.
[27] Article 3 of the Gas Law Regulations.

granting of licenses by the Ministry of People's Power for Energy and Petroleum (now the Ministry of People's Power of Petroleum, MENPET)[28] for the exploration and exploitation of new areas.

According to the *Gas Law*, exploration and exploitation activities of non-associated gas may be carried out by the State directly or through companies owned by it, acting alone or with the participation of national and foreign private sector investors. In order to private investors to develop these activities, they must obtain a license, which is processed and authorized by the MENPET[29] .

The license confers on the holder the exclusive right to carry out exploration and exploitation activities in accordance with the terms established therein. The rights conferred by the licenses are not taxable or enforceable but may be assigned with the prior approval of the MENPET. According to the Regulations of the Gas Law, in the basis of the bidding process the MENPET must include the considerations to which the Republic aspires in exchange for the license.

The *Gas Law* establishes that all assets and facilities related to exploration and exploitation activities carried out under a license are subject to the right of reversion, which is the right of the Republic to acquire ownership of all assets and facilities used by the licensee to fulfill the purpose of the license on the date the license is terminated for any reason. Likewise, the referred Law indicates that the controversies between the Republic and the holder of the license may be resolved by arbitration; however, said Law does not distinguish between local and foreign arbitration.

In this respect, the Regulations of the *Gas Law* establishes that the parties may agree that disputes related to licenses will be finally resolved through arbitration[30].

The license is the title by which the State authorizes the performance of exploration and exploitation activities.

However, since very qualified professionals have developed in detail the meaning and scope of the Gas Law throughout its value chain, I have decided not to go into details on this subject in this essay. Thus, I rather recommend some authors and publications{31].

IV. Reflections on the general basis for a legal framework for gaseous hydrocarbons in Venezuela

The gas industry is in one of its worst historical moments in terms of production of free gas and associated gas, as well as of a significant deterioration of the infrastructure needed to handle natural gas throughout the value chain for use by end consumers. The causes are diverse in nature, but I would summarize them in political, economic, social, and managerial.

The *Gas Law*, as we have pointed out, allows private participation in the entire value chain from the exploration, exploitation, transportation, distribution, and sales stages. However, even though at the beginning of the 21st century (2000-2006) the policy maker and executor gave an impulse to the development of the industry with private participation, the truth is that, as of 2007, this impulse stopped with the entry into force of various laws that limited the participation of the private sector, with the effects that these political and legal actions caused in the fall of the production of crude oil and gas[32].

In this sense, the objective of these reflections is to put on the table to industry players and policy makers, public finance professionals, economists, lawyers, among others, some general basis that can be considered to achieve an adequate legal framework in gas matters. Thus, we mention below the following general basis:

[28] Ministry of the People's Power of Petroleum (MENPET). Website: www.menpet.gob.ve

[29] Baker & McKenzie Caracas Office (2000), "La Regulación de los Hidrocarburos Gaseosos en Venezuela", published by the Venezuelan Association of Gas Processors (AVPG), Volumen N° 1, Caracas, Venezuela

[30] Article 19 of the Gas Law Regulations.

[31] Diógenes Bermúdez (2007), Régimen Jurídico de los Hidrocarburos Gaseosos en Venezuela. Colección Estudios Jurídicos N° 85, Editorial Jurídica Venezolana. Asociación Venezolana de Procesadores de Gas (AVPG), Publications Series. Since 2000, AVPG has published 5 books containing more than 50 articles on natural gas regulation. (No. 1) OFFICE OF CARACAS DE BAKER & MACKENZIE (2000). The Regulation of Hydrocarbons in Venezuela. A General Description of the Organic Law of Gaseous Hydrocarbons and its Regulations and Some Legal Issues in the Gaseous Hydrocarbons Sector. (No. 2) Integral Development of the Natural Gas Industry in Venezuela. Legal and Historical Review. (2004), Several authors. (No. 3) Legal Advances in the Gas Industry in Venezuela. (2007). Various authors. (No. 4) Impact of the Legislation on the Natural Gas Industry in Venezuela. (2009) Various authors. (No. 5) Legal Framework of the Natural Gas Industry in Venezuela. (2011) Various authors.

[32] Since 2007, a set of laws came into force that directly or indirectly affected the gaseous hydrocarbon activities that the private sector had been carrying out throughout the gaseous hydrocarbon value chain. In effect, the National Executive carried out a set of policies aimed at taking control of the hydrocarbons activities throughout the value chain that were under the exercise of the private sector. Among these laws we identify the Law for the Regularization of Private Participation in Primary Activities set forth in Decree No. 1,510 with the Force of Law of Hydrocarbons (Official Gazette No. 38,419 dated April 18, 2006); the Law for the Migration to Mixed Companies of the Association Contracts of the Orinoco Oil Belt; as well as the Exploration Contracts at Risk and Shared Profits (Official Gazette No. 38,632 dated February 26, 2007); the Law on the Effects of the Migration Process to Mixed Companies of the Contracts of Association of the Orinoco Oil Belt; as well as the Exploration Contracts at Risk and Shared Profits (Official Gazette No. 38.785 of October 8, 2007); the Organic Law for the Reorganization of the Internal Market of Liquid Fuels (Official Gazette No. 39,019 of September 18, 2008), and the Organic Law that reserves to the State Goods and Services related to the Primary Activities of Hydrocarbons (Official Gazette No. 39,173 of May 7, 2009).

[33] PROPUESTA DE MARCO CONCEPTUAL PARA UNA POLITICA ENERGETICA EN VENEZUELA. (June 2020) Energy Commission, National Academy of Engineering and Habitat, Palacio de las Academias, San Francisco Stock Exchange. Caracas 1010. Link made on 11/16/2020 https://plumacandente.blogspot.com/2019/09/anih-propuesta-marco-conceptual.html.

1. Integral Energy Policy: The success of a legal framework is based on the definition, elaboration and execution of an integral energy policy that enjoys the greatest consensus to achieve the necessary stability and generate confidence. In this policy, natural gas will play a very important role within a multi-sector economic development plan for the country and as a transition fuel in the world energy matrix[33]. The understanding of the gas industry and its clear differences with other extractive industries will allow a better definition of a government policy in this sector. For this purpose, it will be necessary to have high level professionals in different areas (gas engineers, geologists, economists, lawyers, among others) that will allow to build a plan that considers all the aspects associated to this industry.

2. Institutional Framework: The definition of the roles the different public bodies should have in gas matters. Namely, the Ministry of the Popular Power of Petroleum (MENPET), Vice-Ministry of Gas, PDVSA Gas, Ministry of Finance, Central Bank of Venezuela, ENAGAS, among others. As well as defining clear interaction schemes between such entities and them with the private sector through a high technical level mechanism with clear decision-making capacity for the quick and expeditious resolution of conflicts and consultations between licensees and any other private actor in the natural gas value chain and the authorities. That is, to achieve speed and certainty in the decision-making process by the official sector.

3. Characteristics of the Gas Industry: The gas industry has certain characteristics regarding its economy and its role as a raw material for industrial development that make it special and that are not understood in an integral and appropriate manner by political, economic, and social actors. For this reason, we must work on permanent training on the functioning of this industry in all areas, especially in the sector of the Legislative Power. It is important to understand the economy and the structure of markets. Likewise, investment and production cycles must be taken into account, especially the characteristics of investment in the gas industry throughout the value chain.

4. Tax and Royalty Regime: The tax and royalty regime must be structured in such a way that it allows a balance between the satisfaction of general interests and particular interests. To this end, such regime must take into account the improvement of competitiveness and productivity. This is a very important matter to attract investments. The interaction of public policy makers, public finance professionals, economists, lawyers, among others, is fundamental for the good design of the tax and royalty regime.

5. Licenses, permits and contracts: The development cycle of gas projects is 15, 25 and 35 years, depending on their nature and the characteristics of the projects, which requires a robust legal and contractual regime that considers aspects such as legal security, adaptability to short-term realities and flexibility but, at the same time, guarantees the permanence and continuity of the contracts over time, using the various tools associated with contract risk management. Aspects such as transparency, accountability (income and expenses), environmental security, hygiene and environment of work, environmental protection (environmental impact, remediation, etc.). among others, are aspects that should be taken into consideration. In terms of transparency, we refer to effective systems that regulate, on equal terms, the possibility of reasonably measuring the financial risks and benefits of projects. And, in terms of adaptability, we refer to legislation, licenses, permits, and contracts that take into account the technical, financial and commercial realities, both national and international.

6. Foreign Investment: Appropriate legal framework for foreign investment, adjusted to the new realities of the international market. For example, the legal framework for foreign investment should be reviewed, such as the Constitutional Law of Productive Foreign Investment[34], as well as other sectoral laws, among others: *Organic Law on Hydrocarbons and its Regulations* (aspects such as royalties, strengthening of ENAGAS, jurisdiction in case of conflicts, balance sheet on gas destinations (domestic market and export), and national capital and industrialization. The reinsertion of Venezuela into the Convention on the Settlement of Investment Disputes between States and Nationals of other States, which was denounced on January 24, 2012 by the Bolivarian Republic of Venezuela before the World Bank[35] , must also be evaluated.

Conclusions

This article briefly develops various topics of a technical, commercial, and legal nature regarding the natural gas industry. From what we have mentioned, we are able to identify the following conclusions:

(i) Venezuela has an abundant natural gas reserve, a fundamental raw material for the development of the national industry and a key factor for the economic reactivation of the country.

(ii) Policy makers and professionals specialized in this field must make a concerted effort on how this industry will develop in the next 20, 30 and 40 years (short, medium, and long term).

[1] See the Official Gazette No. 41,310 of December 29, 2017.

[1] See Communiqué of January 25, 2012 issued by the Ministry of People's Power for Foreign Affairs of the Bolivarian Republic of Venezuela, in which it is stated: "The government of the Bolivarian Republic of Venezuela formalized on January 24, 2012, its irrevocable denunciation before the World Bank of the 'Convention on the Settlement of Investment Disputes between States and Nationals of Other States' of 1966, which establishes the International Centre for Settlement of Investment Disputes (ICSID)". This convention was signed by Venezuela in August 1993 and ratified by means of an Approving Law published in the Official Gazette No. 35,685 of April 3, 1995.

Here, the vision of rentier versus industrialization of the country should be reviewed, as well as the role of Venezuelan capital in its development. The interesting thing is that we are not starting from scratch, our industry has an installed capacity throughout its value chain, which requires financial, technical, and human capital support to increase production capacity and satisfy the requirements of the national and international markets.

(iii) The development of the gas industry should consider the various challenges associated with the energy transition such as: global environmental policy of zero CO2 emissions causing the greenhouse effect, and the emerging of alternative energy sources in the medium and long term that will occupy a space in the international market displacing fossil fuels, including natural gas.

(iv) The development of the natural gas industry must be directed primarily to satisfy the needs of the Venezuelan people through the provision of a quality (public) service, as established in Ordinal 29 of Article 156 of the Constitution of the Bolivarian Republic of Venezuela. In this sense, the concept of energy security plays a vital deontological role. This does not suggest that Venezuela should forget about the international market or exports. Fortunately, Venezuela has an extraordinary export potential through offshore projects and although I have said that the domestic market should be primarily served, there is a sufficient resource base to satisfy both domestic and foreign demand.

(v) There are several elements that form the basis of a gas legal framework. I have developed a few in this article, such as: the need to define, elaborate and execute a comprehensive energy policy, which includes the gas industry in its entire value chain. This should define the participation of natural gas in the national energy matrix over the next 20, 30 and 40 years.

(vi) Within the general basis for the construction of a legal framework on natural gas, I have mentioned the importance of having solid institutions, with clearly differentiated roles and composed of qualified professionals who act in accordance with the legal system. Solid institutions will allow for the continuity of contracts without the radical influence of the governments in power. Since these projects have a duration of 25 years, the political actors and specialists in the area must work to build a solution that will give stability to the contracts. This is fundamental to generate confidence in investors.

(vii) I have also pointed out the importance of clear and predictable rules of the game for the parties involved, as well as the importance of defining a competitive tax and royalty regime, considering technical, commercial (market), financial and legal realities. Accordingly, the legal regime to promote the participation of the national and/or international private sector must be attractive, allowing to attract the investments required to develop the gas industry. Furthermore, national capital plays a very important role, and national participation has high capabilities to contribute to the development of the industry. The focus should be on achieving the industrialization of the country since natural gas is a very important driver in the reactivation of the Venezuelan economy.

(viii) Finally, other laws (other than the Gas Law) should be reviewed to make them more attractive to foreign investment. Such is the case of the Constitutional Law of Productive Foreign Investment.

APPLICABLE LEGISLATION TO OIL MIXED JOINT VENTURES

SIMÓN HERRERA CELIS*
MIGUEL RIVERO BETANCOURT**

Introduction

This article touches the most relevant issues of the Venezuelan legislation governing upstream oil mixed joint ventures ("empresas mixtas"), which have as their objective the execution of primary activities concerning liquid, solid and semisolid hydrocarbons and associated natural gas. Such enterprises have their basis in the Hydrocarbons Organic Law of 2001 (reformed in 2006). Up to date, the regulatory framework for the performance of these activities relates to a semi-open economic model, in which only a minority private participation is allowed.

The importance of oil and gas in Venezuela cannot be underestimated, even though the global announcements and actions of the energy transition towards cleaner energies are a big issue to take into account. The country still has huge opportunities for oil and gas investments, as drivers of fiscal income with significant boosting effects in the economy, as we have seen in previous oil booms. These investments have a positive weight in the economy and certainly add value to the downstream hydrocarbons industry with the creation and promotion of industries such as the petrochemicals.

We will examine the most important regulations for oil ventures, cautioning our readers that this brief essay does not cover all the relevant legal issues concerning oil mixed joint ventures, which must be thoroughly review in the event of a legal assessment to decide on a possible investment. We also want to make clear that we have not included our opinion on whether the Anti-Blockade Constitutional Law for the National Development and the Warranty of Human Rights enacted in 2020 may, in any way, modify the legal scheme for the creation, functioning and participation of the private sector in oil joint ventures.

I. The Hydrocarbons Organic Law in upstream and downstream activities

The Hydrocarbons Organic Law ("LOH") is the key legal instrument to carry out exploration, exploitation, transportation, processing, industrialization, and commercialization activities in hydrocarbons projects. The LOH has been established to: (a) secure the State control in all upstream oil projects, significantly restricting the possibility of private participation in primary activities, introducing to that end the form of mixed joint ventures; and, (b) allow the total participation of private capitals in downstream projects, not having the need in these cases to have mixed joint ventures, hence, the projects can be carried out without the involvement of the Venezuelan State. To be clear, in upstream projects the State can be involved either directly or through one of its exclusively owned entities or under the mixed joint ventures' scheme. Further, the Regulation of the Hydrocarbons Law of 1943 and the Regulation for the Conservation of Hydrocarbons of 1969 have not been expressly abrogated, even though their application is limited nowadays.

* Simón Herrera Celis is a consultant at LEĜA Abogados. Lawyer graduated from Universidad Católica Andrés Bello, (1991). Master of Laws at American University, (2013). Diploma in Hydrocarbons and Mining at Universidad Monteávila, (2007). Admitted to practice law in Venezuela and New York. Member of the Venezuelan Association of Arbitration (AVA).

** Miguel Rivero Betancourt is a senior partner in LEĜA Abogados. Lawyer, graduated from the Universidad Católica Andres Bello (UCAB), (1991). He holds a Specialization in International Economy and Integration Law from Universidad Central de Venezuela, (1999). He holds a Law Master's Degree (LLM) in Natural Resources and Environmental Law and Policy and a Specialization in Energy Law, both studies having been completed at the University of Denver, Colorado, (2002). Guest professor at the Hydrocarbons Management Diploma (IESA). President of the Venezuelan Association of Gas Processors (AVPG).

