Nationalizing the Hydrocarbon Industry in Venezuela

Venezuela Holdings, BV, Mobil Cerro Negro Holding, Ltd., Mobil Venezolana de Petróleos Holdings, Inc., Mobil Cerro Negro, Ltd., and Mobil Venezolana de Petróleos, Inc. v The Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/27, Award, 9 October 2014 (Gilbert Guillaume, Gabrielle Kaufmann-Kohler, Ahmed Sadek El-Kosheri)

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Investment treaty arbitration offers few awards on nationalizations. The Award in Mobil v Venezuela (Mobil) is one of them. Maybe because of this, it is a rather disappointing decision to read for those concerned with international investment law. The Claimants (Venezuela Holdings, Mobil Cerro Negro Holding, Mobil Venezolana de Petróleos Holdings, Mobil Cerro Negro and Mobil Venezolana de Petróleos) alleged violations of the provisions on expropriation, fair and equitable treatment (FET) and arbitrary or discriminatory measures of the 1991 Netherlands-Venezuela bilateral investment treaty (the BIT).1 In the Award, the Tribunal did not elaborate on the rich case law available on expropriation and FET. Instead, the Tribunal simply repeated some of the criteria already put forward by other international investment tribunals on these issues, scarcely citing any of their awards. The Tribunal focused primarily on the quantum of the nationalized investments, a topic that is generally best suited for accountants rather than lawyers. The facts of the dispute partly explain this situation. They also provide a rare opportunity to remind us how nationalizations work.

1 This now terminated BIT entered into force in 1993.
Venezuela formally expropriated its hydrocarbon industry in 1975, through the nationalization law of that year (para. 35). This law created Petróleos de Venezuela (PDVSA), a State-owned entity which carried out industrial and commercial activities for the next 15 years, without any participation from private entities (paras. 37–38). In the 1980s, Venezuela decided to develop the extra-heavy hydrocarbon reservoirs of the Orinoco belt and other geographical areas (paras. 38–39). Known as the oil opening, this new policy of Venezuela authorized PDVSA to enter into operating service agreements and association agreements or joint ventures with private companies (para. 40). It also considered the adoption of economic incentivization measures designed to encourage investment, such as the reduction of the income tax rate and of the applicable royalty to private companies operating in the hydrocarbon industry via association agreements with PDVSA (paras. 41–44). Following this new policy of the Venezuelan State, Mobil Corporation entered into two joint venture projects with PDVSA in 1990: one to exploit extra-heavy crude in the Orinoco belt – the Cerro Negro project; and another to explore and exploit light and medium crude adjacent to Lake Maracaibo – the La Ceiba project (para. 45).

When Hugo Chávez became president of Venezuela in 1998, the fate of Mobil Corporation and other foreign investors began to change (para. 86). Exercising delegated legislative powers, the Chávez administration issued a new law on hydrocarbons in 2001, replacing the 1975 nationalization law and the 1943 hydrocarbons law. According to this new law, oil production activities were to be reserved to the State, and private entities would only be authorized to participate in them through mixed enterprises where the State has to own more than 50% of the shares. The entire production of these mixed enterprises would be subject to a 30% royalty rate and would have to be sold to PDVSA or another State-owned company (para. 88). By then, both the Cerro Negro and La Ceiba projects had standing association agreements with Venezuela, providing for different conditions. In 2001 and 2002, the Chávez administration reassured foreign investors that their pre-existing association agreements would be respected (para. 89). In spite of this, Venezuela informed Mobil Corporation in 2004 and 2005 that, under Chávez’s orders, the Ministry of Energy and Mines (the Ministry) was increasing the previously guaranteed 1% royalty rate for both projects to 16.66% (paras. 90–92). The Ministry also informed the Claimant in 2005 that, in conformity with the 2001 hydrocarbons law, the Cerro Negro project would be subject to a 30% royalty rate for average monthly production exceeding 120,000 barrels per day (para. 93).

These were not the only measures adopted by Venezuela that affected foreign investors in the hydrocarbon industry. In 2006, the National Assembly enacted