Update on *PDVSA US Litigation Trust v. Lukoil Pan Americas, et al.*

Richard J. Cooper & Boaz S. Morag[1]

April 10, 2018

On March 15, 2018, we wrote about a lawsuit filed by the PDVSA US Litigation Trust (the "Trust") in federal court in Miami, Florida on behalf of Venezuela's state-owned oil company, Petróleos de Venezuela, S.A. ("PDVSA").[2] The lawsuit alleges that the defendants, a group of 44 oil trading companies, banks and individuals, participated in a 14-year scheme to rig bids, underpay on purchases and overcharge on sales, allegedly resulting in billions of dollars of losses to PDVSA.

In our prior article, we flagged a number of interesting legal and factual questions raised by the suit, such as how the Trust was created, whether it has standing to assert PDVSA's claims, whether some or all of the claims would be barred by applicable statutes of limitation and adequately assert an injury in the United States, and whether the Trust would be able to obtain the cooperation from PDVSA necessary to respond to discovery requests, among others. The case also presents questions as to whether it will have implications for financial creditors of PDVSA, and even creditors of the Republic of Venezuela, who may be able to lay claim to the economic value of the Trust's lawsuit or to any recovery, on the theory that the Trust is pursuing the claims for PDVSA's sole benefit. The documents that have been filed in the suit thus far provide insight into some, though certainly not all, of the questions raised above and also introduce new issues of their own.

I. Current Status of the Litigation

Shortly after filing the action, the Trust filed an *ex parte* motion for a temporary restraining order as to a group of defendants the Trust refers to as the "Morillo Defendants," alleged to be the conspiracy's ringleaders, which does not include the oil trader or bank defendants. The court granted the temporary restraining order only in part, ordering the Morillo Defendants to preserve evidence but denying the Trust's request to seize evidence and freeze those defendants' assets. Since then, the Trust has served many of defendants and has continued to pursue via its motion for a preliminary injunction the relief it was denied *ex parte*. However, it has encountered some difficulty in serving certain of the individual defendants and delay in serving the foreign corporations whose countries require service under the Hague Convention. The defendants who have appeared to date have not only opposed the preliminary injunction, including on grounds that the Trust lacks standing, but have also challenged numerous subpoenas the Trust served on non-parties and the admissibility of certain statements included in the

---

[1] Richard J. Cooper is a Senior Partner in the Restructuring Group at Cleary Gottlieb Steen & Hamilton LLP. Boaz S. Morag is Counsel in the Litigation and Arbitration Group at Cleary Gottlieb. The authors thank Emily Michael for her assistance with this article.

[2] Richard Cooper and Boaz Morag, *PDVSA US Litigation Trust: What Creditors Should Know About the Trust, Its Claims and Its Implications for Venezuela's Restructuring* (March 15, 2018), available at https://client.clearygottlieb.com/52/691/uploads/pdvsa-us-litigation-trust---what-creditors-should-know-about-the-trust--its-claims-and-its-implications-for-venezuela-s-restructuring.pdf.

declarations of the Trust's investigators that were publicly filed with the Trust's amended complaint filed on March 9, 2018 (the "Complaint"). These challenges have resulted in the Court deferring the hearing on the Trust's motion for a preliminary injunction. At a status conference on April 4, 2018 the court accepted that the issue of the Trust's standing needs to be addressed as a threshold matter. The Court has assigned the preliminary discovery issues and the defendants' standing challenge to a magistrate judge for initial consideration at a hearing set for April 16, 2018.

II. What Has Been Disclosed About the Trust?

Our initial article noted that the Complaint was bereft of any details regarding the Trust other than that it was a New York Trust formed in July 2017. Since then, and without disclosing how it was obtained, the Morillo Defendants filed with the Court on March 26, 2018 a partially executed copy of the "PDVSA U.S. Litigation Trust Agreement" (the "Trust Agreement") dated July 27, 2017. On April 2, 2018, the Trust's counsel filed a fully executed and slightly different version of that agreement. The version filed by the Trust names a different PDVSA-appointed Trustee than the version filed by the Morillo Defendants, but is also dated July 27, 2017 and otherwise appears to be the same.[3]

The Trust Agreement confirms that the Trust was created "by PDVSA for the sole benefit, and on behalf of, PDVSA." (Trust Agreement § 2.4). Through the Trust Agreement, PDVSA irrevocably transferred, assigned and delivered to the Trust all of its rights and interests in the claims arising out of the alleged bribery scheme. The agreement also reveals that two weeks before the Trust was formed, PDVSA entered into an engagement letter (the "Engagement Letter") with U.S. counsel (Boies Schiller Flexner LLP and Meister Seelig & Fein LLP) (the "Trust's Lawyers") to act as counsel to the Trust. (*Id.*, Art. I).