On the other hand, the activities relating to non-associated gas (similarly known as "free gas") are regulated under the Organic Law for Gaseous Hydrocarbons of 1999 and its Regulation of 2000.

II. Private capital participation in the execution of primary activities

The use of mixed joint ventures under the LOH was based on a public policy choice made by the lawmakers in 2001, which is one that might be revised by means of a legal reform. In accordance with article 9 of the LOH, the primary activities on liquid (crude oil), solid and semi-solid hydrocarbons and associated natural gas, usually known in the industry as upstream activities, encompass the exploration, extraction of the hydrocarbons in its natural state, collecting, transporting, and initial storage, as well as the works that their handling may require. It is important to point out that the abovementioned activities only include the hydrocarbons in its natural state, leaving out processed hydrocarbons or by-products. Furthermore, in relation to the reserved activities (collecting, transporting and storage), it only refers to the initial collection, transportation and storage, that is, immediately after the extraction of the natural hydrocarbons.
The Venezuelan oil legislation in force (LOH) sets out that the primary activities are reserved to the State in an exclusive but not excluding manner. The Law does allow that the exploration and exploitation rights be conferred upon the mixed joint ventures, in which the private sector has a minority stake of less than fifty percent (50%) in the capital stock. In the articles of incorporation and by-laws of the mixed joint ventures we will find a class A shareholder, affiliate of PDVSA (usually Corporación Venezolana del Petróleo, S.A. ("CVP"), as the corporate vehicle designated for the businesses with private parties, along with PDVSA Social, S.A., which has recently acquired a minimum stake in the mixed joint ventures from CVP, and the class B shareholders, which are the foreign or national private investors (one or more). For the purpose of formalizing the incorporation of the mixed joint ventures for the exercise of primary activities, the LOH requires the previous approval of the National Assembly, for which reason, the National Executive, through the now called Ministry of the Popular Power of Petroleum, must inform it of all pertinent conditions and circumstances, including any special advantages set forth in favor of the Republic.

Complementary legislation was enacted following the LOH, as indicated:

(i) Law for the Regularization of Private Participation in Upstream Activities set forth under Decree N° 1,510 with the Force of Hydrocarbons Organic Law;

(ii) Law for the Migration to Mixed Joint Ventures of Strategic Associations and Profit Sharing Agreements;

(iii) Law on the Effects of the Migration to Mixed Joint Ventures of Strategic Associations and Profit Sharing Agreements; and

(iv) Organic Law Reserving Certain Goods and Services Related to Hydrocarbons Primary Activities.

III. Creation and functioning of mixed joint ventures

Mixed joint ventures adopt the form and legal personality of equity commercial companies regulated under article 200 of the Commerce Code, and in practice they have been incorporated as stock corporations. These enterprises are considered State entities, subject to a particular legal regime. The formalities for the creation and functioning of such upstream enterprises are the following:

(i) Determination of the project by the Ministry of the Popular Power of Petroleum;

(ii) Minority shareholders' selection process;

(iii) Rendering the report to the Permanent Commission of Energy and Mines of the National Assembly;

(iv) Approval of the incorporation and conditions by the National Assembly;

(v) Presidential decree on the creation of the mixed joint venture;

(vi) Ministerial resolution on the geographical area where primary activities shall be performed;

(vii) Registration of the mixed joint venture with the Commercial Registry Office;

(viii) Presidential transfer decree on the exercise of primary activities.

In addition, a joint venture contract between the State entity and the private investors is executed, giving the basis and general framework for the relationship of the shareholders in the mixed joint venture. It is also executed a hydrocarbons sales agreement between the mixed joint venture and the PDVSA affiliate, usually PDVSA Petróleo, S.A., as the company that will acquire the crude oil and associated natural gas for its sale in the international market in the case of the crude.

It is important to mention that the mixed joint venture shall have a maximum term of twenty-five (25) years, with a possible extension of fifteen (15) years, in accordance with article 34 of the LOH. The extension has to be requested to the National Assembly after half of the initial term has elapsed for the performance of the primary activities and five (5) years prior to its expiration date.

IV. Commercialization of natural hydrocarbons, payments of royalties and special taxes

The current business model contemplates a commercialization reserve in favor of wholly-owned State entities, to the detriment of mixed joint ventures for commercializing the crude oil produced by them, in accordance with article 57 of the LOH. Accordingly, the mixed joint ventures must sell the crude oil to the State entities created in accordance with article 27 of the LOH. In any case, such production shall be subject to a royalty in favor of the Republic equivalent to thirty percent (30%) of the volumes of the extracted hydrocarbons, which rate may be reduced upon the decision of the National Executive to twenty percent (20%) in mature or Orinoco Belt extra-heavy oil projects, aiming at achieving the financial feasibility of the exploitation, in accordance with article 44 of said Law.

Even though this essay does not deal with tax obligations, we should add that mixed joint ventures are obligated to pay the following special taxes set forth under 48 of the LOH: Superficial tax, own consumption tax, general consumption tax and extraction tax.

V. Commercialization of refined products

By virtue of *Presidential Decree N° 1.636* of 2002 the export and import activities of hydrocarbons by-products that are currently done by wholly-owned State entities (i.e., gasoline, gas oil, diesel, jet fuel), must be made in the same way, until the National Executive decides otherwise with respect to one or more of such by-products for the international commercialization, in accordance with article 58 of the LOH.

Furthermore, said article 58 does allow vertically integrated mixed joint ventures upstream/downstream dedicated to the production and refining of natural hydrocarbons to export nationally produced by-products, as long as there is no reservation in place as the one provided for under *Presidential Decree N° 1.636*.

VI. Mixed joint ventures and their relationship with PDVSA

In the context of functionally decentralized State enterprises, there are juridical forms of a pure nature embracing a typical public law regime (i.e., autonomous institutes, public institutes - agencies), along with decentralized entities that carry out industrial and commercial activities with a blended legal regime of public law and private law (i.e., State companies).

Petróleos de Venezuela, S.A. (PDVSA) is a State company created by means of a presidential decree in 1975, with the form a stock corporation, in accordance with article 200 of the Commerce Code, wholly-owned by the State, since its shares belong completely to the Republic, being a first degree State company. On the other hand, affiliated companies of Petróleos de Venezuela, S.A. (PDVSA), are also public capital entities, although their shares do not belong directly to the Republic but to PDVSA, the holding corporation that has the authority to direct, coordinate, supervise and control the activities of its affiliates. In accordance with article 107 of the Organic Law for the Public Administration, since there are various States entities in the oil industry, the National Executive has established holding companies of the State entities, with corporate functions acting as headquarters.

Accordingly, PDVSA has a first level of control and supervision in its holding company role, with a mandate over the rest of the oil industry companies and shareowner of its affiliated companies – as PDVSA Petróleo, S.A. (PPSA). Afterwards, there is a second level in the corporate structure represented by the affiliated companies of PDVSA, in which the Republic indirectly owns one hundred percent (100%) of the shares due to the fact that PDVSA is the holder of the totality of the shares – as is the case of the aforementioned PPSA, which is considered a second degree State company. Finally, there is a third level of State companies, represented in upstream oil mixed joint ventures, as States companies with a majority of the shares owned by the State in accordance with the LOH, in which the shareowners are affiliated companies of PDVSA, basically, Corporación Venezolana del Petróleo, S.A. (CVP) and PDVSA Social, S.A.

VII. Applicable regulations to mixed joint ventures

State entities, mixed joint ventures among them, are subject to a legal regime in which private regulations prevail, except for the norms established under the LOH and other laws addressed to the public sector. For such reason, they must comply with the regulations set out in the Commerce Code, the Civil Code and the Labor Organic Law for Workers with regards to contract execution and performance. In addition, mixed joint ventures have to comply with special public law regulations concerning organization, control, procedures, contracting, indebtedness and liabilities, as long as such enterprises are included within the scope of such laws. The main public law regulations that we have identified for mixed joint ventures' analyses are the following:

1. Organic Law of Public Assets

In accordance with article 4 of said Law, mixed joint ventures form part of the public sector in their condition of State entities, that is, legal entities incorporated under private law regulations, in which functionally decentralized public entities identified therein, solely or jointly, have a participation greater that fifty percent (50%) in the capital stock. Consequently, their goods and assets are qualified as public assets.

2. Law of the General Comptroller's Office of the Republic and the National System of Fiscal Control

Pursuant to article 9 of the Law of the General Comptroller's Office of the Republic and the National System of Fiscal Control, mixed joint ventures are subject to its regulations, and the directors of such enterprises must file an annual sworn statement of their assets, in accordance with article 23 of said Law.

3. Anticorruption Law

For purposes of article 4 of the Anticorruption Law the resources handed over to the mixed joint ventures are considered public resources. Furthermore, the administrators and directors of these enterprises are considered public employees, in accordance with article 3 of said Law.

4. Organic Law for the Public Administration

It is worth ratifying that mixed joint ventures are considered State entities, since a functionally decentralized public entity holds a participation greater than fifty percent (50%) in the capital stock, in accordance with article 103 of the Organic Law for the Public Administration. Furthermore, those mixed joint ventures have to comply with the labor bargaining agreement executed between PDVSA and the labor unions, in addition to the ordinary labor legislation, in accordance with 108 of said Law.

5. Organic Law for the Financial Administration of the Public Sector

Mixed joint ventures are subject to the public credit special regime in accordance with article 5 of the Organic Law for the Financial Administration of the Public Sector, since it is a third degree State entity. In any event, the companies created in accordance with the Hydrocarbons Organic Law are expressly excluded from the authorization prerequisites set forth under said Organic Law for the Financial Administration of the Public Sector as stated in article 101, for which reason, in principle, these mixed enterprises do not require the authorization of the National Assembly and the opinion of the Venezuelan Central Bank in the case of public credit operations.

Article 104 of the Organic Law for the Financial Administration of the Public Sector prohibits the Republic and the companies which their main object is not the financial activity, to grant guarantees to back third party obligations, except in the cases authorized for work concessions and national public services. On the other hand, PDVSA and the companies created under LOH are entitled to grant guarantees and securities taking into account that they are excluded from Title III of said Organic Law for the Financial Administration.

6. Public Contracting Law

The Public Contracting Law governs the hiring processes with regards to goods, works and services of entities and agencies of the public administration.

In the event of mixed joint ventures we should ratify that they are third degree State entities, in which the major shareholder is a second degree State entity, that is, Corporación Venezolana del Petróleo, S.A. (CVP). In view of these facts, we are of the opinion that the Public Contracting Law is not applicable to mixed joint ventures, since they are excluded from the subjective scope in accordance with article 3, that is, only first degree and second degree State entities are subject to the regulations of said Law. However, in practice, we have noticed that mixed joint ventures follow the regulations set out under the Public Contracting Law.

7. Constitutional Law on Productive Foreign Investment

The Constitutional Law on Productive Foreign Investment wasenacted by the Constituent National Assembly, assuming the legislative powers of the National Assembly. Under article 22 of said Law there is a program of special benefits granted to foreign investors that have agreed to a foreign investment contract (also known as legal stability contract), following the fulfillment of certain objectives. Some of the contractual benefits for investors may include: Accelerated amortization, tax reliefs, customs and tax exemptions. On the other hand, the individuals and entities subject to this Law are entitled to remitting abroad profits, dividends and income.

8. Bilateral Treaties for the Promotion and Protection of Investments

Several Bilateral Investment Treaties have been signed by Venezuela with other nations and ratified by the National Assembly and the extinct National Congress, by means of the relevant approving laws, in accordance with article 154 of the Constitution in force and article 128 of the 1961 Constitution. Such treaties protect and promote investments by the nationals of the signatory parties, acknowledging fair and equal treatment, as well as the right of compensation in the event of expropriations. The aforementioned Constitutional Law on Productive Foreign Investment has no real impact on the Bilateral Investment Treaties in force, thus, foreign investors will be protected by the benefits and right conceded therein. As a result, they may have access to the international arbitration mechanisms with respect to the investments made in the mixed joint ventures, as long as the arbitration is contemplated under the relevant Bilateral Investment Treaty that the investor could justifiably invoke.

Even though Venezuela denounced and withdrew from the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, by means of which it was created the International Centre for Settlement of Investment Disputes (ICSID), to

which it was a party up until 2012, the rulings arising out of the arbitrations before ICSID must be complied with by the Nation and the investors, as long as such rulings are based on a Bilateral Investment Treaty or it relates to investments made prior to Venezuela's exit from ICSID.

9. Commercial Arbitration Law

In our view, mixed joint ventures as third degree State entities are not subject to the requirements set out under article 4 of the Commercial Arbitration Law, since such norm refers to first degree and second degree State entities. For such reason, arbitration clauses contemplated under commercial, financial and services agreements executed by mixed joint ventures do not require the prior approval of the competent corporate body of the joint venture nor the prior authorization of the Ministry in charge of oil matters, that is, the Ministry of the Popular Power of Petroleum. In practice, however, we have noticed that the Ministry in charge of the oil industry effectively authorizes mixed joint ventures to execute arbitration clauses.

10. Stock Market Law

The Stock Market Law governs the stock markets in Venezuela, which includes the individuals and legal persons that have a role in the emission, custody, investment, securities' brokerage processes, as well as in connected or related activities. In accordance with article 2 of said Law, the public debt bonds and credit bonds issued in accordance with the Central Bank of Venezuela Law, the Banking Sector Institutions Law and the National System for Savings and Loans Law, are excluded from its application, as well as in any law that expressly excludes them. According to article 46 of the Stock Market Law, securities are defined as those financial instruments representing property or credit rights, over the capital of a commercial entity, issued for the short, mid or long term, and in mass, possessing similar features and granting the same rights within their class.

It is important to point out that pursuant to article 4 of said Law, the intermediation includes public sector securities, that is, those issued by agencies and entities of the public administration, of which mixed joint ventures are part of. According to such norm, for the purpose of performing national public debt bonds' brokerage functions or maintaining a public debt bonds' portfolio, all individuals and legal persons, must request a special authorization from the National Superintendence for Securities.

11. Environmental Organic Law

Articles 84 and 85 of the Environmental Organic Law require the preparation of an environmental impact study by the promoters of any project that may degrade the environment with the relevant authorization by the Ministry in charge of environmental matters, in conformity with the plans for the ordering of the territory.

Such study is an essential technical document that lays out the basis of the environmental and social assessment with a preventive nature, containing the various elements that allow the parties to make the decisions in view of the environmental and social implications of each project.

12. Income Tax Law

In accordance with articles 11 and 53 of the Income Tax Law, mixed joint ventures are subject to such tax in connection with their annual available net income for oil exploitation activities with a fifty percent (50%) tax rate. However, Petróleos de Venezuela (PDVSA), its affiliates and oil mixed joint ventures were exonerated from the payment of income tax for the period of one year, pursuant to Presidential Decree N° 4,106 of 2020. The exoneration set out therein applies for the fiscal year corresponding to January 1 to December 31 of 2019. It is the second year in a row that such exoneration has been issued.

13. Presidential Decree N° 2.777

Presidential *Decree N° 2.777* of 2017 sets forth under article 1 a foreign currency centralization policy for the public sector, establishing that Venezuelan State entities and companies must keep its foreign currencies' offshore accounts solely in Banco Central de Venezuela or Banco de Desarrollo Económico y Social de Venezuela (BANDES). It further establishes the obligation to contribute to the so-called Foreign Currency Productive Fund. On the other hand, article 3 of said Decree determines an exemption in favor of Petróleos de Venezuela, S.A. (PDVSA) and its affiliated companies with respect to the aforementioned obligations.

