

Venezuela's Tragic Meltdown

Testimony

to the

United States House of Representatives

Committee on Foreign Affairs

Subcommittee on the Western Hemisphere

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Thank you, Chairman Duncan, Ranking Member Sires, and my local Florida Congresswoman Ileana Ros-Lehtinen for inviting my Testimony before you today. It is an honor.

Let me begin on a personal note. I spend my days and nights working with Latin America -- by day working on sustainable private sector financing for countries and companies across Latin America at an investment bank and by night overseeing a staff of some of the best reporters and journalists around the hemisphere at a newspaper. Both are based in Caracas, Venezuela.

I began working with Latin America at the United Nations Association of the U.S.A. under Assistant Secretary of State Toby Gati and United Nations Ambassador William vanden Heuvel after special graduate study under National Security Adviser Zbigniew Brzezinski & international lawyer Louis Henkin at Columbia and Sir Ian Brownlie at Oxford -- including a stint working with the Senate Foreign Relations Committee as a Harold W. Rosenthal Fellow -- so it is with great pride that I return to testify before the House Foreign Affairs Committee. (Harold Rosenthal, a senior aide to this Committee's Senator Jacob

Javits, was killed in a PLO attack in 1976, and the Fellowship that continues to this day was created in his memory).

In 2000, I moved to Venezuela to run the Latin American operations of U.S. investment bank Oppenheimer and three years later bought a newspaper company there -- *The Daily Journal*, a newspaper founded in 1945 which also owned other important newspapers in Venezuela including *Diario de Caracas* and *Tal Cual*.

In those two roles, I have had the satisfaction of helping to finance development not just in Venezuela but all across Latin America as well as overseeing the training of a host of the region's best journalists. Those positions have also given me a well-placed mid-field seat in the battle for Latin America's heart and soul -- a conflict I am sad to report that the forces of freedom and democracy have been losing badly in Venezuela.

My friends and esteemed colleagues Professor Hector Schamis, Professor Steve Hanke, and Dr. Michael McCarthy will testify to the disastrous results of the Chavez and Maduro administrations on Venezuela. I have been tasked to focus on threats to U.S. national security resulting from Venezuela's communist dictatorship and the country's economic destruction as well as what the U.S. can and should do to assist.

RUSSIA

In late December, my teams at Caracas Capital and the **Latin American Herald Tribune** uncovered that Russia's state owned oil company Rosneft had secured a lien on 49.9% of CITGO in the United States from Venezuela's state owned oil company Petroleos de Venezuela S.A. (PDVSA), potentially making the Russian government-controlled Rosneft the owner of America's sixth largest refinery and a vast pipeline network. That reality is made worse by the fact that Rosneft is under OFAC sanctions from the U.S. as well as being headed by long-time Putin deputy Igor Sechin, who is also a named sanctioned individual.

We made the discovery of Rosneft's UCC lien filing because we were diligently searching for explanations for how PDVSA -- which by the end of November was 2 weeks into technical default on some its \$35 billion in bonds -- was able to come up with the funds to pay the remaining \$440 million of the \$4.2 billion in bond payments it owed in October/November and suddenly cause the Central Bank reserves to rise \$890 million as well. The threads we pulled uncovered that Russia had loaned the Venezuelans \$1.5 billion.

While much of our attention here in the U.S. has been focused on other issues, Russia's Rosneft has been active in Venezuela as well as all over the world.

In the last year, Rosneft has acquired Indian refiner Essar Oil, giving Russia India's second largest refinery, as well as port terminals, power plants and pumps. Rosneft acquired 30% of the Shourouk concession in Egypt and its giant offshore Zohr gas field. Rosneft is even drilling – and this may come as a surprise to many Americans who have given so much blood and treasure to liberate the country – in Iraq (where, by the way, they are also partnered with China).

And this year, because of some additional purchases -- but mainly because of the sale of Venezuela's 50% of the Ruhr Oil Refineries in Germany to Rosneft for \$1.6 billion in 2010 – Rosneft is now the third largest refiner in Germany.

(Instead of keeping the money to invest in domestic oil production, paying for the expropriations or buying even food and medicine for his people, Chavez went into debt to buy over \$6 billion worth of weapons from Putin, including 92 T-72 tanks, 24 Sukhoi fighter jets, S-300 anti-aircraft missile systems, 15 Mi-35m combat helicopters, 20 Mi-17-1B multipurpose helicopters, 3 Mi-26T transport helicopters, in addition to leftist-guerrilla-favorite Kalishnikov rifles.)

