

# Alert

## Sanctions Update: OFAC Sanctions Venezuela's State-Owned Oil Company

February 8, 2019

On Jan. 28, 2019, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") designated Petróleos de Venezuela S.A. ("PdVSA"), the state-owned oil company, as a specially designated national ("SDN"). OFAC also simultaneously issued eight new general licenses and amended one already-existing general license.<sup>1</sup> In addition, on Jan. 31, 2019 and Feb. 1, 2019, OFAC issued new and amended Frequently Asked Questions ("FAQs"), as well as amendments to two of the previously issued general licenses.<sup>2</sup>

As a result of OFAC's action, U.S. persons are now generally prohibited from engaging in transactions with PdVSA and generally must block property interests of PdVSA in their possession or control. However, there are a number of exceptions to these restrictions, as reflected in the new and amended general licenses issued by OFAC in connection with the designation of PdVSA. Careful attention to the new sanctions and general licenses is advised for U.S. persons who have ties to or deal in PdVSA or its securities.

### I. OFAC Designation of PdVSA as SDN

On Jan. 25, 2019, President Trump signed Executive Order ("E.O.") 13857 titled "Taking Additional Steps to Address the National Emergency with Respect to Venezuela." The new E.O. broadens the reach of previously issued E.O.s (13692, 13808, 13827, 13835 and 13850), by amending the definition of the term "Government of Venezuela" to include any person that has acted, or purported to act, on behalf of the Government of Venezuela, including as a member of the Maduro regime. The new E.O. also specifically identifies PdVSA as included in the definition of "Government of Venezuela."<sup>3</sup>

Three days later, following a determination by Secretary of the Treasury Steven T. Mnuchin in consultation with Secretary of State Michael Pompeo that persons operating in Venezuela's oil sector are subject to sanctions pursuant to E.O.13850,<sup>4</sup> OFAC added PdVSA to its List of Specially Designated Nationals and Blocked Persons ("SDN List").

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<sup>1</sup> U.S. Department of the Treasury, "Issuance of a New Venezuela-related Executive Order and General Licenses; Venezuela-related Designation" (Jan. 28, 2019), [available here](#).

<sup>2</sup> U.S. Department of Treasury, "Issuance of Venezuela-related Frequently Asked Questions (FAQs)" (Jan. 31, 2019), [available here](#); U.S. Department of Treasury, "Issuance of Amended Venezuela-related General Licenses and Frequently Asked Questions" (Feb. 1, 2019), [available here](#).

<sup>3</sup> E.O. 13857, "Taking Additional Steps to Address the National Emergency with Respect to Venezuela" (Jan. 25, 2019) [available here](#). See also OFAC FAQ No. 649 (Jan. 28, 2019).

<sup>4</sup> E.O. 13850, "Blocking Property of Additional Persons Contributing to the Situation in Venezuela" (Nov. 1, 2018), [available here](#). For a fuller explanation of E.O. 13850, "Sanctions Update: Iran, Venezuela and Russia," *SRZ Alert*, Nov. 13, 2018, [available here](#).

Under E.O. 13850, the designation of PdVSA as an SDN means that — subject to the exceptions in the general licenses discussed below — all of its property and property interests that are in, or subsequently come within, the U.S., or that are within, or subsequently come within, the possession or control of a U.S. person, constitute blocked property. U.S. persons — again, subject to the exceptions in the general licenses — may not transfer or otherwise deal in property interests of PdVSA, or contribute or provide any funds, goods or services to or for the benefit of PdVSA, or receive any funds, goods or services from PdVSA.<sup>5</sup>

Concurrent with this action, Secretary Mnuchin released a statement that the “... designation of PdVSA will help prevent further diverting of Venezuela’s assets by [Nicolas] Maduro and preserve these assets for the people of Venezuela. The path to sanctions relief for PdVSA is through the expeditious transfer of control to the Interim President or a subsequent, democratically elected government.”<sup>6</sup>

OFAC’s new FAQs further elucidate the purpose of these sanctions: “Treasury will continue to use its economic tools to support Interim President Guaidó, the National Assembly, and the Venezuelan people’s efforts to restore their democracy.”<sup>7</sup>

## **II. New General Licenses and Related FAQs**

In connection with designating PdVSA as an SDN, OFAC amended General License 3 and also issued a number of new general licenses. The amendments to General License 3 and the new General License 9 (and immediate amendment thereto) relate to dealings in certain bonds and securities and are summarized below.