This regulation has brought the attention of mixed joint ventures, as decentralized State entities, bringing the question as to whether they have to comply with the obligations under Decree N° 2,777. The position that we understand has been assumed by the National Executive, which is an opinion that we do not share, is that mixed joint ventures are affiliated companies of PDVSA, and as such, exempted as well from complying with this regulation.

14. Exchange Agreement N° 1

The Constituent National Assembly enacted the Law Abrogating the Law on Foreign Exchange Illegal Acts, assuming the legislative powers of the National Assembly. Said Law purports to decriminalize the foreign exchange market operations. On the other hand, Exchange Agreement N° 1 of 2018 executed between the Venezuelan Central Bank ("BCV") and the Ministry of the Popular Power of the Economy and Finance sets forth the regulatory framework for the Venezuelan foreign exchange market, abrogating the Exchange Agreement N° 9 that used to govern the oil industry.

This Exchange Agreement N° 1 contemplates a new foreign exchange policy, establishing the currency free convertibility, ceasing the restrictions on foreign exchange operations, for which reason centralizes on BCV the acquisition and sale of foreign currencies coming from the public administration and the exportation activities of private parties. Thus, in theory, loosens up on the foreign exchange control regime.

According to article 44 of said Exchange Agreement, mixed joint ventures referred to under LOH are allowed to maintain foreign accounts in banking institutions, foreign or national, for the purpose of the income received, as well as for making the corresponding offshore payments and disbursements. The remaining foreign currency is of compulsory sale to the Central Bank of Venezuela. Mixed joint ventures are not entitled to acquire foreign currency from the BCV for the purpose of complying with their obligations and payments in foreign currency.

Conclusions

At present, private investments in the upstream oil industry has to be done through the mixed joint ventures, in which projects, as we know, the private parties are always minority shareholders, in view of the semi-open economic model set forth under the LOH. This Law is based on the concept of oil sovereignty by means of a critical State intervention in the industry, and as a result, the implementation of a non-successful public policy that implies major investments, major risks and major returns to the Nation. As we pointed out in this brief article, upstream oil mixed joint ventures are subject to a number of important regulations that are the common feature of State entities incorporated as commercial companies, with the combination of a private law and public law regime. It has been shown that these public law regulations are not attractive to the private parties at all.

To sum it up, we believe that in current times there is the need to new and substantial private oil investments in the country, with novel contractual and financing schemes, along with new technologies and involvement of qualified personnel. Therefore, we think that it should be formally instituted a friendly open model, different from the oil joint ventures controlled by the State, by means of a legal oil reform with solid legal grounds that now looks more than necessary, aiming at promoting intensive capital investments in the industry in the coming years.

STATE'S EQUITY PARTICIPATION AND TAXATION IN THE ACTIVITY OF HYDROCARBONS IN VENEZUELA (REFLECTIONS AND IDEAS FOR A REFORM)

ELINA POU RUAN*

Introduction

From the 20th century onwards, most precisely between the 1920s and 1930s, oil activity in Venezuela became the largest source of rental income, bringing with it the neglect and/or annihilation of other sectors of the economy, which led to the modeling of an oil-producing country in the collective, social, and political imaginary. A fact that contributed to the assembly of a set of representations that determined the development and evolution of policies towards that sector[1]; and that today, due to its dramatic decrease and important deterioration of its infrastructure, it requires urgent legislative reforms for its restructuring or reorganization. In this sense, in the opinion of a great majority, said reorganization supposes "a greater participation of the private capital, in parallel to a greater control of the operations on the part of this sector, for managerial and technical decision-making, with the consequent contribution of technology and qualified personnel."[2]

In this context, it is essential to review the scheme of state's equity participation in parallel with a comprehensive reform of the tax system to simplify it, make it fairer, less punitive, and more competitive. Due to the impact that this could have on the attraction of private capital required to make the large investments that the hydrocarbon sector demands for its recovery and industrialization, this article will show a summary of the tax and royalty regime, as provided for in the current legislation, followed by some reflections and ideas for its reform. Not without noting that this article does not cover the analysis of the multiplicity of factors and variables that impact this sector currently, such as the drastic decline in prices and demand for all hydrocarbons, as well as the increasingly strong global trend to replace them with cleaner energy sources.

I. State's equity participation in the activity of hydrocarbons

In Venezuela, the subsoil and its riches belong to the Republic, which determines that those to whom the sovereign State grants or assigns the right to explore and exploit the mining and hydrocarbon deposits must pay a patrimonial participation. This concept is based on the consideration that not even the owner of the land can acquire or use the wealth derived from the subsoil, which are considered public property, inalienable and imprescriptible.

1. Royalties

From there arise the royalties as consideration due for the use or exploitation of a good owned by the Nation.

A. Case of natural and refined hydrocarbons and associated gas, whose royalty regime is governed by the provisions of the Organic Law on Hydrocarbons (LOH)[3]

Of the hydrocarbons extracted from any field, the State has the right to a thirty percent (30%) share as a royalty, and the National Executive may reduce it to twenty percent (20%) for mature fields or extra-heavy oil fields in the Orinoco Belt, when it is demonstrated that it is necessary to reduce the rate for reasons of the project's economic viability; and it is also authorized to return it, in whole or in part, until it reaches thirty percent (30%) again, when it is demonstrated that the project can be maintained with such return.

The royalty may be demanded in kind or in money, in whole or in part. As long as it is not demanded in any other way, it will be understood that it is chosen to receive it totally and in money.

* Elina Pou Ruan is a partner at LEĜA Abogados. Lawyer graduated from Universidad Católica Andrés Bello, (1987). Specialist in Tax Law from Universidad Central de Venezuela, (1997). Member of the Venezuelan Association of Tax Law (AVDT) and its Board of Directors, (2017-2019).

[1] In order to deepen the study of the representations of the oil fact, converted into "imaginary keys" that have prevented the dismantling of the rentier model throughout the years preventing its industrialization and the reception of the transnational capital, without "complexes and victimization", see Nelly Arenas, La Venezuela rentista: imaginario político y populismo, Cuadernos del Cendes, 29 (80), 2012, 137-145, http://ve.scielo.org/scielo.php?script=sci_arttext&pid=S1012-25082012000200007&lng=es&tlng=es.

[2] Simón Herrera Celis, "Algunas notas sobre el régimen jurídico de PDVSA, de cara a una eventual reorganización de la industria de los hidrocarburos", 2020, consulted in original.

[3] Organic Law on Hydrocarbons (LOH), Official Gazette N° 38.493 dated 04-08-2006, articles 44, 45, 46 and 47.

When it is decided to receive the royalty in kind, the transport, storage and services of the operating company may be used, which must provide them to the place indicated by the National Executive, who will pay the price agreed upon for such services.

When it is decided to receive the royalty in money, the operator must pay the price of the corresponding volumes of hydrocarbons, measured in the field of production and at market value, or at an agreed value or, in the absence of both, at a fiscal value set by the liquidator. For such purpose the competent Ministry shall liquidate the corresponding schedule, which must be paid to the National Treasury within five (5) working days following the receipt thereof.

B. Case of gaseous hydrocarbons, whose royalty regime is governed by the provisions of the Organic Law on Gaseous Hydrocarbons (LOHG)[4]

The conditions of the royalties foreseen for gaseous or liquefied hydrocarbons (not associated with oil), are practically identical to those described above, with the difference of a twenty percent (20%) rate and the only option of pricing the volumes at market value in the production field.

2. Special advantages in favor of the Republic

It is a figure that incorporated the LOH of 2006[5] for the case of mixed companies, indicating that at the time of their constitution they must inform "...all the circumstances pertinent to said constitution and conditions, including the special advantages foreseen in favor of the Republic.

The current configuration of these special advantages can be found in the Agreement on the Model Contract for Joint Ventures, whose terms, and conditions, with respect to this aspect, were reformed in September 2009[6] :

A. Additional royalty of three-point thirty-three percent (3.33%)

Calculated on the volumes of hydrocarbons produced in the delimited area, which will be distributed as follows: (i) one point eleven percent (1.11%) which will be distributed as follows: thirty percent (30%) of said percentage in equal parts to the municipalities where the primary activities of the mixed company are carried out, and the remaining seventy percent (70%) to the other municipalities where oil activities are carried out in proportion to the population, and (ii) two point twenty-two percent (2.22%) for a Special Fund administered by the National Executive dedicated to developing endogenous development projects.

B. Shadow tax

A colloquial name given to a levy that seeks to ensure that the State always receives at least fifty percent (50%) of the total income of the projects from the production of crude oil.

For its calculation, the Agreement refers to discounting: (i) fifty percent (50%) of the value of the hydrocarbons extracted in the delimited area, obtained in the calendar year (price sold to PDVSA or its affiliates) and (ii) the sum of all payments made for royalties (including the 3.33%), for income tax, special taxes provided for in the LOH, one percent (1%) invested in endogenous development projects and that paid for any other tax calculated on the basis of income (whether gross or net). This last point would allow us to think that contributions for sudden profits and the diversity of parafiscal contributions, such as those foreseen for science, technology and innovation, sports and drugs, which we will see later, would be discounted.

In other words, the sum of the payments for royalties, income taxes, and others, must be at least equal to 50% of the value of the hydrocarbons produced and, in the event of a deficit, the joint venture is obliged to pay such deficit. Please note that this 50% is not considering the indirect right that the State has as a shareholder of the mixed enterprise in the dividends.

II. Tax regime applicable to the activity of hydrocarbons

This section provides an overview of the general tax regime applicable to all taxpayers, including those in the hydrocarbon sector. To this end, the most relevant aspects of each tax will be highlighted, both the special taxes that are only applicable to this sector and the general ones. It should be noted that the purpose of this article is not to provide a detailed analysis of the tax regime, since this requires an extensive development, both from a constitutional and a legal perspective, which can be found in very specialized manuals. [7]

For the purposes of the analysis of the tax regime that we have proposed, the distinction made by the hydrocarbon legislation in force will be taken into account, in relation to (i) primary activities in the field of liquid hydrocarbons (crude oil), solids, semi-solids and associated natural gas, known in the industry as "upstream" activities, which include exploration, extraction of hydrocarbons in their natural state, their collection, transportation and initial storage, in which private capital may participate in mixed companies together with the

[4] Organic Law on Gaseous Hydrocarbons, G.O. 36.793 of 12/09/1999, article 34.
[5] LOH, article 33.
[6] Agreement for the approval of the modification of the Terms and Conditions for the Creation and Operation of Mixed Companies contained in the Contract Model, G.O. 39.273 of 28/09/2009. The first Agreement of the Terms and Conditions, together with the Model was published in the G.O. 38.410 of 03/31/2006.
[7] Juan Cristóbal Carmona Borjas, Hidrocarburos y Minerales, Derecho y Finanzas, Volumen II (Actividad Petrolera y Finanzas Públicas en Venezuela), Caracas 2016.

majority shareholding of the Venezuelan State[8] , or exclusively for the exploration and exploitation of non-associated gaseous hydrocarbons, due to the granting of licenses by the Ministry with competence to do so[9] , and (ii) non-primary refining and industrialization activities, called "downstream" or "intermediate waters", in which their execution by the private sector is allowed without the participation of the State. [10]

In the same sense, it will be relevant to bear in mind the activities that the current legislation has reserved to the Venezuelan State, such as the case of the internal market of fuels such as gasoline and diesel, which to date has been forbidden both to the private sector and to mixed enterprises. [11]

1. Special taxes provided for in the Organic Law on Hydrocarbons

Special taxes applicable to activities with natural and refined hydrocarbons (oil and associated gas):

A. Surface Tax

It is a tax that is created to prevent the fields that are given up from remaining idle. It is caused by the unexploited surface area, equivalent to one hundred tax units (100 TU) for each square kilometer per year or fraction thereof. The tax is increased annually by two percent (2%) during the first five years and five percent (5%) in subsequent years. [12]

B. Own Consumption Tax

Equivalent to ten percent (10%) of the value of each cubic meter (m3) of hydrocarbon by-products produced and consumed as fuel in operations, based on the sales price to the final consumer. If such product is not sold in the national market, the competent Ministry shall set its price.

C. General Consumption Tax

For each liter of product derived from hydrocarbons, sold in the internal market, a tax is caused between thirty and fifty percent (30% and 50%) of the price paid by the final consumer, whose aliquot between both limits will be fixed annually in the Budget Law. This tax, which shall be paid by the final consumer, shall be retained at the source of supply to be paid monthly to the National Treasury. The National Executive may exonerate this tax, totally or partially, for the time, in fact, it is a tax that in practice has not been applied.

D. Extraction Tax

The extraction tax is one third (33.33%) of the value of all liquid hydrocarbons extracted from any field. This tax is paid monthly and is calculated on the same basis as the royalty that is paid in cash. In calculating the extraction tax, the taxpayer is entitled to deduct any amount paid as royalty, including that paid for special advantages. The National Executive may, under certain conditions, reduce the amount to a minimum of twenty percent (20%) for extra-heavy oil projects.

E. Export Registration Tax

This tax is equivalent to zero-point one percent (0.1%) of the value of all hydrocarbons exported from any national port. The taxable base is determined based on the sales price. For this purpose, the seller shall inform the competent Ministry of the volume, API grade, sulfur content and destination of the cargo and shall submit a copy of the relevant invoice within 45 days from the date of export.

All excise taxes, exceptfor the General Consumption Tax, are deductible for income tax purposes.

2. Special contributions for extraordinary and exorbitant prices in the international market of hydrocarbons [13]

As a result of the rise in oil prices and its derivatives, which occurred with greater intensity between 2006 and 2008, a period in which prices exceeded $140 per barrel, a law was passed that created a tax on sudden and unexpected profits, which was called "special contribution for extraordinary and exorbitant prices". This law underwent three subsequent modifications, through Decree-Laws issued in 2011, 2012 and 2013, the last of which is still in force.

A. Contributions on extraordinary and exorbitant prices, payable monthly, are applied to exporters of liquid hydrocarbons, both natural and improved and derived products. Also, to mixed companies that sell liquid hydrocarbons, both natural and improved, and derivative products to PDVSA and any of its affiliates.

B. The extraordinary price is defined as that which exceeds those whose monthly average of the international quotations of the Venezuelan liquid hydrocarbon basket is greater than the price established in the Budget Law of the respective fiscal year, but equal to or less than eighty dollars per barrel (80 US$/b).

[8] LOH, artícle 9.
[9] LOHG, artícle 24.
[10] " I would like to highlight the opinion of those who confirm that the constitutional framework allows for the total opening to the private sector as long as the management of the hydrocarbon industry continues to fall on Petróleos de Venezuela, S.A. or on the entity that will be created for such purposes; thinking that "...such management must be understood as the supervision, coordination and control of the industry, which includes the powers to bid, select and manage the projects with private investors in their different associative and contractual schemes". See: Simón Herrera Celis, “Algunas notas sobre el régimen jurídico de PDVSA, de cara a una eventual reorganización de la industria de los hidrocarburos”, 2020. cit.
[11] Organic Law for the Reorganization of the Internal Market of Liquid Fuels, G.O. 39.019 of 09/18/2008.

When the monthly average of the international quotations of the Venezuelan liquid hydrocarbon basket is higher than the price established in the Budget Law of the respective fiscal year, but equal to or lower than eighty dollars per barrel (80 US$/b), a twenty percent (20%) rate will be applied on the difference between both prices.

C. The exorbitant price is the one whose monthly average of the international quotations of the Venezuelan liquid hydrocarbon basket is higher than eighty dollars per barrel (80US$/b).