Meanwhile, in Venezuela, Rosneft has partnered in 5 joint oil ventures with PDVSA. Last year it increased its stake in PetroMonagas to 40% after paying Venezuela \$500 million to purchase the portion of the venture that had been expropriated from ExxonMobil. ExxonMobil had owned 42% of what was then called Cerro Negro but has since been re-titled in the new name of PetroMonagas to paper over the previous ownership.

My father, a career Air Force non-commissioned officer, instilled in me a firm belief in the Noah Principle – that is “there are no prizes for predicting rain; there are only prizes for building arks.” With that in mind, I will try to make policy recommendations as we discuss each problem.

POLICY RECOMMENDATION #1: CFIUS ANALYSIS OF CITGO

A preliminary search of the database of the Committee on Foreign Investment in the United States (CFIUS) does not show that the purchase of Citgo by Venezuela has ever undergone a CFIUS review. Under the Exon-Florio Amendment, if a

party has never availed itself of the voluntary CFIUS notification and review process, there is no limitations period on the President's authority to investigate a past transaction, which since the 2007 Foreign Investment and National Security Act includes "energy security."

Second, we have gained access to only 2 pages of the Rosneft contract with Venezuela. We do not know what the trigger is for Rosneft to take control of their 49.9% of Citgo or even if that triggering event has already happened. (Our Citgo investigation sparked additional lawsuits from Canadian goldminer Crystallex [which this weekend had its \$1.4 billion judgment against Venezuela from the World Bank's International Center for the Settlement of Investment Disputes (ICSID) upheld and registered by the U.S. Federal District Court in Washington, D.C.] and ConocoPhillips against Venezuela, PDVSA, Citgo, and Rosneft under Delaware's Uniform Fraudulent Transfer Act. Those plaintiffs are seeking discovery in an attempt to find out similar information which Venezuela has so far blocked with an appeal to the U.S. Federal Court of Appeals.)

A CFIUS review would be able to access the Venezuela-Russia contract to know if Rosneft is already the owner of Citgo.

DEBTOR: PDV HOLDING, INC. CONFIDENTIAL DRAFT

EXHIBIT A
TO FINANCING STATEMENT (FORM UCC-1)

DEBTOR: PDV Holding, Inc.
SECURED PARTY: ROSNEFT Trading S.A.

Item 4 (continued)

The collateral covered by this UCC-1 financing statement is all of the Debtor's right, title and interest in the following, whether now existing or hereafter from time to time arising, whether now owned or hereafter acquired, and wherever located (collectively, the "Collateral"):

- i. 49.9% of the shares of capital stock of CITGO Holding, Inc., a Delaware corporation, and any successor thereto ("CITGO Holding") now or in the future issued by CITGO Holding (together with the certificate representing the same), represented as of the date hereof by the certificates and the shares of common stock identified in Annex I (collectively, the "Pledged Shares");

Third, in October 2016, in an attempt to stave off default, PDVSA cajoled holders of \$2.8 billion of its \$7.2 billion in maturing debt to swap into \$3.4 billion of new PDVSA debt collateralized by the other 50.1% of Citgo. It is possible that Rosneft owns a large share of those bonds, with the possibility of giving Russia majority control of Citgo. Again, a CFIUS committee would be able to get access to those details to be able to determine the potential owners of that other half of Citgo.

POLICY RECOMMENDATION #2: REASSESS OUR OIL RELATIONSHIP

Venezuela is the third largest foreign supplier of oil to the U.S. and we are Venezuela’s biggest customer. In basic terms, the U.S. has been financing Venezuela’s “revolution.”

A brief look at the numbers will help clarify the situation.

OPEC crude oil production

According to secondary sources, OPEC crude oil production in February decreased by 0.14 mb/d from the previous month to average 31.96 mb/d. Crude oil output increased the most in Nigeria, while production in Saudi Arabia, Iraq, UAE and Angola showed the largest declines.