The remaining General Licenses, many of which are explained in FAQs issued by OFAC on Jan. 31, 2019, relate to (i) authorizing certain activities involving PDV Holdings Inc. (“PDVH”), CITGO Holding Inc. (“CITGO”) and Nynas AB (“Nynas”) (General Licenses 7 and 13); (ii) authorizing transactions involving PdVSA for certain entities operating in Venezuela (General License 8); (iii) authorizing the purchase in Venezuela of gasoline from PdVSA (General License 10); (iv) authorizing certain activities necessary to the maintenance or wind down of operations or existing contracts with PdVSA (General Licenses 11 and 12) and (v) authorizing transactions for the conduct of official business of the United States government by employees, grantees or contractors (General License 14).

### **A. General License 3B**

General License 3B (Authorizing Transactions Related to, Provision of Financing for and Other Dealings in Certain Bonds), issued on Feb. 1, 2019,<sup>8</sup> authorizes U.S. persons to engage in all transactions related to, the provision of financing for, and other dealings in the bonds listed in

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<sup>5</sup> E.O. 13850, §§ 1, 4. U.S. persons are also prohibited from conspiring to violate any of these prohibitions and from engaging in any transaction that evades or avoids, has the purpose of evading or avoiding, causes a violation of, or attempts to violate, these prohibitions. *Id.*, § 5.

<sup>6</sup> U.S. Department of the Treasury, Press Release, “Treasury Sanctions Venezuela’s State-Owned Oil Company Petroleos de Venezuela, S.A.” (Jan. 28, 2019), [available here](#).

<sup>7</sup> OFAC FAQ No. 660 (Jan. 31, 2019).

<sup>8</sup> General License 3B (Feb. 1, 2019), [available here](#). General License 3B replaces and supersedes in its entirety General License 3A. General License 3A was issued on Jan. 28, 2019. It, in turn, replaced and superseded the previously existing General License 3, which was issued on Aug. 25, 2017.

the Annex to the license that would otherwise be prohibited by Section 1(a)(iii) of E.O. 13808,<sup>9</sup> provided that any divestment or transfer of, or facilitation of divestment or transfer of, any holdings must be to a non-U.S. person.<sup>10</sup> Notably, PdVSA bonds that were previously listed in the Annex to General License 3 are not among those listed in the Annex to General License 3B; instead, they are now listed in the Annex to General License 9A (further discussion below).<sup>11</sup>

In addition, the license authorizes all transactions and activities (including transactions in securities and security derivatives) that are ordinarily incident and necessary to the wind down of financial contracts or other agreements involving or linked to the bonds specified in the Annex, through March 3, 2019, provided that such agreements were entered into prior to 4 p.m. EST on Feb. 1, 2019.<sup>12</sup> This allows transactions that involve or are linked to the bonds specified in the Annex that were initiated prior to the issuance of General License 3B to be wound down, including resolving the purchase and sale of securities, securities lending, repurchase agreements, and swaps and derivative contracts in securities.<sup>13</sup>

Last, the license also authorizes all transactions related to, the provision of financing for, and other dealings in bonds that were issued prior to Aug. 25, 2017 by U.S. entities owned or controlled by the Government of Venezuela, other than Nynas, PDVH, CITGO and any of their subsidiaries.<sup>14</sup>

FAQ No. 662 makes clear that, although non-U.S. persons may continue to deal in bonds specified in the Annex to General License 3B, to the extent that transactions involving the bonds specified in the Annex to General License 3B involve U.S. persons or the U.S. financial system, such transactions may not involve sales of any interests in such bonds to U.S. persons (other than as described above).<sup>15</sup>