The rate applicable to the contribution for exorbitant price has the following sections: (i) exorbitant prices greater than eighty dollars per barrel (80 US$/b), but less than one hundred dollars (100 US$/b), an aliquot equivalent to eighty percent (80%) of the total amount of the difference between both prices will be applied; (ii) exorbitant prices equal to or greater than one hundred dollars per barrel (US$100/b), but less than one hundred and ten dollars per barrel (US$110/b), an aliquot equivalent to ninety percent (90%) of the total amount of the difference between both prices shall be applied; and (iii) exorbitant prices equal to or greater than one hundred and ten dollars per barrel (US$110/b), an aliquot equivalent to ninety-five percent (95%) of the total amount of the difference between both prices shall be applied.

3. Income Tax

Income tax[14] is levied on net and available annual income (excluding those exempted and exonerated), from foreign or local sources, obtained by natural and legal persons, considered resident and domiciled in the country, according to the legally established parameters. Non-domiciled or non-resident persons will be subject to the tax provided that the source or cause of the enrichment is or occurs in Venezuela, and in case they have a permanent establishment or a fixed base in the country, they will be taxed exclusively on the income from domestic or foreign sources attributable to such permanent establishment or fixed base.

A. CDT or accreditation

In the absence of a Double Taxation Agreement, the credit provided for in the Law is applicable, which allows those who have a permanent establishment or fixed base in the country to credit against local income tax the same tax that they have paid abroad for the enrichment of extraterritorial source, only in the proportion that the net enrichment of foreign source represents in the total of the overall net enrichment.

B. Rates

Taxpayers engaged in the exploration and exploitation of oil and associated gas, and related activities such as refining and transportation, or the purchase of hydrocarbons and their derivatives for exploitation purposes, are subject to a fixed tax rate of fifty percent (50%).

Companies exclusively engaged in the refining of hydrocarbons or the upgrading of heavy and extra-heavy crude oil, or those engaged in the exploration and/or exploitation of non-associated gas, the processing, transportation, distribution, storage, marketing and export of gas and its components, are subject to the generally applicable progressive tax rate, with a maximum rate of thirty-four percent (34%).

C. Deductions

Costs and expenses incurred in Venezuela, normal and necessary to produce the enrichments, including royalties and other taxes paid, will be deductible. Expenses incurred abroad are not deductible, except for the following: a) expenses related to the generation of income from foreign sources or export sales; b) fees for technical assistance and technological services performed abroad and used in Venezuela; and c) a "reasonable" allocation of general management and administration expenses incurred abroad charged by the foreign parent company to the local branch or permanent establishment.

[12] t should be noted that the value of the current TU, which does not reflect real accumulated inflation levels, is Bs. 1,500 per TU, which represents an approximate amount of US$ 0.15 per square kilometer (assuming a value of Bs. 1,000,000 per bolivar).
[13] Law that creates Special Contribution for Extraordinary Prices and Exorbitant Prices in the International Hydrocarbon Market, G.O. 40.114 of 02/20/2013.

D. Depreciation and amortization

The primary method of depreciation is straight-line, which should be used unless the law permits the use of another method. This is the case of taxpayers engaged in the exploitation of hydrocarbons and related activities, such as refining and transportation, who will use the depletion method.

Amortization is deductible only when the relevant area is in production and with respect to assets located in the country. Amortizable capital investments include a) the cost of the licenses granted, including the acquisition price and related expenses; b) direct expenses for exploration, topographic studies and other similar activities; c) a reasonable share of other indirect expenses incurred in the operations of the fields; and d) any other expense that may be characterized as a permanent investment.

The basis for the amortization of direct exploration costs is the unamortized investment cost, the total recoverable reserves in proven areas and the total production of the company.

Drilling and other development costs, whether for tangible or intangible items, should be amortized using the depletion method. Dry wells may be capitalized or expensed in the current year.

E. Availability of exchange rate gains or losses

Gains or losses arising from the adjustment of assets or liabilities denominated in foreign currency or with an exchange rate adjustment clause are considered available in the fiscal year in which the consideration relating to such assets or liabilities occurs, whether due, collected or paid, whichever occurs first. Therefore, assets or accounts receivable denominated in foreign currency are not automatically adjustable for exchange rate changes at the end of the tax period, nor are they taxable or deductible as losses.

F. Loss regime

The imputation of losses of extraterritorial source to enrichment or loss of territorial source will not be admitted. The carry-forward period for tax losses is three years. No refund of tax losses is allowed.

G. Transfer Pricing

Taxpayers who conduct transactions with related parties are subject to transfer pricing rules and therefore are required to calculate their income and costs for such transactions based on the prices and methods that would be used if the transactions were conducted between independent entities in comparable transactions.

Entities are considered "related" in the following cases: a) if one entity participates, directly or indirectly, in the administration, control or assets of the other; b) if the same persons participate, directly or indirectly, in the administration, control or assets of both entities; and c) it is presumed, unless proven otherwise, that the entities are related if they are located in low tax jurisdictions.

During the month of June of each year, taxpayers must report to the Tax Administration, all transactions with related entities executed within the previous fiscal year.

Finally, it is important to note that transfer pricing rules apply only with respect to cross-border (international) transactions. Therefore, the domestic sale of hydrocarbons to Petróleos de Venezuela, S.A. (PDVSA) or its affiliates, by a mixed company, would not be subject to the transfer pricing rules.

H. Undercapitalization

Under these rules, interest paid directly or indirectly by a taxpayer to a related party is deductible only to the extent that debt to related parties, when added to debt to unrelated parties, does not exceed the taxpayer's net worth (1:1 debt-to-equity ratio).

The portion of related party debt that exceeds the 1:1 ratio should be considered as "taxable equity" and the associated interest is considered non-deductible for income tax purposes.

I. International Fiscal Transparency Regime

Taxpayers with direct or indirect investments in branches, companies, real estate, personal property, shares, bank accounts, investment accounts or participation in other similar entities, trusts, investment funds or investments of similar nature in tax havens, are subject to the transparency rules. All transactions with entities located in low tax jurisdictions are presumed to be related party transactions and therefore subject to Venezuelan transfer pricing rules (including thin capitalization). Taxpayers subject to tax transparency rules are required to file an annual information return on the investments they have made or maintain during the year in low tax jurisdictions, accompanying the statements of account for deposits, investments, savings or any other document that supports the investment.

J. Tax withholdings

Withholding agents are required to withhold tax on almost all payments to third parties (except most sales), in percentages ranging from one percent (1%) to five percent (5%), and the taxpayer bearing the withholding may credit the full amount of such withheld tax against his or her final tax liability for the period.

[14] Income Tax Law, G.O. 6.210 of 12/30/2015.
[15] Decree No. 3.569, G.O. 41.452 of 02/08/2018 and Decree No. 4.106, G.O. 41.809 of 01/28/2020.

In the case of cross-border payments, such as interest, technical assistance payments, and royalties, withholding usually equals the final tax liability. The effective tax rates (assuming the maximum rate of 34%) that are applicable are as follows: a) royalties: 30.6% (34% on assumed income of 90%); b) technical assistance: 10.2% (34% on assumed income of 30%); c) interest paid to creditors other than financial institutions: 32.3% (34% on assumed income of 95%); and d) interest paid to financial institutions: 4.95%.

K. Capital Gains Tax

In a tax proportional to the dividends originated in the net income of the payer that exceeds its net taxable income. Such tax must be withheld by the payor at the time of distribution; therefore, the tax is designed to tax distributed earnings not taxed at the level of the entity generating the earnings.

Dividends paid by a company engaged in the exploration, exploitation, refining and transportation of oil and associated gas, or the purchase of hydrocarbons and their derivatives for exploitation purposes, are subject to a fixed rate of 50%, of the remainder a fixed rate of 34% is applied.

L. Decrees exempting PDVSA, its subsidiaries and joint ventures from the payment of income tax (fiscal years 2018 and 2019)

For fiscal years 2018 and 2019, the National Executive has exonerated the payment of income tax for territorial or extraterritorial enrichments obtained by PDVSA, affiliated companies and mixed companies domiciled or not domiciled in Venezuela, from hydrocarbon production activities. [15]

It has been expressed in these Decrees that the objective of such fiscal benefits is to increase the productive capacities of the oil sector, to reestablish the levels of hydrocarbon production of the national oil industry, as well as to comply with the plans for research and development of new technologies. [16]

4. Value Added Tax[17]

A. General considerations

(i) The general VAT rate (between 8% and 16.5%) applies to imports and most sales of goods and services.

(ii) Exports of goods and services are taxed at a rate of zero percent (0%).

(iii) There is a rate for luxury consumption (between 15% and 20%), in addition to the general rate, applicable to the goods indicated in the Law.

(iv) An additional rate (between 5% and 25%) was created applicable to goods and services paid in foreign currency, crypto-currency or crypto-assets other than those issued and supported by the Republic. It has not been applied yet because the National Executive has not issued the decree to fix the rate. Such rate is not applicable to the entities of the National Public Administration with or without business purposes.

(v) The tax rate applicable to sales of natural hydrocarbons made by mixed companies, regulated in the LOH, to PDVSA or any of its affiliates will be zero percent (0%).

(vi) An eight percent (8%) rate is applicable to services rendered to the public authority, in any of its manifestations, in the exercise of professions that do not involve the performance of acts of commerce and involve predominantly intellectual work or action.

(vii) This monthly tax uses a debit system (VAT on sales of goods and services) against credit (VAT on imports and internal purchases of goods and services).

(viii) In service imports, the importer is responsible for paying the VAT on behalf of the non-domiciled entity in Venezuela, which becomes a credit for the importer.

(ix) The taxpayer must file a monthly return and the excess credit, if any, is carried forward to subsequent periods.

(x) Special taxable persons must apply VAT withholding (75% of VAT). Such withholding is applied by the payer who acquires goods or is the recipient of a service.

B. Incentives for industrial projects

Taxpayers dedicated to the execution of industrial projects for more than six (6) tax periods may suspend the compensation of input VAT, generated in the pre-operational stage, to the first tax period in which the first tax liability is generated. Such debits may be adjusted by the inflation index (IPC).

Taxpayers dedicated to the execution of industrial projects essentially oriented to exports can recover the tax credit generated in the pre-operational stage.

C. Exemption from VAT, Import Tax and Customs Regime Determination Fee, as well as any other applicable tax or fee (May 2020)

[16] It is worth asking about the magnitude and effectiveness of the fiscal sacrifice in the achievement of the proposed objectives at a time when this industry is going through the lowest production levels ever, with the consequent losses and / or reduced enrichment, even more so when both decrees were issued in the eighth month of fiscal year 2018 and after the closing of fiscal year 2019.

[17] Law establishing the Value Added Tax, G.O. 37.002 of July 28, 2000.

lThe National Executive, by means of Decree No. 4.220[18], issued in May 2020, exempted the payment of VAT, Import Tax and Customs Regime Tax, as well as any other tax or rate provided for in the current legislation, applicable to imports and sales made in the national territory, of fuels derived from hydrocarbons, as well as inputs and additives that improve the quality of gasoline, made by public or private entities. The duration of the exemption is one year.

The Decree urges all public authorities (state and municipal) to adopt measures to extend the exemption to taxes, rates, contributions and other levies that they administer within the framework of their competence, in order to leverage the hydrocarbons industry.

5. Tax on Large Financial Transactions[19]

This tax (IGTF) is levied with a zero point seventy five percent (0.75%), on debits and cancellations of debts of special taxpayers.

The Law establishes a tax exemption for public entities with or without business purposes qualified as special taxpayers, which means that this exemption is applicable to joint ventures.

Becauseof the Decree of 4.220 of VAT exemption in the import and sale of fuels derived from hydrocarbons, the IGTF must not be paid on the occasion of debits to bank accounts or cancellations for fuel purchases, but compliance with certain requirements is required to enjoy the benefit. [20]

6. Tax on Large Estates[21]

It is a tax on the net worth of individuals and legal entities that qualify as special taxpayers, whose assets (in ownership or possession) have a value equal to or greater than one hundred and fifty million tax units (150,000,000 TU).

The Law establishes a tax exemption for functionally decentralized entities, which means that this exemption is applicable to mixed enterprises.

7. State Taxes

States may charge a tax for the services they provide. However, if a national entity providing the service is located in a State that has not enacted a local law for its collection, it will be that entity of national character that will be entitled to receive payment, provided that it is provided for in the National Tax Stamp Act.[22]

The most relevant stamp tax for hydrocarbon projects is the one percent (1%) tax applicable to subscription and capital increase.

8. Municipal Taxes

The most relevant municipal tax is the tax on economic activities, whose rates, applicable to gross income, have been increasing in recent years, due to inflation and the need for resources of these local authorities, but especially those applicable to suppliers of the hydrocarbon industry, much higher than the rest. [23]

The most relevant aspect regarding municipal taxes is the reserve of the National Power of taxation in matters of hydrocarbons, which leads to the impossibility of taxing "upstream" activities of the hydrocarbon sector with such taxes. [24]

9. Parafiscal Contributions

In the last decades, an important number of parafiscal contributions have been enacted, the most relevant being the following:

A. Contribution to Science, Technology and Innovation[25]

Companies whose annual gross income exceeds one hundred thousand tax units (100.000 TU), will pay the following contribution:

a. One percent (1%) over the gross income, in case of private capital companies when the economic activity is one of those contemplated in the Organic Law of Hydrocarbons and the Organic Law of Gaseous Hydrocarbons, as well as those dedicated to mining, processing and distribution.

It could be thought that, even though the intention of the legislator is not clear, it is possible to include in the previous category, among others, companies dedicated to exploration activities in search of non-associated gaseous hydrocarbon deposits and the exploitation of such deposits; as well as the collection, storage and use of both non-associated natural gas coming from such exploitation, and the gas that is produced associated with oil or other fossils; the processing, industrialization, transportation, distribution, domestic and foreign trade of such gases.

b. Five percent (0.5%) of the gross income, in the case of public capital companies when the economic activity is one of those contemplated in the Organic Law of Hydrocarbons and the Organic Law of Gaseous Hydrocarbons, as well as those dedicated to mining, processing and distribution.

The Law does not clarify whether public capital companies are to be understood as those exclusively owned by the Republic, such as PDVSA and its wholly owned subsidiaries, or whether mixed companies are also included in this category.

[18] Exoneration Decree No. 4.220, G.O. 41,890 of May 29, 2020.
[19] Law on Taxation of Large Financial Transactions, G.O. 6.210 of 12/30/2015.
[20] SENIAT ruling N° SNAT/2020/00029, G.O. 41.914 of 03/07/2020.
[21] Constitutional Law creating the Tax on Large Estates, G.O. of 08/16/2019.
[22] Tax Stamp Law, G.O. 6.150 of 11/18/2014.

B. Contribution to Sport[26]

The contribution to be made by companies or other organizations will be one percent (1%) of the net profit or annual accounting profit, when this exceeds twenty thousand tax units (20.000 TU).

C. Anti-drug contribution[27]

Companies that employ 50 or more workers must pay one percent (1%) of the profit or loss in operations for the year to the National Anti-Drug Fund within sixty continuous days from the close of the respective fiscal year.

III. Reflections and ideas for a reform

The recovery of our hydrocarbon industry and the industrialization of the country in general is a priority issue that deserves deep reflections on the size of the State and its role in the economy. Without any doubts, this is something that could favor reforms in public finance policies and in its regulatory framework, to promote greater participation of the private sector, in parallel with the restoration of the independence of the Public Powers and the Rule of Law, with a view to offering greater protection, security and legal stability for investors.

In this sense, it will be necessary to undertake a review of the State's equity participation in the activity of hydrocarbons and a comprehensive reform of the tax system to simplify it, make it fairer, less punitive, and more competitive. But this will be insufficient if the Venezuelan State does not generate confidence and offers a reoriented vision of hydrocarbon policy, which assumes the opening of the business towards private investment, with enthusiasm and without reservations.