Table 5 - 7: OPEC crude oil production based on secondary sources, tb/d

	<u>2015</u>	<u>2016</u>	<u>2Q16</u>	<u>3Q16</u>	<u>4Q16</u>	<u>Dec 16</u>	<u>Jan 17</u>	<u>Feb 17</u>	<u>Feb/Jan</u>
Algeria	1,106	1,088	1,084	1,090	1,089	1,087	1,053	1,053	-0.2
Angola	1,753	1,730	1,772	1,761	1,623	1,674	1,659	1,641	-18.2
Ecuador	544	546	550	547	543	544	531	526	-4.4
Gabon	220	217	219	219	209	209	201	194	-6.9
Iran, I.R.	2,838	3,502	3,539	3,646	3,725	3,725	3,778	3,814	36.1
Iraq	3,935	4,382	4,290	4,396	4,601	4,642	4,476	4,414	-62.0
Kuwait	2,771	2,849	2,799	2,879	2,876	2,859	2,718	2,709	-9.3
Libya	405	391	312	311	571	610	680	669	-11.1
Nigeria	1,861	1,577	1,541	1,417	1,570	1,474	1,550	1,608	58.0
Qatar	666	656	662	652	645	641	623	622	-0.5
Saudi Arabia	10,142	10,406	10,299	10,596	10,544	10,443	9,865	9,797	-68.1
UAE	2,898	2,967	2,921	3,004	3,082	3,090	2,962	2,925	-36.9
Venezuela	2,367	2,159	2,182	2,112	2,056	2,034	2,003	1,987	-16.0
Total OPEC	31,506	32,470	32,168	32,629	33,135	33,029	32,097	31,958	-139.5

Note: Totals may not add up due to independent rounding.

Source: OPEC Secretariat.

Despite sitting on the world’s largest oil reserves, Venezuela’s oil production has fallen below 2 million barrels per day. That is down from 3.5 million bpd when Chavez took over the country.

According to PDVSA’s 2015 audited financials, the country uses 580,000 bpd domestically for fuel and power plants. Most of that is sold at less than a penny a gallon -- so at a total loss – leaving just 1.4 million bpd for export.

Costos y Gastos no Recuperados por Venta de Productos en Venezuela

El estado consolidado de resultados integrales del año terminado el 31 de diciembre de 2015, incluye costos y gastos netos no recuperados por \$7.680 millones (Bs.528.077 millones) [\$16.068 millones (Bs.334.536 millones) en 2014 y \$15.193 millones (Bs.92.525 millones) en 2013], originados principalmente por:

- La venta de los combustibles destinados al mercado nacional se realiza a precios regulados establecidos por el gobierno nacional, los cuales son significativamente menores a los costos de producción y venta. Durante 2015, PDVSA destinó al mercado interno 580 miles de barriles por día (MBD) [647 MBD 2014 y 686 MBD en 2013] de combustibles, incurriendo en costos netos de producción y ventas no recuperados para ese mismo año por \$7.494 millones (Bs.515.287 millones) [\$9.960 millones (Bs.207.367 millones) en 2014 y \$14.958 millones (Bs.91.094 millones) en 2013]. Las ventas y los costos de producción y venta de combustibles al mercado nacional, se incluyen en sus correspondientes rubros en el estado consolidado de resultados integrales, de cada año presentado.

Of that remaining exportable 1.4 million bpd, 579,000 bpd go to China. The problem being that **Venezuela receives no cash for those exports**. China has loaned Venezuela over \$60 billion dollars (65% of all its investment in Latin America) and Venezuela has already spent all that money and repays that loan by sending crude to Beijing.

Durante el año terminado el 31 de diciembre de 2015, PDVSA despachó petróleo crudo y productos por 579 MBD con un valor de \$8.371 millones (Bs.575.589 millones) [472 MBD con un valor de \$14.371 millones (Bs.299.204 millones) en 2014 y 485 MBD con un valor de \$16.559 millones (Bs.104.322 millones) en 2013], en el marco del Acuerdo de Suministro con la República Popular China (véase la nota 7-b). Los cobros correspondientes a los volúmenes entregados por PDVSA son recibidos por el BANDES, para garantizar el

With 580,000 bpd being burned domestically at a loss and 579,000 bpd going to China for free to repay loans, Venezuela is left with just 800,000 bpd to export for hard cash.

The bulk of that goes to the USA, where according to the Energy Information Agency, Venezuela shipped 719,000 bpd to the U.S. in December, making us their largest customer – and the largest consistently paying customer.

To keep it simple, rounding up to 1 million bpd for cash sale at Venezuela's average price so far in 2017 of \$45 a barrel (Venezuela's mix of heavy oil trades at \$10 below Brent and WTI), Venezuela is realizing just \$45 million per day. \$45 million per day in a country of 31 million is less than \$1.50 per person. (And I should point out that is before the actual costs of producing the 2 million bpd which is conservatively \$10 a barrel).