Significantly for purposes of the challenge to the Trust's capacity to assert PDVSA's claims, the Trust Agreement recites that it was entered into by PDVSA "acting in this matter through the Minister of the People's Petroleum Power as a representative duly authorized to take action on behalf of PDVSA" and was executed on behalf of PDVSA by Nelson Martínez, the then Minister of the People's Petroleum Power. (Trust Agreement, Preamble). Mr. Martínez has since been arrested on corruption-related charges.[4] Although not designated as party to the Trust Agreement, the document was also executed by Reinaldo Muñoz Pedroza, who was at the time and remains Venezuela's *Procurador General de la República* (Attorney General). The other parties to the Trust Agreement are the three Litigation Trustees: the PDVSA appointee, Alexis Arellano Bolívar, *Gerente General de Administración* (General Business Manager) of the Ministry of the People's Petroleum Power, and the two appointees of the Trust's Lawyers, Vincent Andrew of Private Capital Advisors, Inc. in New York City and Edward P. Swyer of The Swyer Companies in Albany, New York. (*Id.*, § 4.1). In the version of the Trust

[3] The Trust Agreement as submitted by the Morillo Defendants is found at Docket Entry 161-1 and the version submitted by the Trust can be found at Docket Entry 221-14 in Case No. 1:18-cv-20818-DPG in the United States District Court for the Southern District of Florida, Miami Division.

[4] The stated reason for Martinez's arrest was that he allegedly allowed a CITGO refinancing deal to proceed without the approval of the Venezuelan government. *See Venezuela's Ex-Oil Minister and Ex-PDVSA Head Arrested*, BBC News (Nov. 30, 2017), available at http://www.bbc.com/news/world-latin-america-42182289.

Agreement submitted by the Morillo Defendants, the PDVSA-appointed Trustee was Miguel Bolívar, the Corporate Treasury Manager at PDVSA.[5]

Although the Litigation Trustees are generally responsible for managing the Trust's assets (including its claims against the defendants and the recoveries on such claims), when it comes to settling any claims, the Trustees' decision must be unanimous and must be taken in "consultation with" the Venezuelan Attorney General. (Trust Agreement § 3.3(a)). Any distribution of proceeds to PDVSA is then "subject to the approval of the" Attorney General. (*Id.*, § 3.6(a)). All notices "to PDVSA" under the Trust Agreement are to be sent to a legal consultant within the Ministry of the People's Petroleum Power. (*Id.*, § 9.9(b)). PDVSA, however, retained the right to determine along with the Trust's Lawyers the compensation to be paid to the Litigation Trustees. (*Id.*, §4.4(a)).

As to the financial arrangements underlying the Trust, many of those details appear to be contained in the Engagement Letter, which, although identified as an exhibit to and made a part of, the Trust Agreement, has not been filed with the court by either side. Nonetheless, the Trust Agreement contains some clues. First, the Trust Agreement recites that an entity called "Algamex" "may provide funding to fund the fees, expenses, and costs of the Litigation Trust," but that "[a]ny failure or inability of the Litigation Trust to obtain funding will not affect the enforceability of the Litigation Trust." (*Id.*, § 2.3). Second, the Trust Agreement provides that in "accordance with the Engagement Letter, all expenses of prosecuting the [litigation claims], including payments to all professionals, shall be borne by parties receiving 66% of the Proceeds of the [litigation claims]." (*Id.*, §3.5(d)). The term "Proceeds" is defined as "the actual consideration, if any, received as a result of any judgment, settlement, or compromise of any of the [litigation claims], *provided, however*, that, as contemplated in the Engagement Letter, the Litigation Trust shall not receive more than 34% of the final amount of Proceeds." (Trust Agreement, Annex A) (emphasis in original). Thus, it would appear that unlike the more typical structure in contingency fee cases where expenses are advanced by counsel but deducted from gross proceeds *before* the allocation of the net proceeds between the lawyers and the client, here the Trust's Lawyers are to receive 66% of the gross proceeds to cover their advancement of expenses and their contingency fee interest, with PDVSA, as Trust beneficiary, being capped at recovering no "more than 34% more of the final amount of Proceeds."