The first thing that should be noted is that the large of royalties and taxes that weigh on minority investors that participate in joint ventures with PDVSA, is not the most attractive in the current conditions of the world oil market. Nor is it the best situation compared to other countries of the LATAM region that offer investment opportunities and competitive advantages due to the situation of its economies and its technological and industrial development.

Venezuela is not exactly a tax haven, on the contrary, it is a country with a strong fiscal pressure that deserves to be reviewed in the face of the notable and progressive deterioration of public services and the need to assume the payment of alternative private services. Therefore, if we think about the duty to contribute to public expenditures through the payment of taxes and about the taxable capacity as a measure and of taxation, it is worth wondering if it is justified to maintain this fiscal pressure or if, on the contrary, it could be convenient for the State to assume its reduction. The latter in function of the achievement of extra-fiscal goals of growth and development, through the implementation of a fiscal policy of low tax rates and incentives to attract investment in new technologies and in the long-awaited industrialization of the country.

Similarly, it is necessary to ask to what extent the coexistence of royalties and the various taxes would be slowing or preventing the growth of an industry. In the same way, it would be necessary to ask whether this tax burden brings greater benefits than the generation of wealth, the reinvestment of capital in new capital goods and technological development, the generation of a greater number of jobs, and the multiplier effect towards other sectors and economic agents.

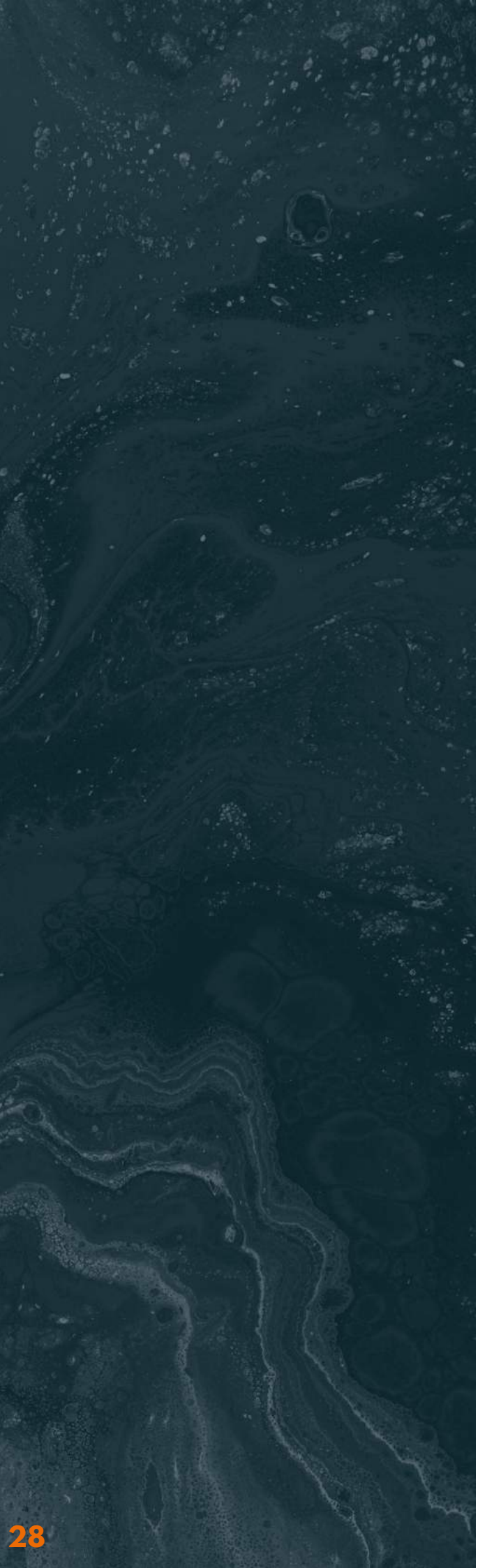
This leads us to compare the royalties with the income tax or with the tax on sudden profits, and to think if it is necessary that all the burdens subsist? What are the benefits or disadvantages of raising or lowering the tax rates? To what extent should one be greater than the other?

In the specific case of royalties, one should ask whether it is worth maintaining rates above 20%, considering both the rapid development of other energy sources in the world, as well as the lower and insufficient production of internal fuel and the need for satisfying the domestic market. It also seems interesting to make the current royalty scheme more flexible, with wider bands between the minimum and maximum limits, to abandon the concept of the sovereign State that yields the exploitation of its wealth in exchange for an invariably fixed income, for a State that negotiates and manages the sustainable development of the country and supports the growth of private and productive enterprise.

Related to the simplification of the tax regime, it is important to review the proliferation of taxes and their incidence on identical or similar manifestations of taxable capacity, such as the duplicated case of the general consumption tax provided for in the Organic Law on Hydrocarbons and in the Value Added Tax Law.

Special mention deserves, the income tax, in which it is necessary to restore the progressiveness of its rates and the system of adjusting for inflation. More than ever, it is justified to allow all taxpayers to determine their income considering the devastating effects of inflation, especially in the situation of hyper-inflation that Venezuela is experiencing, otherwise, fictitious income will be taxed.

[23] On average current rates range from 2% to 5%, however, in the case of suppliers to the hydrocarbon industry they can exceed 10%.
[24] National Constitution 2009, article 156, numeral 12.
[25] Organic Law on Science, Technology and Innovation, G.O. 6.151 of 18/11/2014.
[26] Organic Law on Sport, Physical Activity and Physical Education, G.O. 39.741 of 23/08/2011.
[27] Organic Law on Drugs, G.O. 39.535 of 21/10/2010.



Finally, one may ask whether, in the event of the desired opening, and with a view to the industrialization of the country and not only of the hydrocarbon industry, if it would be justified to continue maintaining a higher tax rate for said sector.

Downstream, it is important to insist on tax harmonization at the municipal level, in order to establish reasonable limits to municipal taxation and specially to avoid unequal and discriminatory treatment of suppliers to the hydrocarbon industry. It is necessary to establish a system of bands for setting the rates that municipalities can charge for the tax on economic activities.

Finally, mention is made of the imbalance that the Organic Tax Code has been suffering, whose punitive profile has been increased in every reform, especially in the latest with the mechanism of updating the fines for the use of the exchange rate of the currency of greatest value at the time of payment. The use of this mechanism with the great loss of the value of the currency generates astronomical fines that are not proportional to the “damage” generated by the taxpayer. In this sense, there must be a reform of the current Code that restores the balance between tax administrations and taxpayers.

As a corollary of the above, the country requires comprehensive reforms for its reconstruction and development, which offers legal security and neutral, competitive, and attractive schemes for investors.

INTERNATIONAL COMMERCIAL ARBITRATION IN THE OIL INDUSTRY

SIMÓN HERRERA CELIS*
JOSÉ ALBERTO RAMÍREZ LEÓN**

Preliminary ideas

Arbitration is an institution that allows in an efficient way and in shorter time periods to solve conflicts within the parameters and restrictions contemplated in the national and international legal systems. Its flexibility is a key feature and differentiates it from the rigidity that identifies the traditional judicial system. Arbitration brings multinational companies closer to the countries that receive investments, without the intervention of a supposedly State monopoly in the administration of justice. However, even though there is an ongoing debate about the suitability of arbitration, in our opinion, this institution contributes to create a climate of confidence in favor of investments. In an oil producing country like Venezuela, eager for new projects and financial resources, this should be highly relevant today.

In international arbitration, a neutral forum other than that of the contracting parties is usually used, so that arbitration awards made outside their borders should be able to be recognized and executed in any of the countries that are signatory parties to the treaties in force. The recognition and enforcement of awards is regulated by the Conventions of Panamá, Montevideo and New York, which are laws in force in Venezuela through the ratification laws issued by the former Venezuelan National Congress, as well as by the Commercial Arbitration Law of 1998. In order to understand the concept of international arbitration, one must first consider the effective application of international treaties with respect to the enforcement of awards issued by international courts, in addition to the nationality of the parties and the place where the arbitration is carried out, if it differs from the substantive law applicable to the substance of the dispute.

In this brief introduction it is necessary to mention that there is a clear conceptual difference between international commercial arbitration and investment arbitration. This article will focus on the first of these two types, not without bearing in mind that investment arbitration which settles disputes between investors and States is a matter of great significance.

I. Basic concepts about the state oil companies in Venezuela

The contracts of the oil industry in any country are multiple and varied by virtue of the complexity and specialty of its activities. In this opportunity we will concentrate on the arbitration of contracts of the Venezuelan oil industry in the exploration and production of liquid hydrocarbons (upstream activities), which can only be carried out by the State, by companies completely owned by the State or by mixed companies, in accordance with article 22 of the *Organic Law of Hydrocarbons of 2001.*

The State companies in the Venezuelan oil industry are headed by Petróleos de Venezuela, S.A. (PDVSA), a wholly-owned State corporation, which was created by Presidential Decree in 1975 as a result of the oil nationalization process and with the initial purpose of planning, coordinating

* Simón Herrera Celis is a consultant at LEĜA Abogados. Lawyer graduated from Universidad Católica Andrés Bello, (1991). Master of Laws at American University, (2013). Diploma in Hydrocarbons and Mining at Universidad Monteávila, (2007). Admitted to practice law in Venezuela and New York. Member of the Venezuelan Association of Arbitration (AVA).

** José Alberto Ramírez León is a partner of LEĜA Abogados. Lawyer graduated from the Universidad Católica Andrés Bello, (1999). Master of Laws at the University of Missouri-Columbia, (2005). Executive Director of the Venezuelan Association of Arbitration (AVA). University professor in the field of commercial arbitration. Member of the lists of arbitrators of the Business Center for Conciliation and Arbitration (CEDCA) and the Arbitration Center of the Caracas Chamber of Commerce.

and supervising all oil and gas operations in the country. PDVSA is thus a public industrial holding, with interests, shares and participations in the national and world oil business.

State-owned companies and joint ventures are subject to a special legal regime, even though they are commercial companies, since both private law and public law rule govern their creation and operation. It should be noted that the mixed companies created for the exercise of exploration and production activities of liquid, solid and semi-solid hydrocarbons and associated natural gas (known in the *Organic Hydrocarbons Law as primary activities*) are considered State-owned companies, since they have a functionally decentralized entity, such as Corporación Venezolana del Petróleo, S.A., as holder of a participation greater than fifty percent in its capital stock, as provided in Article 103 of the *Organic Law of Public Administration* of 2014.

Upstream mixed oil companies respond to the criteria of State control contemplated in Articles 22, 33 and 34 of the *Organic Law of Hydrocarbons*, according to which the State only allows minority private participation in these companies, since the State must have a majority share of more than fifty percent in the capital stock. Additionally, these mixed companies must be previously authorized by the Venezuelan National Assembly for their creation and operation. We do not yet know if the recently enacted *Constitutional Anti-Blockade Law* for National Development and the Guarantee of Human Rights of 2020 will definitively modify the criteria for minority private participation regulated in the *Organic Law on Hydrocarbons*, in order to allow a majority or even exclusive participation by the private sector in upstream activities.

II. The constitutional and legal recognition of arbitration in Venezuela

The importance of arbitration was recognized by the Venezuelan National Constituent Assembly two decades ago, granting it constitutional status. Thus, according to the 1999 Constitution, the justice system is integrated by both the courts of the Republic and the alternative means of justice and the citizens participating therein. Article 258 of the Constitution further establishes that the alternative means of conflict resolution must be promoted by the Law, namely, arbitration, conciliation, mediation, and any other alternative means.

Arbitration in Venezuela is mainly regulated by the Commercial Arbitration Law, as well as by the Laws ratifying the above mentioned Treaties. Commercial arbitration is limited to matters in which the parties have the capacity to compromise and with the limitations imposed by the concept of public policy. The aforementioned 1998 arbitration legislation excludes from commercial arbitration disputes directly related to the powers or functions of State sovereignty or of public law persons.

Notwithstanding the foregoing, these exceptions must be viewed in a restricted fashion, otherwise, arbitration related to the intense commercial activity of the Venezuelan Public Administration and its instrumentalities (commercial companies, autonomous institutes and financial institutions) would not be accepted.

According to the so-called Model *Law on International Commercial Arbitration adopted by the United Nations Commission on International Trade Law (UNCITRAL)* in 1985, arbitration of a commercial nature comprises commercial transactions involving the supply or exchange of goods or services, distribution agreements, commercial representation or agency, factoring, leasing of goods, construction, engineering, licensing, investments, financing, banking, insurance, exploitation agreements or concessions, joint ventures and other forms of industrial or commercial cooperation, as well as the transportation of goods and passengers.

The *Organic Law of Hydrocarbons* in Article 34 on mixed companies sets out that disputes of any nature that may arise due to the performance of hydrocarbon activities that cannot be resolved amicably by the parties, including arbitration in the cases allowed by the Law governing the matter, shall be decided by the competent courts of the Republic, in accordance with its Laws. The legislator does not provide further details as to which cases would be permitted to be submitted to arbitration. Article 24 of the *Organic Law of Gaseous Hydrocarbons* of 1999 establishes a rule very similar to that of the *Organic Law of Hydrocarbons*, referring to arbitration as an ideal mechanism for the resolution of conflicts. That special law regulates upstream and downstream projects and activities relating to natural gas not associated with oil.

With regard to the mixed oil companies resulting from the extinct operating agreements, the National Assembly through a parliamentary accord dictated its terms and conditions of creation and operation in 2006, modified in 2009. Said terms and conditions establish that any dispute or controversy that cannot be resolved amicably by the parties, shall be submitted to the decision of the courts of the Republic. Before initiating any litigation, the parties are obliged to seek the possibility of using mechanisms to resolve amicably any disputes of any nature that may arise, including requesting opinions on technical matters from independent experts appointed by mutual agreement. In addition, we note that the jurisdiction clause contemplated in this authorizing parliamentary accord for the contract for the incorporation and operation of a joint venture is replicated in a fairly similar manner in the rest of the parliamentary accords for oil joint venture contracts with which we are familiar.

III. Oil companies in the light of the Commercial Arbitration Law

The Commercial Arbitration Law establishes a mechanism of authorizations of a dual nature with respect to public law persons, within which we must include public capital oil companies. According to its article 4, when one of the parties to an arbitration agreement is a company in which the Republic, the States, the Municipalities and the Autonomous Institutes have a participation equal or superior to fifty percent (50%) in the capital stock, or a company in which the aforementioned persons have a participation equal or superior to fifty percent (50%) in the capital stock, said agreement will require for its validity the approval of the competent statutory body and the written authorization of the Minister in charge, which is none other than the Minister with competence in hydrocarbons.

In order to understand how Article 4 operates in public capital oil companies in Venezuela, we highlight that (i) Petróleos de Venezuela, S.A. (PDVSA) is a mercantile company where the Bolivarian Republic of Venezuela holds one hundred percent (100%) of its capital stock. This is known as a first degree state-owned company; (ii) Corporación Venezolana del Petróleo, S.A. (CVP) is a mercantile company where PDVSA holds one hundred percent (100%) of its capital stock. This is known as a second degree state-owned company; and (iii) an upstream mixed oil company, is a mercantile company where usually CVP holds over fifty percent of its capital stock. The latter is known as a third degree state-owned company.

In our opinion, Article 4 in question refers to those cases in which a first or second degree state-owned company can go to arbitration, in terms of its level of decentralization to the public administration. To this end, the norm establishes two concurrent conditions: (i) the approval of the competent statutory body, without indicating whether it is the shareholders' meeting, the board of directors or some other corporate body, and (ii) the authorization of the Minister of in charge of the hydrocarbons industry.

