US SANCTIONS ON VENEZUELA: ALTERNATIVES TO MAXIMUM PRESSURE

OIL FOR VENEZUELA

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About Oil for Venezuela

Oil for Venezuela is a non-profit organization dedicated to the study of policy initiatives that can address Venezuela's humanitarian crisis without being conditioned on a solution to the country's political conflict. We search for de-politicized, transparent and sustainable mechanisms that can harness the country's wealth and productive potential in order to attend the most urgent problems faced by Venezuelans today.

Research Team for "US sanctions on Venezuela: alternatives to maximum pressure."

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FOREWORD

The hard truth is that the policy adopted by the United States towards Venezuela over the past four years has been unsuccessful in reaching its intended objectives. Venezuela is no closer than it was four years ago to reach a peaceful resolution to its political crisis, the violation of human and political rights has intensified, and the economic and humanitarian crisis has reached dimensions that would have seemed unimaginable back then. Although accurate data on economic and social conditions is hard to come by, there is enough information to conclude that the country is on the verge of a humanitarian catastrophe.

The aim of this document is to sketch out ideas towards a potential reformulation of that policy. These ideas are intended to start a much-needed discussion of how to fix the U.S.'s Venezuela policy so that it helps put the country on the road to re-democratization and protects vulnerable Venezuelans from the collateral effects of the political crisis. It is intended to initiate a conversation that can serve as a sounding board for new proposals and innovative thinking.

Our work is based on two premises. First, that economic sanctions need to be made flexible enough to make room for genuine and workable humanitarian exceptions. This will require creating space for and supporting negotiations around humanitarian agreements involving the country's dual administrations. Second, that U.S. policy can be reframed so that it generates the correct incentives for a transition to democracy.

Oil for Venezuela remains committed to working on proposals that can help improve the lives of Venezuelans and contribute to finding a peaceful resolution to the country's political crisis.

Francisco Rodríguez

Director

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Sanctions have been the primary tool in the Trump Administration's "maximum pressure" campaign to influence political change in Venezuela. As 2021 approaches, and the shortcomings of the "maximum pressure" campaign are clear, the U.S. government could embark on an exercise to rethink its Venezuela policy and what to do with existing sanctions. The lifting of existing sanctions could be used as an incentive to encourage parties in Venezuela to negotiate a path to free and fair elections. With that goal and seeking to protect the human rights of Venezuela and meet the country's urgent humanitarian needs, we propose four basic principles that should guide a redesign of the U.S.'s Venezuela strategy.

1. **View existing sanctions as a tool in a strategy for re-democratization.** While the "maximum pressure" approach is ineffective and imposes very high costs on the most vulnerable Venezuelans, sanctions can be used to effectively support a re-democratization strategy by clearly signaling that they will be lifted in case that the Maduro government undertakes significant democratic reforms. While it is unrealistic to expect Maduro to accept calling early presidential elections (and much less, as the current U.S. framework contemplates, resigning from office), it is more plausible that he could be induced to approving electoral reforms that include the appointment of electoral authorities and accepting international observers to oversee coming electoral contests. Rather than the unrealistic goal of provoking a regime implosion, sanctions should aim to create incentives for both sides of Venezuela's political conflict to resolve their differences through a framework that provides sufficient guarantees to the losers so as to incentivize them to adhere by the results of free and fair elections.

2. **Approve broad humanitarian exceptions.** Re-democratization is a gradual process while addressing Venezuela's humanitarian crisis is urgent. The United States needs to redesign its sanctions strategy to ensure that sanctions do not exacerbate the country's humanitarian crisis. OFAC should issue general licenses that allow U.S. persons to engage in transactions with the Venezuelan government when the purpose of these transactions is to address the country's humanitarian emergency. Licenses should cover transactions that allow the government to generate export revenues and obtain the financing necessary to pay for imports of food, medicines, and other essentials as long as the application of funds to humanitarian ends can be independently verified (e.g., through the involvement of international organizations).

3. **Promote sectoral agreements.** Even a wholesale lifting of economic sanctions would not enable by and of itself the Venezuelan public sector to regain access to U.S. export or financial markets. As long as the U.S. continues to recognize Guaidó (or anyone else) while Maduro wields *de facto* power, then an agreement between Guaidó and Maduro will be needed for Venezuela to export oil or access funds in the United States financial system. The U.S. could nevertheless condition its active support for the opposition on its willingness to enter into sectoral humanitarian agreements that allow the country to use funds for attending the humanitarian emergency. These agreements could include the creation of mechanisms for the sale of oil and the use of multilateral financing under a program overseen by agencies such as the United Nations that ensure that the resources are used for meeting basic Venezuelan needs.