In short, the United States is keeping the lights on in Venezuela.

At the same time, because of the obvious shortage of cash, Venezuela is extremely dependent on the U.S. and Citgo (which is one of the few companies in the world willing to extend Venezuela credit today) for shipments of refined oil products such as naphtha, MTBE, diesel and fuel oil. In a country where drivers are now lining up in hours long waits for fuel as shortages of gas run rampant, blocking the flow of those fuel exports to Venezuela – which are also used to fuel the army’s tanks, jets, armored vehicles and military machine being used against their own people – could be an effective way to send a message.

But if the Venezuelan regime continues to deny its people food and medicine as well as basic human and democratic rights, we should also consider pulling the plug on that flow of money, by either putting a tax on oil imports from Venezuela or even halting them altogether. Those who trample on the free world’s most basic norms should not be allowed to profit from access to the free world’s greatest market.

POLICY RECOMMENDATION #3: INCREASE THE BLACKLISTS

Thanks to the efforts of Congresswoman Ros-Lehtinen and the members of this committee, the House and Senate passed – and President Obama signed -- the Venezuela Defense of Human Rights and Civil Society Act of 2014. With the addition of Venezuela Vice President Tareck El Aissami, who was named a “drug kingpin” (along with his “testaferro” Samark Lopez Bello) last month, the U.S. Treasury’s Office of Foreign Assets Control (OFAC) blacklist now contains 12 high-ranking Venezuelan officials, including former Ministers of Justice and the Interior (in charge of all the courts and police and investigative forces in the country), former Ministers of Defense, and even current state governors (who would have been replaced in gubernatorial elections last year but which the regime has blocked from taking place).

An indictment for drug trafficking against the current Minister of Justice and Interior, Major General Nestor Reverol, was unsealed in New York in August. He has not yet graduated to the OFAC list.

A former minister of Justice and the Interior, Ramon Rodriguez Chacin, was put on the OFAC list for material assistance to the FARC. Emails from Rodriguez

Chacin, indicating the degree of cooperation between the Venezuelan government and the FARC, were found on the laptop of FARC leader Raul Reyes, including documentation of \$250 million worth of weapons for the FARC. Rodriguez Chacin was replaced by El Aissami, who has now also graduated to the OFAC list, and as the current Vice President, is the second most powerful man in Venezuela.

In addition, because of the efforts of those here in Congress, over 140 mainly, extremely wealthy Venezuelans who have collaborated with, participated in and profited from corruption in the Venezuelan government have now had their visas pulled. Although this list remains unpublished because of privacy concerns, publicizing the banned names is also something that should be discussed, but regardless, that list should also continue to be expanded.

We are all proud of your efforts here in Congress to push the Obama Administration to sanction Venezuelans guilty of human rights abuse and corruption using the Venezuela Defense of Human Rights Act. More names of the corrupt should be added.

Since the Venezuelan institutions and their checks and balances have been hijacked and corrupted, it is up to us to stand for their beleaguered people.

Because of the neutering of the domestic press, it is the foreign press and the foreign press reporters in Venezuela that are left to do much of the work of getting the word out, which they do at great risk.

Congress, the Administration, Prosecutors and the Courts here must continue to do the heavy-lifting of fighting and prosecuting the corruption and continue to provide evidence of the corruption, so that Venezuelans can see the evidence of the betrayal, deceit and criminality of their leaders with their own eyes.

Those who trample the most basic tenets of the West's rule of law – from the universal rights of man and human rights to those against bribery, corruption, drug trafficking, theft, money laundering, and murder -- must not be allowed to enjoy the economic and political benefits that flow from our society's diligence in upholding that moral core curriculum.

CONCLUSION

Allowing Venezuela to fall further into the hands of drug kingpins -- with close relationships with Cuba, Iran, Hamas, Hezbollah, Russia and China -- intent on doing us harm while sitting on top of the world's largest oil reserves must not be an option.

Likewise, allowing Venezuela to fall further into anarchy and chaos will only open the door to further death and destruction, heightening regional insecurity and Latin American instability.

If the United States is unable to bring democracy to its own backyard, what chance does it have for bringing it to the rest of the world?

Thank you for your time, efforts, concern and good offices.

I am happy to elaborate further on any of these strategies and others.