Joint ventures as third-degree state-owned enterprises would not be subject to the requirements set forth in the aforementioned regulations, since we insist that they only regulate first and second degree state-owned enterprises. For this reason, the clauses and arbitration agreements contemplated in the commercial and financial contracts, as well as in the service contracts, which were signed by the mixed enterprises would not require the prior approval of the competent statutory body, nor the authorization of the Minister in charge. In practice, we have observed that the Minister of Petroleum effectively authorizes mixed companies to sign arbitration clauses or agreements, while mixed companies authorize such arbitration clauses or agreements both in board of directors' meeting resolutions and in shareholders' meeting resolutions. In this sense, in the contracting of specialized oil services required by the mixed companies, necessary to assist in the exercise of their activities, such as seismic, drilling and maintenance services, as well as in the contracts for the purchase and sale of hydrocarbons, loan contracts, guarantee contracts, such companies have the right to include an arbitration clause or agreement, without it being necessary under the Law to go to the Ministry with competence in hydrocarbons to request its authorization or to its statutory body.

In sum, leaving aside the mixed oil companies, there is no discussion that Petróleos de Venezuela, S.A. (PDVSA), PDVSA Petróleo, S.A., Corporación Venezolana del Petróleo, S.A. (CVP) and any other first or second degree oil company where the Republic or a State company has an interest equal to or higher than fifty percent of the capital stock, must obtain the aforementioned authorizations set forth under the Commercial Arbitration Law to enter into arbitration agreements or clauses.

VI. Two important judicial decisions issued in the context of the concept of immunity from jurisdiction and the restrictions of the Law on Private International Law

Immunity from jurisdiction is a concept that has been widely discussed in Venezuela. It has even led to special laws in the United States, Spain and the United Kingdom. There is also the United Nations Convention on State Immunities, which has not been ratified by Venezuela. It is important to distinguish between the right not to be sued or prosecuted before the jurisdictional bodies of another State and the right not to have the judgment executed, which is why two complementary rights are established within the concept of immunity from jurisdiction.

In addition, there is a distinction between relative and absolute immunity. According to the doctrine of absolute state immunity, foreign states cannot be sued or subjected to the jurisdiction of the courts of a given country, even in civil or commercial matters, for reasons of sovereignty and public interest. On the other hand, the doctrine of relative immunity recognizes that States act as individuals in commercial, industrial, and credit activities. The latter doctrine is based on a dual premise. On the one hand, States enjoy immunity for acts performed in the exercise of their sovereignty, called acta jure imperii. At the same time, however, States cannot protect themselves against the immunity of their acts in respect of the management or administration of private property, known as acta jure gestionis.

In Venezuela, the former Supreme Court of Justice in plenary session, in a sentence issued on August 17, 1999, in the case of Association Agreements for the Exploration at Risk and Production of Hydrocarbons under Shared Profits, within the framework of Article 5 of the repealed Organic Law that Reserves to the State the Industry and Commerce of Hydrocarbons of 1975 (known as the Nationalization Law), determined the validity of the inclusion of an arbitration clause in a contract of national public interest

between PDVSA and foreign companies, due to its commercial nature and its importance for the achievement of the economic measures adopted by the Public Administration, concluding that it is the latter who must determine the suitability of arbitration as the mechanism that best contributes to the fulfillment of the purposes pursued with the agreements. With this important 1999 ruling, the Supreme Court recognized that the 1961 Constitution, now repealed, set out in Article 127, the relative immunity from jurisdiction, equivalent to the relative immunity clause established in Article 151 of the 1999 Constitution.

Later, in a judgment issued on October 17, 2008, in the case Interpretation of Article 258 of the Constitution, the Constitutional Chamber of the Supreme Tribunal of Justice confirmed the integration of arbitration as part of the system of administration of justice in Venezuela, allowing the Venezuelan State to submit potential conflicts to arbitration on the basis of promoting international economic relations. The Constitutional Chamber, as the maximum interpreter of the constitutional regulations, held that the Constitution does not advocate a theory of absolute immunity, recognizing the possibility for the State to settle in arbitration disputes derived from contracts of general interest.

The contracts that PDVSA and affiliated companies sign with private investors for the performance of primary activities and that give rise to mixed companies require the authorization of the National Assembly, and therefore must be considered contracts of national public interest, pursuant to Article 150 of the Constitution and Article 33 of the Organic Law on Hydrocarbons. Undoubtedly, the Constitutional Chamber limited the nationalist criterion of strict sovereign immunity that had been previously established by other Chambers of the Supreme Tribunal of Justice that interpreted Article 151 of the Constitution, reaffirming that our constitutional text embraces the system of relative immunity. This pragmatic approach of the Supreme Tribunal is justified by the need of the State to enter into commercial relations with foreign actors to develop activities essential to the achievement of its purposes that cannot be satisfied by the State itself. Thus, the State is forced to participate in a globalized market with well-defined traits, among which the choice of arbitration as an ideal means for the resolution of possible conflicts stands out.

Article 47 of the 1997 Law on Private International Law provides that the jurisdiction corresponding to Venezuelan courts may not be conventionally abrogated in favor of foreign courts or arbitrators' rulings abroad in those cases where the matter concerns disputes relating to real rights over immovable property located in Venezuelan territory, or where the matter is one that cannot be settled or one that affects the essential principles of Venezuelan public policy.

This rule, which is almost a replica of Article 2 of the Code of Civil Procedure, imposes additional limitations to international arbitration, other than those contemplated in the Law of Commercial Arbitration, particularly with respect to real estate located in the territory of the Republic.

V. The applicable law, the mercantile uses and customs, the lex mercatoria and the lex petrolea

Article 29 of the Law on Private International Law provides that contractual obligations are governed by the law indicated by the parties. Additionally, the reality of arbitration in Venezuelan oil industry contracts does not prevent arbitrators from taking into account the stipulations of the contract and the commercial uses and customs, as expressly recognized in Article 8 of the Commercial Arbitration Law. Commercial customs are also accepted in Article 9 of the Commercial Code, and in Article 31 of the Law on Private International Law when it refers to the rules, customs and principles of International Commercial Law and internationally accepted commercial uses and practices. These uses, practices and customs bring us closer to the concept of the lex mercatoria, as those referring to commercial practices in a given industry. Arbitration awards issued by institutions recognized worldwide could also be considered as a source of the so-called lex mercatoria. Of course, this lex mercatoria will serve as an aid, first, for the contracting parties in the execution of the contract, and then, for the arbitrators, to issue their award. The lex mercatoria may also be incorporated into contractual relations when the parties agree in their contracts to refer to international customs and practices, and to the best practices and standards of the industry.

The lex petrolea is a concept inspired by the same principles that inform the lex mercatoria, which is why both notions tend to be confused. In this way, the lex petrolea is incorporated to the legal system through contractual clauses that refer expressly to practices and customs in the oil industry, as well as to the integration of diligence and compliance standards linked to the international oil industry in the execution of its different contracts. Both the lex mercatoria and the lex petrolea, as well as the mercantile uses and customs constitute a source of law in Venezuela and complement our regulatory framework. These "soft" non-state norms or soft law, as they are known in modern International Law, are increasingly common and of homogeneous application in transnational industries such as the oil industry. Their manifestations are diverse and include, for example, the standardized models of contracts of the Association of International Petroleum Negotiators (AIPN), norms that can be applied to the commercial relations of the parties in substitution of state law, such as the UNIDROIT Principles of International Commercial Contracts, or standard clauses that can be incorporated into contracts by reference, such as the Incoterms of the International Chamber of Commerce (ICC).

On the other hand, from the point of view of procedural rules particularly related to arbitration law, we can also mention the Code of Good Arbitration Practices of the Spanish Club of Arbitration, the IBA (International Bar Association) Rules on Evidence in International Arbitration, and the IBA Guidelines on Conflicts of Interest in International Arbitration.

VI. The Constitutional Law on Productive Foreign Investment and the Anti-Blockade Law on Arbitration

In 2017 the National Constituent Assembly passed the Constitutional Law on Productive Foreign Investment, in the exercise of the legislative function constitutionally conferred upon the National Assembly. It also issued the aforementioned Constitutional Anti-Blockade Law for National Development and the Guarantee of Human Rights (Constitutional Anti-Blockade Law).

Article 6 of the Constitutional Law on Productive Foreign Investment may create uncertainty as to its meaning, by establishing that foreign investments shall be subject to the jurisdiction of the Venezuelan courts, in accordance with the provisions of the Constitution and the Laws. This rule does not actually promote open arbitration, but neither does it oppose to its use. In fact, we consider that the parties have the possibility to agree on the arbitration agreement in a contract of a commercial, industrial or credit nature, based on the principle of autonomy of the parties. By making an express reference to the Constitution and being this the highest rule in the internal order, it is plausible to conclude that arbitration continues to be an accepted mechanism to settle disputes under the Constitutional Law on Productive Foreign Investment. Further on, the same article provides that the Republic may participate in alternative means for the resolution of disputes within the framework of the integration schemes with Latin America and the Caribbean, as well as within other integration schemes.

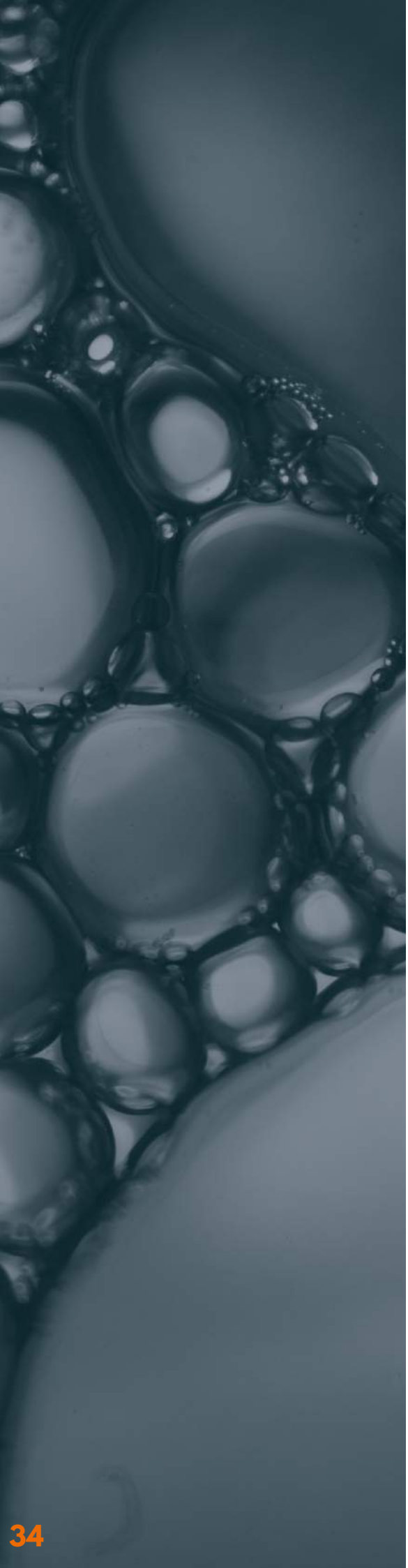
On the other hand, according to Articles 34 and 35 of the Constitutional Anti-Blockade Law, the Republic and its various entities may enter into contracts with investment protection and dispute resolution clauses, for the purpose of generating confidence and stability, subject to the agreement and favorable opinions of the Ministry with competence in matters of economy and finance and the Attorney General's Office.

VII. The recent ruling of the Constitutional Chamber that could question the autonomy of the parties' will in matters of arbitration

The jurisprudence of the Supreme Tribunal has almost always been a positive influence in the development of commercial arbitration in Venezuela, since the enactment of the Commercial Arbitration Law and the Constitution of 1999, as evidenced by the judgment issued on June 19, 2001 by its Political-Administrative Chamber in the Hoteles Doral case, and the judgment issued on November 3, 2010 by its Constitutional Chamber in the Astivenca case, among other important decisions.

However, the Constitutional Chamber of the Supreme Tribunal of Justice, on February 20, 2020, issued an interlocutory judgment, in which it ordered the Centro Empresarial de Conciliación y Arbitraje (CEDCA), in the city of Caracas, to forward the file to decide on the request to hear the case initiated by one of the parties in the arbitration proceedings. The Constitutional Chamber decided in that judgment to suspend this procedure, before the award was issued, pursuant to a reputed competence granted by the Organic Law of the Supreme Tribunal of Justice.

In this regard, it should be noted that the Commercial Arbitration Law expressly provides that arbitration proceedings may only be challenged once the corresponding award has been issued, through an annulment recourse against the award itself before the ordinary jurisdiction. The intervention of the judiciary is only appropriate in very specific cases of appeal, but at no time is the interference of a court of ordinary jurisdiction authorized in the resolution of the substance of the dispute discussed in the arbitration proceedings as has happened in this case. The constitutional judge erroneously justifies the suspension of the arbitration procedure, by virtue of a mere request by one of the parties to take the appropriate measures to restore constitutional public order, clearly overstepping its legal powers.



The fact of interrupting the arbitral procedure in the decision-making stage and subtracting from the arbitral tribunal the capacity to issue an award, so that it is the Judicial Power that does it or orders it to be done in a certain manner, violates the necessary and reciprocal collaboration that must exist between the arbitration tribunal and the Judicial Power, leaving the arbitration deprived of its exclusive and excluding character. In addition, this erroneous interpretation by the Constitutional Chamber contradicts the fundamental aspect of independence attributed to the arbitration tribunal both by the Commercial Arbitration Law and the arbitration clause signed by the parties.

This interlocutory decision of the Supreme Tribunal of Justice, issued just weeks before the formal suspension of most public activities in Venezuela on the occasion of the pandemic, which occurred on March 13, 2020 through a Presidential Decree, has caused great concern in the national and international forum. Therefore, we hope that the Constitutional Chamber will rectify its position in its substantive decision to return to the arbitrators their power to decide the dispute.

Conclusions

In Venezuela there is a regulatory framework that clearly promotes international commercial arbitration, despite the fact that nationalist views and some judicial decisions sometimes unfortunately obstruct its development. Currently, State-owned companies are an active and necessary part of the upstream liquid hydrocarbons business, and as public sector companies they have an authorizing regime that they must comply with in order to sign agreements and arbitration clauses. The particular conditions of the upstream mixed companies with respect to arbitration do not include this authorizing regime, although in practice they have received a treatment that is not differentiated from the companies that make up the public holding company PDVSA. On the other hand, the concept of immunity from jurisdiction is a relative one that allows international commercial arbitration to be used in cases of a commercial nature.

The upstream oil industry has an assortment of players of diverse nationalities, financial capacities, knowledge and expertise, participating through contracts of a wide-ranging nature and complexity. From the physical security contract for the protection of facilities; the contract for the design, construction, installation and commissioning of an offshore production platform; to the contract for exploration at risk and profit or production sharing. It is in these circumstances that a global culture in favor of international commercial arbitration has developed. Let us not forget that private investors and contractors prefer to have arbitration as a means of dispute resolution in their contracts. For its part, the Venezuelan judiciary must give clear and unequivocal signals of respect for the institution of international commercial arbitration in which the neutral forum and the powers of the arbitrators prevail.

This is the reality of the oil industry worldwide and today's Venezuelan challenges must be responded to with pragmatism and a sense of urgency to boost private

PUBLIC AND PRIVATE INITIATIVE IN MINING ACTIVITY IN VENEZUELA: AN INTRODUCTION

CARLOS GARCÍA SOTO*

Introduction

The legal-administrative regime of mining activity in Venezuela consists (i) of general legislation, applicable directly or additional, as the case may be, to that activity, contained in *the Constitution, the Law of Mines*[1] and *the General Regulations of the Law of Mines*[2] ; (ii) by special legislation, contained in Laws and Decrees that have reserved mining activity in relation to some minerals, and (iii) by complementary legislation, such as environmental legislation applicable to mining activity.