III. Defendants' Challenges to the Trust's Standing

The fact that certain of the defendants were able to obtain a copy of the Trust Agreement facilitated their making a preliminary challenge to the standing of the Trust.

a. The Venezuelan and New York Law Issues

The defendants contend that the Trust Agreement is null and void under Venezuelan law because: (1) the Minister of the People's Petroleum Power did not have the legal authority to enter into or execute the contract of behalf of PDVSA, and (2) the Trust Agreement was not approved by the National Assembly, as is required to validate international contracts of Venezuelan public companies. The defendants support their position with a lengthy opinion of a

[5] Docket Entry 161-1 at 8, 16.

Venezuelan law expert, who argues that under PDVSA's bylaws, only the Board of Directors of PDVSA has the power to authorize contracts and only the President of the Board, with the Board's prior authorization, may properly execute those contracts. Because neither the Minister of the People's Petroleum Power or the Attorney General appear to have had prior authorization from the PDVSA Board, their actions cannot bind PDVSA and the contract cannot be considered valid to transfer PDVSA's claims to the Trust, according to the defendants' expert.

Additionally, defendants contend, Venezuelan law requires that the National Assembly, Venezuela's legislature, approve all public interest contracts entered into by public companies. The defendants' expert concludes that because PDVSA is a public company and the Trust Agreement is a public interest contract, it was required to be submitted to the authorization of the National Assembly in order to be valid.

The defendants also challenge the Trust Agreement under New York law for several reasons. First, they claim that the Trust Agreement does not comply with the requirements of New York's Estates, Powers and Trusts Law, which governs New York trusts, because its execution by the Litigation Trustees was not witnessed or acknowledged by a notary public. Second, the defendants argue that the Trust Agreement violates the Rule Against Perpetuities. And third, they argue that the property used to fund the trust (PDVSA's litigation rights arising out of the alleged bribery scheme) is too broad and speculative to be accurately identified.

b. The Trust's Response

The Trust's response to date on the standing issues under Venezuelan law relies primarily on the position that the defendants' challenge to the Trust's validity is barred by the Act of State doctrine. The Act of State doctrine "precludes any review whatever of the acts of the government of one sovereign State done within its own territory by the courts of another sovereign State." *First Nat. City Bank v. Banco Nacional de Cuba*, 406 U.S. 759, 763 (1972). Under the doctrine, U.S. courts must generally deem valid any act of a foreign sovereign taken within that sovereign's own jurisdiction. *W.S. Kirkpatrick & Co. v. Envtl. Tectonics Corp., Int'l*, 493 U.S. 400, 404 (1990).

Because the defendants challenge the power of Venezuelan government officials to enter into the Trust Agreement, the Trust argues that the court is being asked to evaluate the acts of a sovereign that occurred within the borders of Venezuela and constituted public acts of Venezuelan officials. Consequently, the Trust argues that the U.S. court is obliged to refrain from questioning whether the Trust Agreement was validly entered into under Venezuelan law. The Trust also disputes the defendants' interpretation of Venezuelan law, and has indicated that it will submit a contrary legal opinion, though it has not yet done so.

The Trust has also responded to the defendants' arguments under New York law, including by submitting an acknowledgement form signed by Litigation Trustees Vincent Andrew and Edward Swyer and notarized on April 2, 2018 confirming that they had signed the Trust Agreement.

c. Analysis

The most interesting aspect of the defendants' standing challenge is the issues raised under Venezuelan law, first whether the Act of State doctrine precludes the Florida court from examining the authority issue at all, and even if it is not precluded from doing so, whether it has another reason not to delve into the intricacies of Venezuelan law.