## **B. General License 9A**

General License 9A (Authorizing Transactions Related to Dealings in Certain Securities)<sup>16</sup> authorizes transactions and activities otherwise prohibited by Section 1(a)(iii) of E.O. 13808 or E.O. 13850 that are ordinarily incident and necessary to dealings in any debt (including bonds listed on the Annex to General License 9A, promissory notes and other receivables) of, or equity in, PdVSA or any entity in which PdVSA owns (directly or indirectly) a 50 percent or greater

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<sup>9</sup> Section 1(a)(iii) of E.O. 13808 provides: “All transactions related to, provision of financing for, and other dealings in the following by a United States person or within the United States are prohibited: ... bonds issued by the Government of Venezuela prior to the effective date of this order”. See E.O. 13808, “Imposing Additional Sanctions With Respect to the Situation in Venezuela,” (Aug. 24, 2017), [available here](#).

<sup>10</sup> The license also authorizes all transactions that are ordinarily incident and necessary to facilitating, clearing and settling trades of holdings in the bonds specified in the Annex to the license, regardless of whether the sale or transfer was to a non-U.S. person, provided that such trades were placed prior to 4 p.m. EST on Feb. 1, 2019. This authorization allowed trades placed prior to Feb. 1, 2019 to settle in the ordinary course, regardless of whether the sales and transfers were to non-US persons. See OFAC FAQ No. 662 (Feb. 1, 2019).

<sup>11</sup> OFAC FAQ No. 651 (Jan. 31, 2019).

<sup>12</sup> General License 3B(c).

<sup>13</sup> OFAC FAQ No. 662 (Feb. 1, 2019).

<sup>14</sup> General License 3B(d).

<sup>15</sup> OFAC FAQ No. 662 (Feb. 1, 2019).

<sup>16</sup> General License 9A(a) (Feb. 1, 2019), [available here](#). General License 9A was issued on Feb. 1, 2019. It replaces and supersedes General License 9, which was issued on Jan. 28, 2019.

interest (together, “PdVSA securities”) issued prior to Aug. 25, 2017, provided that any divestment or transfer of any holdings in PdVSA securities must be to a non-U.S. person.<sup>17</sup> Such transactions and activities include facilitating, clearing and settling of transactions to divest to non-U.S. persons PdVSA-related securities, including on behalf of U.S. persons.<sup>18</sup>

The license also authorizes, through March 3, 2019, transactions and activities, including transactions in securities and security derivatives, otherwise prohibited by Section 1(a)(iii) of E.O. 13808 or E.O. 13850 that are ordinarily incident and necessary to the wind down of financial contracts or other agreements that were entered into prior to 4:00 p.m. EST on Jan. 28, 2019, involving, or linked to, PdVSA securities issued prior to Aug. 25, 2017.<sup>19</sup> This provision was intended to allow the wind down of agreements entered into prior to the imposition of sanctions on PdVSA, including resolving the purchase and sale of securities, securities lending, repurchase agreements, and swaps and derivative contracts in securities.<sup>20</sup>

Finally, the general license authorizes all transactions and activities that are ordinarily incident and necessary to dealings in any bonds issued prior to Aug. 25, 2017 by PDVH, CITGO and Nynas and their subsidiaries.<sup>21</sup>

The license expressly does not authorize, among other things, “U.S. persons to sell PdVSA securities to, to purchase or invest in securities of, or to facilitate such transactions with, directly or indirectly, any person whose property and interests in property are blocked pursuant to E.O. 13850” including PdVSA and any entities in which PdVSA owns a 50 percent or greater interest, “*other than purchases of or investments in PdVSA securities (including settlement of purchases or sales that were pending on January 28, 2019) that are ordinarily incident and necessary to the divestment or transfer of PdVSA securities*” (emphasis added).<sup>22</sup>

Ultimately, U.S. persons may continue to hold their interests in PdVSA debt and equity issued prior to Aug. 25, 2017, but there are restrictive requirements on the sale of those interests in the secondary market — specifically, U.S. persons may not sell their interests to another U.S. person, to PdVSA itself or its subsidiaries, or to another SDN. Moreover, General License 9A generally does not authorize U.S. persons to purchase or acquire new interests in PdVSA bonds, debt or equity (including the bonds listed in the Annex to General License 9A), except that, to the extent that divesting or transferring PdVSA-related debt or equity from a U.S. person to a non-U.S. person requires engaging in certain securities-related transactions (such as purchasing or settling purchases of PdVSA debt or equity), U.S. persons may engage in such transactions.<sup>23</sup>

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<sup>17</sup> General License 9A(a).