From a constitutional point of view, the constitutional regime of mining activity assumes that

(i) Mining deposits, whatever their nature, belong to the Republic, are public domain property and therefore inalienable and imprescriptible (article 12)[3], and
(ii) The regime and administration of mines is the responsibility of the National Public Authorities (article 156.16)[4].

General legislation and special legislation set out the areas of public initiative and private initiatives in mining activity, setting out the assumptions and ways in which the Venezuelan State and individuals may carry out this activity, autonomously or jointly, as the case may be.

In recent years, the scope of private sector action in the mining business has been impacted by the reserve that over a significant number of minerals the State has made in its favor for the exercise of primary activities. This has been a major limitation on the scope of private initiative, which has, of course, led to an extension of the scope of public initiative in mining activity.

This brief essay aims precisely to try to identify the channels through which public and private initiatives in mining activity in Venezuela may take place, in accordance with the current legal regime, derived from that general and special legislation.

I. Public initiative in mining activity

1. Introduction

By public initiative in mining activity we understand the set of ways through which the National, Central or Decentralized Public Administration, can carry out mining activity, in accordance with the provisions of the *Law on Mines and its Regulations*, and special legislation on mining matters.

Indeed, by listing the modalities of public and private participation in mining activity, the article 7.1 of the *Law of Mines* recognizes that the exploration, exploitation and use of mining resources may be executed directly by the National Executive.

The types of initiative we will describe are, on the one hand, the assumptions of *direct* exploration and exploitation of mining activity by the State. On the other hand, the exploration and *indirect* exploitation by the Venezuelan State is given by the figure of the mining concession, which in any case will be studied among the modalities of private initiative.

2. Mining activity carried out by the Central National Public Administration (the Republic)

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* Carlos García Soto is a partner LEĜA Abogados. He is a lawyer graduated magna cum laude from the Universidad Monteávila, (2004). Doctor of Laws from the Complutense University of Madrid, (2014). Professor of Administrative Law at the Universidad Central de Venezuela and Regulatory Environment at IESA. Director of Law and Society, Journal and Blog of the Faculty of Legal and Political Sciences of the Universidad Monteávila. Treasurer of the Venezuelan Association of Administrative Law. President of the Legal Committee of the British Chamber of Venezuela.

[1] Official Gazette N° 5.382 extraordinary dated 09-28-1999.

[2] Official Gazette N° 37.155 dated 03-09-2001.

[3] These characteristics of mining sites are reiterated in article 2 of the Law of Mines and by article 6.4 of the Organic Law of Public Assets (Official Gazette N° 6.155 extraordinary dated 11-19-2014).

[4] That is why the Explanation of Reasons for the Law of Mines points out:

"In this sense, one of the fundamental principles that nourish the basis of this Draft Decree-Law, is the express declaration that the mines are property by the Republic. This declaration is enshrined in our legal order from the Decree of El Libertador, given in Quito on October 24, 1829, anticipating in many years to new theories and systems, on the nationalization of mines. On the basis of this principle, the State behaves before the mining wealth as a true owner, and not as a mere administrator of it, therefore, it can exploit by itself in a regime of concurrence with third parties through concessions or it can reserve the exploitation, without at any time detaching itself from the property of the mines. The Project adopts the dominant system that includes the two modalities mentioned above, that is, the direct exploitation or exploitation through optional concessions, consequently, this leads to the elimination of the royalty system and therefore the figures of denouncement, free exploration, the exclusive exploitation and free use disappear".

First, the Venezuelan State may carry out mining activity directly through the Ministry responsible for mining, as is derived from article 23 of the *Law of Mines*. That Ministry, as the body of the Republic, can thus carry out the primary activities of mining activity. In practice, however, what happens most often is that this right is transferred to the authorities of the Decentralized National Public Administration.

3. Mining activity carried out by the National Decentralized Public Administration (decentralized bodies)

On the other hand, mining activity can also be carried out directly by the State through bodies of the National Decentralized Public Administration, as is derived from article 23 of the *Law of Mines*.

In practice, in fact, it is often the case that mining activity is carried out directly by the State through the authorities of the National Decentralized Public Administration, specifically through State companies. In such cases, the Republic, by body of the Ministry with competence in the field of mining, may transfer to a company of the National Decentralized Public Administration the right to exercise primary activities. This was the case, for example, of *Decree N° 3.607, by which it is transferred to the Venezuelan Mining Corporation, S.A., (CVM), the right to the exercise of primary exploration and exploitation activities of gold and other strategic minerals.[5]*

4. The particular case of State companies

It is usual for such transfers to be made in favor of a State company, given the eminently commercial nature of the mining activity. The State company thus serves the State as an instrument for the exercise of economic activities, specifically in the mining sector.

The case of the State companies responds to a traditional figure of Venezuelan administrative organization and economic management, through commercial companies in which the State is the majority shareholder, and exerts a real commercial control.[6]

Under the regime of the Organic Law of Public Administration (LOAP)[7] could be considered included the State companies in which the Venezuelan State owns the total shares, as well as the State companies in which a private company has a shareholding, always below 50% (article 103 of the LOAP). As we will see when studying the private sector participation ways, under the *Organic Law that reserves to the State the Activities of Exploration and Exploitation of Gold, as well as those related and auxiliary to them*, is referred to as "mixed joint ventures " the State companies in which the shareholding of individuals is allowed.

But from the perspective we are addressing now, what we want to specify is that the Venezuelan State can directly carry out the primary activities of the mining sector through a State company, whose share capital is fully subscribed by the State. This is the case, for example, of the State company Carabobo Oro, C.A., whose creation was authorized by *Decree N° 3.378, which authorizes the creation of a State Enterprise, in the form of an Anonymous Company, called Carabobo Oro, C.A., which will be attached to the Ministry of the People's Power of Ecological Mining Development, and will last forty years.[8]*

II. Private initiative in mining activity

1. Introduction

We can understand by private initiative in mining activity the ways through which individuals, national or foreign, can participate in mining activity, in accordance with the titles provided for in the legislation.

Private initiative in mining activity is regulated by general legislation (*Law of Mines and its Regulations*) and special legislation, particularly that which has reserved mining activity to the State in relation to certain minerals (such as the *Law of Gold*),for which general legislation will then be of additional application.[9]

2. Modalities of private participation in mining activity [10]

A. Introduction

The private sector may participate in mining activity in a number of ways, depending on whether or not it is primary activities in the mining sector, or whether they are the other activities that may take place in this sector. Such primary activities are those relating to the exploration and exploitation of mining sites, while not all other activities that may be carried out on the occasion of the existence of the deposits will be primary activities. This distinction will be key to distinguishing the different scenarios through which individuals can engage in mining activity.

B. Exploration and exploitation concessions

a. Introduction

[5] Official Gazette N° 41.477 dated 09-07-2018, reprinted in Official Gazette N° 41.478 dated 09-10-2018.
[6] Under the general regime of the Organic Law of Public Administration, here the State can be understood both in its aspect of the Central National Public Administration, and in its aspect of the National Decentralized Public Administration.
[7] Official Gazette N° 6.147 extraordinary dated 11-17-2014.
[8] Official Gazette N° 41.379 dated 04-17-2018.
[9] On regulatory techniques and the participation of private capital in the mining industry, see Allan R. Brewer-Carías, "El régimen de participación del capital privado en las industrias petrolera y minera: desnacionalización y técnicas de regulación a partir de la Constitución de 1999", in VII Jornadas Internacionales de Derecho Administrativo Allan Randolph Brewer-Carías". El principio de legalidad y el ordenamiento jurídico-administrativo de la libertad económica, Volumen I, Funeda, Caracas, 2004, pp. 50 and below.

Individuals may participate *directly* in primary exploration and exploitation activities through the figure of the mining concession.

As we have pointed out, mining sites are assets of the public domain. This means, in short, that individuals cannot hold the right to property in such deposits, which are excluded from private appropriation under Venezuelan law.

Therefore, individuals can only explore and exploit mining deposits if they have a mining concession, which is a species of the public domain concession regime, under the rules provided in the *Law of Mines and its Regulations[11]* as will be briefly explained below.

In any case, it is understood that the figure of the concession entails *indirect* exploitation by the State, which participates in *mediate* in the holding by means of the figure of the concessionaire.

b. The mining concession regime under the *Law of Mines*

Given that minerals are assets in the public domain (articles 12 of the Constitution and 24 of the Law of Mines), primary activities in the mining sector can only be carried out by the individual if a mining concession is granted to him, as noted.[12]

The mining concession is defined by article 24 of the Law of Mines as follows:

"**Article 24**: The mining concession is the act of the National Executive, by which rights are granted and impose obligations on individuals for the use of mineral resources existing in the national territory.

The mining concession confers on its holder the exclusive right to the exploration and exploitation of mineral substances granted within the spatial scope granted".

c. The demanial reservation by Laws and Decrees

This general principle could, however, be altered: the State may establish a "demanial reserve" on certain minerals, which may now only be the subject of primary activities by the State, thus prohibiting private participation under the figure of the mining concession (article 23 of the *Law of Mines*)[13]. From that point of view, the reservation goes from non-exclusive (under the general regime of *Law of Mines*) to being exclusive (under the declared reserve regimen) [14] In accordance with that rule:

"**Article 23:** The National Executive may, where appropriate in the public interest, reserve by Decree certain mineral substances and areas containing them, to explore or exploit them only directly by the body of the Ministry of Energy and Mines, or by means of bodies of the exclusive property of the Republic".[15]

In our view, even though the rule refers to Decrees, we believe that such a reservation can also be made by law, as has indeed happened.[16]

Precisely what has happened in recent years is that the National Executive has reserved primary activities on a significant set of minerals[17]. This trend began with gold ore, but has then expanded to other minerals which has led to an extension of the scope of public initiative in the mining sector.

Indeed, in 2011 was publish the *Organic Law which reserves to the State the Activities of Exploration and Exploitation of Gold, as well as those related and auxiliary to them* (Law of Gold). Although the Law originally only reserved to the State the primary activity relating to gold, then the 2015 reform included the possibility of establishing reserves on any other "strategic mineral", when so declared by Decree. Strategic minerals are defined in article 5 of the current Law as "those that are considered of national convenience and in the public interest, declared as such by Decree dictated by the National Executive".

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[10] See Víctor Rafael Hernández-Mendible, "Regulación minera", in Jesús María Casal y Jorge Luis Suárez (Coordinators), La libertad económica en Venezuela: balance de una década (1999-2009), Universidad Católica Andrés Bello, Caracas, 2011, pp. 327 and following and Mauricio Rafael Pernía-Reyes, "La minería en Venezuela y el nuevo régimen jurídico del aprovechamiento del oro", in Revista Tachirense de Derecho, N° 23, January-December, 2012, pp. 114 and following.

[11] The Regulations of the Law of Mines, in fact, contain the development of the regulation provided for in the Law on the Figure of the Mining Concession (articles 10 and following).

[12] See José Ignacio Hernández G., "Régimen jurídico-administrativo del Coltán como mineral estratégico", in Revista Electrónica de Derecho Administrativo Venezolano, N° 9, May-August, 2016, pp. 101-103, pp. 101-103. The author points out on the concept of mining concession that "The mining concession is the act by which the Administration assigns to private investment the right of exploration and exploitation of deposits, which are property owned by the Republic of the public domain, in accordance with articles 12 of the Constitution and 24 of the Law on Mines" (p. 102 , footnote 13). See also "Sobre el régimen de los recursos naturales y el ambiente, y las técnicas tradicionales del Derecho Administrativo", in Revista de Derecho Público, N° 136, October-December, 2013, pp. 22 and following.

[13] "This reservation is called the 'demanial reserve', as it consists of the decision by which the Administration assumes for itself the management of mining rights, denying the possibility that these rights exercised by private initiative through concession. Such a reservation may be agreed even by administrative act, in enforcement of the Law of Mines" (José Ignacio Hernández G., "Régimen jurídico-administrativo del Coltán como mineral estratégico", cit., p. 102).

[14] See Allan R. Brewer-Carías, "Sobre el régimen de los recursos naturales y el ambiente, y las técnicas tradicionales del Derecho Administrativo", cit., p. 23.

[15] Article 86 of the Law reiterates the Executive's power to reserve such activities by Decree.

For this reason, under that Law and under any other Decree or Law that reserves certain minerals to the State, mining activity relating to those minerals is subject to that special regime. In such cases, general mineral legislation, i.e. basically the *Law of Mines and its Regulations,* are then of additional application.

The fundamental consequence of these reserves in favor of the State is that the exploration and exploitation of reserved minerals can only be carried out directly by the State, thus excluding the possibility of private participation through the figure of the mining concession.

In the case of gold and other strategic minerals, in addition, under the *Gold Law[18]* the sale and delivery of gold and other strategic minerals is done in favor of the Central Bank of Venezuela{19] Pursuant to article 31:

"**Article 31:** Gold and other strategic minerals obtained as a result of any mining activity in the national territory will be mandatory for sale and delivery to the Central Bank of Venezuela. The Central Bank of Venezuela may authorize, the sale and/or delivery of each ore to a different entity, in the terms established for that purpose".[20]

In September 2020, however, was publish the Resolution N° 20-08-01 of the Central Bank of Venezuela[21], according to the Central Bank of Venezuela may "decline" the offer that must necessarily be made to it of gold, and "authorize" the sale of gold directly abroad (article 1). For the purpose of issuing the marketing authorization, the person concerned shall pay the Central Bank of Venezuela, for the activities and services related to the issuance of the marketing authorization, typical of the technical analyses associated with the determination of the weight and purity of the gold ore, a percentage between nine per cent (9%) up to fourteen per cent (14%) authorized amount (article 3).

[16] It was the case, although certainly by Decree-Law, of the steel sector in the Guayana region, by Decree N° 6.058, with Rank, Value and Force of Organic Law on the Management of Companies That Carry Out Activities in the Steel Sector in the Guayana Region (Official Gazette N° 38.928 dated 05-12-2008).