Though neither side has yet briefed this point, it is significant that the Trust Agreement includes a New York choice of law clause, that states: "This Litigation Trust Agreement shall be governed by, and construed and enforced in accordance (sic) the laws of the State of New York, without giving effect to the principles of conflicts of law thereof." (Trust Agreement § 9.3). This unqualified choice of law clause differs from the provision in the Republic's bonds, which subject the bonds to New York law, but states that: "Authorization and execution of this agreement by the issuer, however, shall be governed by the laws of the Republic of Venezuela."[6] The Trust Agreement further includes a broad arbitration clause requiring that any dispute, including over the "validity" of the agreement, "shall be determined by binding arbitration in New York City." (*Id.*, § 9.4). The agreements to apply New York substantive law to all issues of "enforce[ment]" and to arbitrate any disputes between PDVSA and the Litigation Trustees over the "validity" of the Trust Agreement in New York have two potential ramifications to the standing debate between the Trust and defendants.

The first ramification is that the election of New York law and of arbitration of disputes in New York undermines any defense based on the Act of State doctrine. That is because the doctrine applies only to acts of a sovereign that are taken within the sovereign's borders under color of that sovereign's laws.[7] After all, the doctrine's rationale is to avoid the affront of a U.S. court invalidating the decisions taken by a foreign sovereign within its own territory under its interpretation of its own laws. A corollary to this principle is that Act of State doctrine also applies only to those acts completed within the physical territory of the foreign state.[8] Here, the express choice by the Venezuelan Minister of the People's Petroleum Power and the Attorney General to (a) subject the enforceability of the purported assignment of PDVSA's litigation claims to the Trust to New York law and to arbitration in New York, and (b) transfer PDVSA's litigation claims to a New York-domiciled trust for purposes of pursuing those claims in courts

---

[6] *See* Fiscal Agency Agreement Among the Bolivarian Republic of Venezuela, Banco Central de Venezuela, Deutsche Bank AG and Bankers Trust Company, dated July 25, 2001 at § 12; Fiscal Agency Agreement Among the Republic of Venezuela, Banco Central de Venezuela, and the Chase Manhattan Bank, dated August 6, 1998, at § 12.

[7] *See Federal Treasury Enterprise Sojuzplodoimport v. Spirits Intern. B.V.*, 809 F.3d 737, 743 (2d Cir. 2016). In *Federal Treasury Enterprise*, a Russian state-owned entity brought a trademark infringement action against defendants who allegedly usurped the trademark rights to Stolichnaya® vodka in the United States. The defendants argued that the Russian plaintiff did not have standing to bring the claim because the Russian government had improperly assigned the intellectual property rights associated with the Stolichnaya mark to the plaintiff. The Second Circuit held that a U.S. court is precluded from examining the validity of an assignment of intellectual property rights by the Russian government to a Russian entity because "the Russian Federation's Decree was the act of a foreign sovereign . . . 'done' within the boundaries of Russia." *Id.*

[8] *See Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 425 (1964) ("The courts of one independent government will not sit in judgment upon the validity of the acts of another *done within its own territory*.").

outside of Venezuela, render those acts not subject to Venezuelan law and to resolution outside of Venezuela, thereby undermining the essential premises of the Act of State doctrine.[9]

Second, even if the Act of State doctrine would not bar looking at the validity of the Trust Agreement under Venezuelan law, there is a separate question as to whether the Court should do so. Ordinarily, where a contract is silent as to choice of law, the question of whether the signatory had the actual authority to bind a foreign state-owned corporation would be decided under the law of that corporation. The Trust Agreement, however, contains a New York choice of law provision. In *IRB-Brasil Resseguros, S.A. v. Inepar Investments* and *Ministers and Missionaries Benefit Board v. Snow*, the New York Court of Appeals confirmed that a New York choice of law provision in an agreement (including an instrument governed by the NY Estates, Powers and Trusts Law ("EPTL")) mandates the application of New York substantive law, including to the validity of the instrument and authority of its signatories, even where application of foreign law would yield a different result than applying New York law.[10] Accordingly, although neither party has yet raised the Trust Agreement's choice of law and dispute resolution clauses, the Florida Court may determine that although it is not barred by the Act of State doctrine from considering Venezuelan law, the choice of New York law requires that only the substantive law of New York be applied to decide the issue of the Trust Agreement's validity.