<sup>18</sup> General License 9A(b). In addition, the license authorized transactions and activities that were ordinarily incident and necessary to facilitating, clearing, and settling trades of holdings in PdVSA securities described above, provided that such trades had to be placed prior to 4:00 p.m. EST on January 28, 2019. As with General License 3B, this authorization was intended to allow trades that were initiated prior to the imposition of blocking sanctions on PdVSA to settle in the ordinary course to both U.S. and non-U.S. persons. See General License 9A(c) and OFAC FAQ No. 661 (Feb. 1, 2019).

<sup>19</sup> General License 9A(d).

<sup>20</sup> OFAC FAQ No. 661 (Feb. 1, 2019).

<sup>21</sup> General License 9A(e).

<sup>22</sup> General License 9A(f)(2).

<sup>23</sup> OFAC FAQ No. 661 (Feb. 1, 2019).

In sum, while non-U.S. persons may continue to deal in PdVSA debt and equity, involvement by U.S. persons or the U.S. financial system must be in compliance with the terms of General License 9A, which generally prohibits U.S. persons from purchasing such securities.<sup>24</sup>

FAQ No. 650 addresses the level of due diligence associated with ensuring that transfers or divestment of debt in blocked persons are consistent with General License 9A — namely, that such divestment is actually made to a non-U.S. person. OFAC expects firms to conduct due diligence on their own direct customers and firms otherwise may “rely upon the information ordinarily available to them.”<sup>25</sup> However, consistent with FAQ No. 116, if a firm has “information in its possession leading it to know or have reason to know” that the buyer is a U.S. person, then it may be held responsible if it does not take steps to prevent the trade from being consummated.<sup>26</sup>

The new FAQs specify that mutual funds and exchange traded funds that are U.S. persons may not buy, sell or otherwise engage in transactions related to debt, equity or other holdings in SDNs (such as PdVSA), unless authorized by a general or specific license.<sup>27</sup> A U.S. fund that contains such blocked holdings is generally not considered a blocked entity, U.S. persons may continue to invest in the fund and the fund may continue to operate. The fund may divest itself of blocked holdings only with OFAC authorization.<sup>28</sup>

In addition, the new FAQs clarify that U.S. (and non-U.S.) persons may continue to constitute, offer and trade in synthetic exchange traded funds which track baskets of debt, equity or other holdings in an SDN to provide a return approximating the returns on such baskets, so long as the “underlying basket being tracked includes less than a predominant share by value of debt, equity, or other holdings in blocked persons.”<sup>29</sup>

### III. Duration of PdVSA Sanctions

The FAQs indicate that the sanctions imposed on PdVSA are likely to continue until a “bona fide transfer of control” to Interim President Guaidó or a democratically elected government is accomplished. In the interim, “Treasury will continue to use its economic tools to support Interim President Guaidó, the National Assembly and the Venezuelan people’s efforts to restore their democracy.”<sup>30</sup>

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If you have any questions concerning this *Alert* or would like assistance complying with the new requirements, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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<sup>24</sup> *Id.*

<sup>25</sup> OFAC FAQ No. 650 (Jan. 31, 2019).

<sup>26</sup> *Id.*

<sup>27</sup> OFAC FAQ No. 652 (Jan. 31, 2019).

<sup>28</sup> *Id.*

<sup>29</sup> OFAC FAQ No. 653 (Jan. 31, 2019).

<sup>30</sup> OFAC FAQ No. 660 (Jan. 31, 2019).

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