[17] Since 2016, the President of the Republic has issued a very large number of Decrees to declare the reservation of primary activities on various minerals. This is the case, for example, Decree N° 2.413, by which they are declared as strategic elements for their exploration and exploitation of Niobium (Nb) and Tantalio (Ta), and are therefore subject to the regime provided for in the Decree with Rank Value and Force of Organic Law that reserves to the State the Activities of Exploration and Exploitation of Gold and other Strategic Minerals (Official Gazette N° 40.960 dated 08-05-2016). Other Reserve Decrees have been as follows: Decree N° 455, by which it reserves to the National Executive, by the body of the Ministry of the People's Power of Petroleum and Mining, the direct exercise of the exploration and exploitation of Nickel and other minerals associated with it, which are in the area comprising the extinguishing concessions indicated thereof (San Antonio No. 1, Camedas No. 1; Camedas No. 2, Camedas No. 3, among others (Official Gazette N° 40.265 dated 10-04-2013); Decree N° 456, by which it reserves to the National Executive, by body of the Ministry of the People's Power of Petroleum and Mining, the exercise of the activities of exploration and exploitation of the mineral of Roca Fosfática that is located in the area called Los Monos-El Tomate, in the jurisdiction of the Liberator Municipality of the state Táchira (Official Gazette N° 40.265 dated 10-04-2013); Decree N°. 2.781, declaring diamond exploration and exploitation as a strategic element for its exploration and exploitation, and is therefore subject to the regime provided for in the Decree with Value Range and Force of Organic Law that Reserves to the State the Activities of Exploration and Exploitation of Gold and Other Strategic Minerals (Official Gazette N° 41.122 dated 03-27-2017); Decree N° 2.782, by which copper is declared as a strategic element for its exploration and exploitation, and is therefore subject to the regime provided for in the Decree with Value Range and Organic Law Force that reserves to the State the Activities of Exploration and Exploitation of Gold and Other Strategic Minerals (Official Gazette N° 41.122 dated 03-27-2017); Decree N° 2.783 declaring silver as a strategic element for its exploration and exploitation, and is therefore subject to the regime provided for in the Decree with Rank, Value and Force of Organic Law that reserves to the State the Activities of Exploration and Exploitation of Gold and Other Strategic Minerals (Official Gazette N° 41.122 dated 03-27-2017); Decree N° 3.597 declaring coal as strategic ore for exploration and exploitation, and is therefore subject to the regime provided for in the Decree with Value Range and Force of Organic Law that Reserves to the State the exploration and exploitation of gold and other strategic minerals (Official Gazette N° 41.472 dated 08-31-2018); Decree reserved to the National Executive by the Organ of the Ministry of People's Power with competence in the field of Mining, the direct exercise of the exploration and exploitation activities of the Feldespato Ore and other Minerals associated with it, which are located in the areas called: La Gloria 3, La Gloria 4 and Hato San Antonio; located in the municipalities of San Carlos Lima Blanco and Tinaco and Falcón of the state Cojedes (Official Gazette No. 6,387 extraordinary dated 07-03-2018); Decree N°. 3.857, by which it reserves to the National Executive, by the body of the Ministry of People's Power with competence in the field of mining, the direct exercise of the exploration and exploitation of phosphate rock ore and other minerals associated with it, which are located in the area called Los Monos – La Linda– Los Bancos, located in the jurisdiction of the Libertador municipality of Táchira state (Official Gazette N° 41.643 dated 05-29-2019); Decree N° 3.858, by which it reserves to the National Executive, by body of the Ministry of People's Power with competence in mining, the direct exercise of the exploration and exploitation of feldspato ore and other minerals associated with it, which are located in the area called Palo Grande, located in the Bruzual municipality of Yaracuy state (Official Gazette N° 41.643 dated 05-29-2019), and Decree N° 3.859, by which it reserves to the National Executive, by body of the Ministry of People's Power with competence in mining, the exercise of the exploration and exploitation activities of titanium ore and other minerals that are associated with it, which is located in the area called San Quintín, located in the Manuel Monge municipality of Yaracuy state (Official Gazette N° 41.643 dated 05-29-2019).

[18] Official Gazette N° 39.759 dated 09-16-2011. See Alejandra Figueiras Robisco, "El Decreto que reservó al Estado la actividad minera del oro", in Revista de Derecho Público, N° 130 (Estudios sobre los Decretos-Leyes 2010-2012), April-July, 2012. This Law would be reformed by Decree-Law N° 8.683 dated 12-08-2011 (Official Gazette N° 6.063 extraordinary dated 12-15-2011). It would then be reformed by Decree-Law N° 1.395 dated 11-13-2014 (Official Gazette N° 6.150 extraordinary dated 11-18-2014). The current Law is the Organic Law that reserves to the State the Activities of Exploration and Exploitation of Gold and Other Strategic Minerals (Official Gazette N° 6.210 extraordinary dated 12-30-2015).

[19] The first version of the 2011 Law included this rule but only concerning gold, and instead of the Central Bank of Venezuela, the sale was to be made to the Republic, or the body designated (article 21). The 2015 reform, as can be seen from the above-mentioned rule, extended the obligation to the other "strategic minerals".

C. Small mining

Another form of private initiative provided for by the *Law of Mines* is "small mining". Pursuant to article 64 of that Law:

"**Article 64**: Small mining is the activity carried out by natural or legal persons of Venezuelan nationality for the exploitation of gold and diamonds, for a period not exceeding ten (10) years, in areas previously established by resolution, by the Ministry of Energy and Mines, whose area shall not exceed ten (10) hectares, to be worked by a number no more than thirty (30) individually considered workers".

D. Mining Community

Mining community is another figure that allows private initiative in the mining sector. According to section 77 of the *Law of Mines:*

"**Article 77**: In order to obtain a better use of mining resources, facilitate technical operations, improve the performance of farms and protect natural resources and the environment, the State will promote the establishment of mining communities.

For the purposes of this Law, mining community means the grouping of small miners in various areas of the same or several of them, located in such a way as to allow the joint use of all or part of the services necessary for their use in the exercise of mining activity".

E. Strategic Alliance

In the field of primary activities of gold and other minerals that have been classified as strategic, the *Gold Law* allows strategic alliances to be established between the public and private sectors, aimed in any case at the exercise of small mining. Under article 5 of that law, a Strategic Alliance is "the agreement between a private or community enterprise and the National Power for the purpose of sharing productive processes, either in the same activity or in associated chains. In these alliances the companies involved retain their legal identity separately and establish the association for the purposes described".[22]

F. Artisan mining

Another form of private initiative in the mining sector is artisan mining. Pursuant to article 82 of the Law:

"**Article 82**: Artisan mining is one characterized by personal and direct work in the exploitation of gold and alluvial diamonds, by means of manual, simple, portable equipment, with rudimentary extraction and processing techniques and which can only be exercised by natural persons of Venezuelan nationality".

G. Related or auxiliary mining activities

Privates may also carry out what the Act calls "related or auxiliary mining activities". In accordance with article 86 of the Law:

"**Article 86:** The storage, possession, benefit, transport, circulation and trade of minerals governed by this Law shall be subject to the supervision and inspection by the National Executive and to the regulations and other provisions which it should issue, in defense of the interests of the Republic and mining activity. When this is in the public interest, the National Executive may reserve by decree any such activities with respect to certain minerals".

H. Again, the case of State companies (mixed joint ventures)

We noted that public initiative can be carried out through State companies, which may have total shareholdings of the State, or may allow shareholdings of individuals. Under the terminology of the *Gold Law*, State companies in which the private sector has a shareholding are referred to as "mixed joint ventures". In any case, such a "mixed joint ventures " is a kind of the type of State companies, according to the concept set out by the LOAP.

Private participation through the mixed joint ventures in the field of reserved minerals is subject to important regulations, such as those provided for in article 17 of the *Gold Law*, on the freedom of companies participating in joint ventures to dispose of the shares they hold in the mixed joint ventures[23]. Article 31 of that law provides that gold and other strategic minerals obtained as a result of any mining activity in the national territory shall be mandatory to sell and deliver to the Central Bank of Venezuela, as noted. In any case, as also noted, the Central Bank of Venezuela may authorize, the sale and/or delivery of each ore to a different entity, in terms established for this purpose.

[20]Under the validity of the Law of Gold of 2014, Joint Resolution N° 090 and N° 15-06-01 of the Ministry of the People's Power of Petroleum and Mining was issued, which states that from the entry into force of this Resolution, individuals, companies or forms of association that carry out gold exploration and exploitation activities in areas intended for mining activities in the national territory , must sell to the Central Bank of Venezuela, all the gold material obtained during this activity, with its metal alloys of a non-polluting nature and in any of its presentations, through the Centers established for this purpose by that Institute (Official Gazette N° 40.692 dated 06-30-2015). Since the extension of the obligation to sell the other "strategic minerals" was established in the Law of Gold of December 2015, this Resolution refers only to the sale of gold.

[21] Official Gazette N° 41.958 dated 09-04-2020.

[22] Then article 10 of the Law of Gold point out that the exercise of reserved activities can be carried out through Strategic Alliances "formed between the Republic and production units, socio-productive organizations, companies and other forms of association permitted by law, which will be oriented to the activity of small mining, duly registered in the Single Mining Register, subject to authorization granted by the Ministry of People's Power with competence in mining matters".

Example of such mixed joint ventures is the Turkish-Venezuela Binational Mining Anonymous Society (MIBITURVEN, S.A.), whose creation was authorized by *Decree N° 3.598, authorizing the creation of a Joint Venture between CVG Compañía General de Minería de Venezuela, C.A., (MINERVEN) and Empresa Marilyns Proje Yatirim, S.A., in the form of Sociedad Anónima, called Empresa Mixta Sociedad Anónima Minería Binacional Turquía - Venezuela (MIBITURVEN, S.A.). [24]*

I. Contractors

The figure of the contractor is an indirect way of private participation in the mining sector. The contractor may be of State, as well as of the concessionaire, as well as of the various figures established for private participation, including the mixed joint ventures. [25]

J. Recapitulation

As can be seen, in terms of private participation in primary mineral exploration and exploitation activities, there are two main ways for the private sector:

(i) in the case of mining activity on a mineral that has not been reserved, the individual may hold a mining concession;

(ii) in the case of mining activity on a mineral that has been reserved, the individual may participate indirectly through (a) small mining; (b) mining community; (c) related or ancillary mining activities; (d) as a minority partner in a State company; (e) through a strategic alliance, or (f) as a contractor.

3. Exceptions and limits on private participation in mining activity

A. Introduction

Although the general principle is that any person, natural or legal, national or foreign, domiciled in the country, may obtain mining rights, in order to carry out the activities indicated in the Law (article 17 of the *Law of Mines)*, the *Law of Mines* itself provides for certain exceptions from the exercise of these rights.

a. Temporary disabling

Under the article 20 of the Law of Mines, no one could aspire to mining rights, either on their own or by person, except by inheritance or legacy, the "members" (*rectius:* officials) of the National, State or Municipal Public Power (and their relatives), which are mentioned in that standard. Article 9 of the *General Regulations of the Law of Mines* adds other officials to that list.

According to the article 21 of the Law warns that persons affected by the incapacity referred to in the Law may not acquire mining rights until a period of not less than five (5) years has elapsed, since the cessation of the impediment that caused them.

b. Permanent disabling

Under article 22 of the *Law of Mines*, foreign governments may not hold mining rights within the national territory.

However, according to the same rule, in the case of companies that depend on such governments or companies in which they have such a share, that by capital or statutes, it confers control of the company, they will require the prior approval of the Congress of the Republic (*rectius*: National Assembly) for the granting of mining rights.

III. Some features of the current environment for mining activity in Venezuela

1. Introduction

It is known how the legal business environment like the miner is strongly influenced by the political, economic and social context of each country. That is precisely why the study of the ways for public and private initiative in mining activity is one of the main issues in this area.

By the time these lines are written, there are five aspects that we consider to be highlighted when analyzing the current environment for mining activity in Venezuela.

2. The progressive expansion of the scope of the mineral reserve in favor of the State

The first aspect to be highlighted is the progressive expansion of the scope of the mineral reserve in favor of the State. As noted, article 23 of the *Law of Mines* empowers the National Executive to reserve by decree mineral substances and areas containing them to explore or exploit them.

[23] Under the Law of Gold regime, mixed joint ventures are those in which the Republic has a stake of no less than fifty-five (55%) capital (article 10).
[24] Official Gazette N° 41.472 dated 08-31-2018.
[25] As derived from articles 18 and 26 of the Law of Gold.
[26] Official Gazette N° 40.855 dated 02-24-2016.
[27] In accordance with article 1 of the Decree, "The National Strategic Development Zone "Arco Minero del Orinoco" is created, for the sectoral stimulus of the activities associated with the mineral resources held by the country, with criteria of sovereignty, sustainability and systemic vision with the system of sectoral and spatial plans of the country, in accordance with the Decree with Rank, Value and Strength of the Law on Integral Regionalization for Socioproductive Development of the Fatherland. This area shall be governed by the regulations provided for in this Decree". On the other hand, article 4 of the Decree states that "The regime provided for in this Decree has as its priority the creation of the necessary stimuli to increase the capacities to exploit the potentials of mineral resources in the Mining Arch of Orinoco, in line with the goals set out in the Plan of Economic and Social Development of the Nation (...)".
[28] Official Gazette N° 6.583 extraordinary dated 12-12-2020.

Since 2011, the President of the Republic has issued Decrees to reserve to the State primary activities on different minerals. This has resulted in the private initiative in the mining sector decreased significantly since that year.

3. The creation of the Mining Arch

Mining activity in Venezuela has been significantly impacted since 2016 by the creation of the "Arco Minero del Orinoco" *by Decree N° 2.248, which creates the National Strategic Development Zone "Arco Minero del Orinoco*"[26]. The Orinoco Mining Arch area covers more than 12% of Venezuela's area (article 2).

This Decree subjects mining activity to be carried out in the area delimited in the Decree to a special regime.[27] This regime assumes, for example, that the National Executive may establish special public procurement mechanisms (articles 15 and 16). It provides for tax incentives for financing and import (articles 17, 18, 19 and 21), simplification of customs formalities (articles 22 and 23), among other measures.

4. U.S. government economic sanctions in the mining sector

On the other side, it should be noted that the United States Government has imposed sanctions on the State company CVG Compañía General de Minería de Venezuela CA (Minerven) and its president. This significantly limits public initiative in the mining sector, since such a state enterprise is key to the current public sector participation scheme in that sector.

5. The *"Constitutional Anti-Lock Law"*

It should be noted that the *Constitutional Anti-Lock Law for National Development and the Guarantee of Human Rights* (Constitutional Anti-Lock Act)[28] has recently been issued by the National Constituent Assembly, in which, for

example, the National Executive is empowered to "modify the mechanisms for the establishment, management, administration, operation and participation of the State of certain public or mixed joint ventures, both domestically and abroad", which could involve altering the regime applicable to state companies, and particularly to mixed joint ventures, in the mining sector.

On the other hand, article 31 allows the National Executive to lift marketing restrictions for certain categories of subjects, in strategic activities of the national economy, which could mean, for example, unwind restrictions on the marketing of gold.

6. The Law of Mines Bill

Furthermore, it should be noted that the Energy and Mines Commission of the National Assembly adopted in September 2020 a *draft of the Law of Mines*, which is still pending first and second discussions.

Conclusions

The legal-administrative regime of mining activity in Venezuela is composed of a general regime, basically contained in the *Law on Mines and its Regulations*, and a special regime, contained in Laws and Decrees that have reserved mining activity in relation to some minerals, and a complementary regime, such as environmental legislation applicable to mining activity.

This legal-administrative regime allows public initiative and private initiative - to various degrees - in mining activity. While the general principle arising from the *Law of Mines and its Regulations* is that the domestic or foreign investor may obtain mining concessions for the exercise of primary activities, the truth is that since 2011 the Venezuelan State has been progressively resuming the exercise of primary activities on a very significant amount of minerals.

This has meant that the scope of private initiative in mining activity has been reduced since 2011. The participation of private individuals in primary activities is thus established indirectly through minority shareholdings in mixed joint ventures in cases where the mineral reserve has been declared. The number of Decrees since 2011, as is said, has increased significantly.

Finally, it should be noted that the regulatory environment of mining activity also poses significant challenges for the domestic or foreign investor, as is derived from the same reserve policy implemented since 2011, from the economic sanctions imposed by the United States Government on a State company in this sector, as well as from the Constitutional Anti-Lock Law issued by the National Assembly.

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Miguel Rivero Betancourt

Contact information
Miguel Rivero Betancourt
Leader of the practice area
Email: mrivero@lega.law
Tel: +58 412 2318571

José Alberto Ramírez León

Simón Herrera Celis

Carlos García Soto

Carlos Alberto Henríquez

Elina Pou Ruan

+58 412.2318.571 | www.lega.law | RIF: J-30816060-1

Caracas: Urb. La Castellana, Av. Eugenio Mendoza, Torre La Castellana, Floor 7, Chacao 1060-A, Edo. Miranda, Venezuela.

Valencia: Av. Paseo Cabriales, Sector Kerdel, Torre Movilnet, Floor 8, Ofic 9/10, Edo. Carabobo, Valencia, Venezuela.

Barquisimeto: Carrera 16, between the streets 24 y 25, Edif. Centro Cívico Profesional, Floor 5, Ofic 5, Edo. Lara, Venezuela.