As a practical matter, it is possible that the court's decision on the Trust's validity may be influenced in part by whether PDVSA and/or the National Assembly weigh in on these issues of authority of the Ministry of the People's Petroleum Power to bind PDVSA and the effectiveness of the agreement absent National Assembly approval. The National Assembly is reportedly investigating the execution of the Trust Agreement for compliance with Venezuelan law. The Court could thus receive conflicting views regarding the Trust Agreement's validity, not just from legal experts hired by the parties, but from PDVSA itself and various persons within the Venezuelan government.

In short, as anticipated in our prior article, the standing issues are complicated in this case and create a significant early hurdle for the Trust to overcome if this action is to proceed to the merits.

---

[9] By contrast, in the Stolichnaya trademark case, the Court of Appeals found that the validity of the challenged assignment "is a question of Russian law decided within Russia's borders, rather than a matter of U.S. law with a situs in the United States." *Federal Treasury Enterprise Sojuzplodoimport*, 809 F.3d at 744.

[10] *IRB-Brasil Resseguros, S.A. v. Inepar Investments, S.A.*, 20 N.Y. 3d 310, 315 (2012) (finding that choice of law clause meant New York substantive law applied to determine the validity of a contractual guarantee under General Obligations Law § 5-1401 even though application of Brazilian law would arguably have resulted in the agreement being void for the signatories' lack of actual authority and affirming validity of the guaranty under the New York law doctrine of ratification). In *Ministers and Missionaries Ben. Bd. v. Snow*, 26 N.Y. 3d 466, 468 (2015), the Court of Appeals extended the *IRB* holding "to contracts that do not fall under General Obligations Law § 5-1401 including a retirement plan subject to the EPTL, and clarif[ied] that this rule obviates the application of both common-law conflict-of-laws principles and statutory choice-of-law directives, unless the parties expressly indicate otherwise."

IV. Other Legal Issues

In addition to the standing issue, the filings to date foreshadow a number of interesting legal arguments about the claims being asserted and provide additional information that may shed light on some of the questions we previously raised.

a. RICO Injury—As noted in our prior article, a federal civil RICO claim requires that the plaintiff allege and prove a domestic injury to business or property and does not permit recovery for foreign injuries.[11] In its Complaint, the Trust alleged that PDVSA suffered a domestic injury because it incurred losses to its U.S. bank accounts. It also argues that PDVSA's ability to buy and sell certain products in the U.S. decreased as a result of the defendants' alleged scheme, and that this loss of U.S. business constitutes a domestic injury. In arguing that a preliminary injunction is unwarranted because the RICO claim is unlikely to succeed on the merits, the defendants assert that this allegation does not suffice to show a domestic injury. Even if PDVSA's bank accounts received less money because of a scheme to depress prices for PDVSA's oil sales, the defendants argue that PDVSA has no property located in the U.S. that was stolen or harmed. Rather, they contend, the Trust "alleges a theft of information *from Venezuela* and the bribery of officials *in Venezuela* in a scheme orchestrated by 'two *Venezuelan* nationals.'"[12]

Even if but for a RICO violation, PDVSA would have received more money into its U.S bank account and even if that qualifies in principle as a domestic injury, it is not clear, as a factual matter, what portion of the billions of dollars in damages the Trust is claiming would have been deposited in PDVSA's U.S. bank account. It is one thing for the proceeds of dollar-denominated transactions such as those alleged in the Complaint to be wired through correspondent bank accounts in the United States en route to their final destination in a PDVSA account, but it is another matter entirely to say that, in the ordinary course, PDVSA maintains bank accounts in the U.S. which are the final destination of such wire transfers. If the Trust is essentially arguing that the destination of the proceeds of much of PDVSA's sales or purchases of hydrocarbon products is to U.S. bank accounts in PDVSA's name, that would be welcome news to numerous creditors who have been searching and will continue to search in earnest for attachable PDVSA assets in the United States.

b. Cooperation from PDVSA—In our prior article we noted the potential consequences were the Trust to be unable to comply with discovery requests because it lacked access to PDVSA's books, records and witnesses. Although the Trust Agreement expressly states that PDVSA transferred "all of their (sic) respective rights, title and interests in and [] any privilege or immunity attaching

---

[11] See *RJR Nabisco, Inc., et al v. European Community et al*, 136 S. Ct. 2090, 2111 (2016).

