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LEGAL PROTECTIONS AVAILABLE WHEN FOREIGN NATIONS NATIONALIZE INDUSTRIES

by
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On February 13, 2008, Judge Deborah A. Batts of the U.S. District Court for the Southern District of New York confirmed the attachment of assets belonging to the national Venezuelan oil company (Case No. 07cv11590). At least \$315 million remain frozen in an account at the Bank of New York. The dispute between American oil company ExxonMobil and state-owned Petroleos de Venezuela S.A. (PDVSA), concerns the June 2007 “nationalization” of the Cerro Negro heavy crude exploration and processing project in the Orinoco basin. In July 2007, the Venezuelan government added insult to injury when it also hit ExxonMobil’s subsidiary with a claim for back taxes based on the incorrect application of a U.S.-Venezuela tax treaty. At the end of the period granted by the government, the parties failed to reach a satisfactory agreement to convert the strategic joint venture, which was operated by ExxonMobil, into a “mixed capital” company 60% owned by PDVSA.

Seven out of eleven oil companies involved in the expropriation reached agreements with the Venezuelan government. The remaining four – ConocoPhillips, ExxonMobil, Petro-Canada and OPIC – tried to negotiate the payment of the compensation to which they are entitled after being forced to withdraw from the projects. In its memorandum in support of the attachment, ExxonMobil claimed that the government of Venezuela breached their agreement by taking a discriminatory action against the company, because the expropriation measure does not apply equally to all corporations in the “Bolivarian” Republic of Venezuela. PDVSA responded by claiming that ExxonMobil had “unclean hands,” because it did not disclose its legal strategy during the renegotiation of the venture’s debt for which the \$315 million were intended. In her ruling, Judge Batts said that ExxonMobil would likely prevail in the dispute. In addition, the PDVSA subsidiary involved is removed enough from the Venezuelan government not to enjoy sovereign immunity.

ExxonMobil also shocked Venezuelan authorities with the filing of a Mareva injunction in British court, a legal remedy considered by experts to be a judicial nuclear weapon that leaves defendants virtually powerless. This is a type of early, interlocutory, ex-parte injunction, used in Commonwealth jurisdictions, that prevents civil defendants from disposing of assets before a judgment is made. Within days, PDVSA woke up to \$12 billion in assets frozen in the United Kingdom, where it indirectly owns two refineries, in the Netherlands and the Netherlands Antilles. Venezuela's oil minister Rafael Ramirez described these actions as “legal terrorism.” Venezuela

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even presented the case before the Organization of Petroleum Exporting Countries (OPEC), which backed Venezuela in a written declaration of the last ministerial meeting, held on March 5 in Vienna.

These actions were initiated by ExxonMobil in London and New York City in advance of the start of an arbitration procedure before the International Chamber of Commerce in New York City. It was the second arbitration sought by ExxonMobil since last year when it brought a case before the International Centre for Settlement of Investment Disputes (ICSID), an agency of the World Bank (ICSID Case No. ARB/07/27). The terms of the contract arbitration clause allowed the parties to seek interim judicial relief without waiving their rights.

On March 18, Paul Walker, the judge in the dispute with Exxon Mobil in England, decided to revoke the measure that had frozen \$12 billion in assets of the Venezuelan government for more than a month. The ruling by Judge Paul Walker ordered lifting “immediately” the freeze on the assets and asked Venezuela for the submission of a detailed estimate of the damage caused by the measure. Lastly, he ordered ExxonMobil to pay PDVSA the £380,000 retainer for legal costs incurred by the Venezuelan government to defend PDVSA in court. Judge Walker focused his verdict on the absence of sufficient evidence to anticipate the possibility that PDVSA would engage in international fraud against ExxonMobil to avoid paying a fair value for its stake in Cerro Negro. Walker acknowledged that the Mareva injunction is usually applied in order to avoid the disposal of assets that can occur during the time that elapses when an arbitration proceeding takes years to resolve, but he said that it is hard to presume the disposal of assets by a company with \$56 billion in assets recorded in its books at the close of 2006. ExxonMobil spokesman Alan Jeffers said that the court “did not question the merits of the underlying claim of Mobil Cerro Negro.”

The blatant repudiation of a contract by a foreign government has to elicit the same, if not a more severe, response as it would be if the situation arose between private parties. ExxonMobil has made clear it does not intend to sit waiting for a resolution from the arbitral tribunals. The anti-discrimination language in the agreement with PDVSA certainly helped distinguish any generalized government policy affecting businesses from the deliberate targeting of international oil companies. Further, Venezuela is not in a privileged bargaining position. Most of the heavy crude produced in Venezuela is high in sulfur, and thus only suitable for processing at specially fitted refineries. The status of the Chalmette refinery the two companies share in Louisiana also remains to be resolved. PDVSA cannot go without dealing with U.S.-based companies, as the United States is its largest customer.

Venezuela has significant oil reserves and needs the expertise and technology that only the large international oil companies possess. Thus, as ExxonMobil did, any company dealing with foreign governments should undertake a careful analysis of the strategic alternatives in case of a dispute and include effective forward-looking defensive provisions in any agreement entered into. These actions should generate enough leverage in favor of the company to protect the economic interests of the shareholders. In today’s world, where governments are taking an increasingly aggressive posture towards private businesses, ExxonMobil’s worthy legal fight bears close monitoring.