

U.S. Sanctions New Debt and Equity Issuances by Venezuelan Government

August 25, 2017

On August 25, 2017, President Trump issued an [Executive Order](#) severely restricting transactions in debt and equity of the Government of Venezuela and of state-owned entities, including Petroleos de Venezuela, S.A. (PdVSA). Simultaneously with the Executive Order, OFAC issued a number of general licenses and [Frequently Asked Questions](#) relating to the new sanctions. These new actions build on sanctions targeting Venezuelan officials, discussed [here](#), and continue the trend toward targeted “bespoke” sanctions short of full blocking of all transactions with a targeted regime or country.

The new sanctions:

- Prohibit dealings in existing debt of the Government of Venezuela (and its controlled entities) by U.S. persons or within U.S. jurisdiction, subject to an [extensive list of exceptions](#) for specified issuances;
- Prohibit all dealings by U.S. persons or within U.S. jurisdiction in new debt of the Government of Venezuela with a duration of longer than 30 days and of PdVSA with a duration of longer than 90 days, or new equity of any state-controlled entity;
- Bar the purchase of securities from the Government of Venezuela within U.S. jurisdiction, other than permitted new debt; and
- Bar all distributions of profits and earnings within U.S. jurisdiction to the Government of Venezuela by state-owned entities.

If you have any questions concerning this memorandum, please reach out to your regular firm contact or the following author

WASHINGTON
2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
T: +1 202 974 1500
F: +1 202 974 1999

Paul Marquardt
+1 202 974 1648
pmarquardt@cgs.com



I. Debt and Equity Restrictions of the Executive Order

The Executive Order prohibits transactions in four categories of debt and equity:

- Debt of the Government of Venezuela issued prior to August 25, 2017, subject to a long list of specific exceptions;
- Debt of the Government of Venezuela issued on or after August 25, 2017, with a duration of longer than 30 days;
- Debt of PdVSA issued on or after August 25, 2017, with a duration of longer than 90 days; and
- New equity of the Government of Venezuela.

The Executive Order defines the “Government of Venezuela” to include any agency or instrumentality of the government and any entity owned or controlled by the government, including the Central Bank of Venezuela and PdVSA. Under existing OFAC precedent, OFAC will also consider any entity 50% or more owned by PdVSA or the Government of Venezuela, directly or in a chain of subsidiaries at least 50% owned by sanctioned persons, to be a sanctioned person. Thus, the test is either control or a chain of 50% ownership. All debt issuances of greater than the relevant duration by any such state-linked entity,¹ and all equity issuances of such entities, will be restricted.

However, with respect to restrictions on trading in the existing debt of the Government of Venezuela, [General License 3](#) provides that the restrictions do not apply to an [extensive list](#) of existing issuances. General License 3 also exempts bonds issued by U.S. persons controlled by the Government of Venezuela, including CITGO Holding Inc. and its subsidiaries.

These prohibitions apply to U.S. persons and to dealings within the United States. That means that the prohibitions apply to transactions settled through U.S. institutions as well, whether as a result of clearing U.S. dollar payments through U.S. correspondent accounts

¹ Although PdVSA is the “Government of Venezuela,” OFAC guidance clarifies that the longer debt limit controls.

or of clearing transactions in securities held in custody within the United States or by U.S. persons.

Existing precedent under the Ukraine-related sanctions programs also indicates that OFAC will take a very wide, substance over form view of what constitutes “debt,” which will include not only traditional bonds and bank loans but all other forms of extensions of credit, including (for example) repo agreements, term deposits, and extended payment terms. Similarly, “equity” will be read broadly to cover any evidence of title or ownership.

These restrictions only apply to debt with respect to which the Government of Venezuela is obligor and do not, for example prohibit extensions of credit in which a Government of Venezuela entity acts as lender or to purchase goods from a Government of Venezuela entity.

These sanctions are not blocking sanctions, and so any attempted transaction violating the restrictions above must be rejected (refused) rather than blocked (with assets frozen in a separate account and reported to OFAC).

II. Distribution Restrictions of the Executive Order

The Executive Order prohibits dividend payments and distributions of profits to the Government of Venezuela from any entity it owns or controls, directly or indirectly, by a U.S. person or within the United States. As above, this prevents any U.S. dollar distributions from Venezuelan-owned entities that clear through U.S. correspondent accounts (as the vast majority of interbank transfers do). It also prohibits distributions from CITGO, a major subsidiary of PdVSA located in the United States.

III. Investment Restrictions of the Executive Order

The Executive Order prohibits the purchase, directly or indirectly, by a U.S. person or within the United States of securities from the Government of Venezuela (other than permitted debt described above). This prohibition has interesting implications.

The prohibition is not limited to securities issued by Venezuelan entities, nor is it limited to debt. Thus, for

example, it appears that U.S. Treasury bonds held by the Venezuelan government could not be sold, as they would be held within the United States. It would also appear that any U.S. dollar payment creates at least some risk that a securities purchase could be found to be “within the United States” as a result of interbank U.S. dollar clearing. OFAC guidance issued together with the new sanctions indicates that the U.S. is targeting the Government of Venezuela’s attempts to liquidate assets, perhaps at “fire sale” prices, to meet short-term financing needs.

It is unclear what would constitute indirectly buying securities “from” the Government of Venezuela; for example, if the government were to sell a large securities position to a third party in Europe and that third party were in turn to try to sell some of those securities to U.S. persons, it is unclear how OFAC would view the on-selling transactions.

Finally, the indirect purchase prohibition seems to create a risk with respect to any mutual fund or other collective investment vehicle that invests in new securities issued by an entity controlled by the Government of Venezuela.

IV. Effective Date and Exceptions

The sanctions are generally effective immediately. However, [General License 1](#) provides that any transaction ordinarily incident to winding down a contract entered into prior to August 25, 2017, that is prohibited by any of the trading restrictions on debt or securities is permissible, so long as the wind-down transactions do not otherwise violate sanctions and are completed by September 24, 2017. Such wind-down transactions are subject to a reporting requirement to OFAC. The grandfathering provisions do not apply to distributions of dividends or profits to the Government of Venezuela. OFAC’s guidance also indicates that, as with Russian debt, future drawdowns on facilities for which all material terms were contractually committed prior to the effective date of sanctions are not prohibited so long as no material amendment to the terms of the debt is made.

CITGO Holding Inc. and its subsidiaries, the U.S. operations of PdVSA, are exempted from the restrictions on new debt and equity and the purchase of securities by [General License 2](#) (so long as no other entity owned or controlled by the Government of Venezuela is involved) Again, dividends or other distributions of profits to the Government of Venezuela (or PdVSA) are not exempted.

Finally, [General License 4](#) permits dealings in otherwise prohibited debt to finance the exports or re-exports from the United States or by a U.S. person destined for Venezuela of agricultural commodities, medicine, and medical devices.

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