[12] Defendants' Joint Response in Opposition to Plaintiff's Motion for a Preliminary Injunction, *PDVSA US Litigation Trust v. Lukoil Pan Americas LLC, et al.*, Case No. 1:18-cv-20818-DPG (Mar. 26, 2018) (Docket Entry 161 at 24) (emphasis in original).

to any documents or communications (whether written or oral) associated with the [claims]," (Trust Agreement § 2.2(b)), the agreement contains no provision by which PDVSA agrees to provide information or cooperate with the Litigation Trustees in their pursuit of the assigned claims against the defendants. Such cooperation/access to information and witnesses clauses are common in agreements transferring claims to litigation trusts, because by definition the trust would otherwise have none of the documents, information or employees necessary to pursue the assigned claims. It is conceivable that such issues are addressed in the Engagement Letter between PDVSA and the Trust's Lawyers or that counsel for PDVSA and the Trust received an extensive download of information and documents before the suit was filed. But if not, the cooperation and information access issue may become significant, particularly if PDVSA takes a position contrary to the Trust on the standing question.

c. Attachment Risk—The Trust Agreement confirms that PDVSA is the sole beneficiary of the Trust and that, after deducting legal fees and other expenses, PDVSA has the right to receive all remaining recoveries even if in total that is no more than 34% of the aggregate proceeds. PDVSA also appears to have exercised and continues to exercise significant control over the litigation process by retaining the law firms who are prosecuting the claims assigned to the Trust, by purporting to appoint one of the three Trustees, and by having control over the Trustees' compensation. This evidence of control may increase the chance of a court finding that the Trust's separate legal status cannot shield its assets from PDVSA's creditors.

It is also worth noting that the Trust Agreement's execution may have implications for the various Republic creditors asserting that PDVSA is the alter ego of the Republic. It is notable that the Trust Agreement was entered into on PDVSA's behalf by the Minister of the People's Petroleum Power and with the consent of the Attorney General of Venezuela. Further, the Attorney General's approval is required in order for the Trust to distribute any proceeds of the litigation to PDVSA. Indeed, no PDVSA employee is entitled to receive any notices of information communicated in accordance with the Trust Agreement. The fact that government officials and no PDVSA officer executed the Trust Agreement and have the ability to dictate if and when PDVSA receives the benefits of PDVSA's litigation claims suggests significant control of PDVSA's assets and decision making by the Republic. This type of government control over PDVSA's operations and assets – if the Trust Agreement's validity is sustained – may lend additional credence to the argument that PDVSA is the alter ego of the Republic, an issue that is currently pending before the Delaware district court in proceedings by Crystallex International Corporation to seek to enforce against assets of PDVSA a $1.4 billion judgment against the Republic.[13]

[13] As discussed in the authors' prior article, *Venezuela's Imminent Restructuring and the Role Alter Ego Claims May Play in this Chavismo Saga*, https://www.clearygottlieb.com/~/media/organize-archive/cgsh/files/2017/publications/venezuela-alter-ego--cooper-morag-11-9-2017.pdf, Crystallex International

V. Conclusion

The U.S. PDVSA Litigation Trust suit entails a number of significant procedural and substantive hurdles. First, the court will have to wade through the competing arguments on the standing question to determine whether the Trust may pursue claims on behalf of PDVSA. After that, the Trust will face continued opposition to its motion for preliminary injunction, and defendants have announced that they intend to file, motions to dismiss the various causes of action. Resolution of the standing issue may have implications not just for this case, but for whether PDVSA may be bound by the Venezuelan government to any future debt restructuring and the extent to which National Assembly approval is required for such a restructuring. More immediately, however, the Court will rule on the likely motions to dismiss. That ruling, assuming that the case is not dismissed, could indirectly incentivize financial creditors of PDVSA and the Republic to seek to obtain value for themselves from the Trust's claims. Finally, the fact that PDVSA may only have a maximum interest of 34% of the proceeds recovered by the Trust under the Trust Agreement could diminish financial creditors' interest in attempting to seek to enforce their claims against the Trust and raise further questions about the circumstances of its creation.

Corporation is currently litigating whether PDVSA is the alter ego and liable for the debts of the Republic as part of its ongoing enforcement efforts.