4. **Clarify criteria for personal sanctions.** The arbitrariness of designations as Specially Designated Nationals (SDNs) diminishes their effectiveness. The U.S. needs to lay down a clear line of what thresholds should not be crossed by Venezuelan officials or their collaborators. Ideally, personal sanctions should be restricted to cases in which there is evidence of corruption and human rights violations. Designations should not be targeted at political actors who disagree with the United States, and the threat of sanctions should not be used to induce political decisions by the opposition leadership. There should also be greater multilateral coordination with other governments that have imposed personal sanctions; ideally, neither the criteria for imposing sanctions nor the list of sanctioned officials should differ much across Western democracies.

UNDERSTANDING VENEZUELA SANCTIONS: A BRIEF EXPLAINER

The Venezuela sanctions regime includes a set of interrelated laws, regulations, and executive branch decisions that aim to regulate the interactions of both U.S. and non-U.S. persons with the Venezuelan government and past and current officials. Sanctions target both individuals linked to the *de facto* government led by Nicolás Maduro and impose more wholesale restrictions on interactions with the Venezuelan state and its agents.

Personal sanctions commonly take the form of inclusion of individuals associated with the regime in the list of Specially Designated Nationals (SDNs) maintained by the Office of Foreign Assets Control. SDN designation implies a legal prohibition on U.S. persons and firms entering into any type of commercial or financial transaction with the sanctioned person. There are currently 167 Venezuela-linked SDNs, including political leaders and businesspersons allegedly associated with corruption, human rights violations, or subversion of democracy. Although some designations linked to drug trafficking are made on the basis of the Kingpin Act, most designations occur under the authority granted to the U.S. government as a result of the Obama administration's 2015 declaration of a national emergency with respect to Venezuela.

Several nations, including Canada, Switzerland, and the European Union, have also imposed personal sanctions, making these the one area of sanctions policy in which there is some degree of multilateral convergence. That said, there are reasons to be concerned that personal sanctions may be overused. Since there is no due process associated with SDN designations, there is the potential for excessive discretionality. There is also the strategic concern that rather than create incentives for regime change, excessive application of personal sanctions may have raised perceived exit costs, spurring key *Chavista* leaders to rally around Maduro.

Financial sanctions were first imposed through Executive Order 13808 of August 24, 2017 and preclude any financing or payment of dividends to the Government of Venezuela or its controlled entities. Although some exceptions were built in for short-term financing and humanitarian lending, these were closed as a result of the posterior imposition of sectoral and government sanctions. The 2017 financial sanctions not only barred new lending but also impeded refinancing of existing debts. The evidence shows that the sanctions strongly hurt the oil industry, particularly through their effect on oil joint ventures, which had been highly dependent on international financing.[1] By barring any debt refinance, the sanctions also impeded the country from restructuring its debts, forcing it to enter into a protracted debt default.

Sectoral sanctions are restrictions on transactions with firms in a particular sector of the Venezuelan economy. They stem from Executive Order 13850, which allows the Treasury Department to determine that broad sectors of the Venezuelan economy are contributing to the national emergency, and to subsequently bar transactions with specific persons or firms in those sectors. Up to now, these sanctions have been imposed on firms in the oil, gold, finance, and security and defense sectors. They preclude any transactions between U.S. persons and sanctioned firms, such as the state-owned oil monopoly PDVSA, state-owned mining companies like MINERVEN, and various state-owned banks. Just sectoral sanctions on the oil sector have led the country to lose around 400 thousand barrels per day of production, worth around USD 5bn a today's prices, or around 80% of the country's current exports.[2]

Government sanctions were imposed through Executive Order 13884 of August 2019 and barred any transactions with the Government of Venezuela or its controlled entities. Note, however, that many of these transactions would have been barred anyway because of financial and sectoral sanctions. Furthermore, by August of 2019, the U.S. had already recognized the government of Juan Guaidó. Therefore, technically these sanctions preclude transactions with the Guaidó administration. They also impede asset seizures by creditors and thus act as a *de facto* asset protection order, although whether the U.S. has a right to restrict creditor actions through this type of decisions is controversial and currently the subject of several court actions.

[1] Rodríguez, Francisco "Sanctions and the Venezuelan Economy: What the Data Say." July 2019.

[2] Estimates from Rodríguez (2019), *op cit.*.

Secondary sanctions. The United States government does not have jurisdiction to impose restrictions on the trade of nationals of other countries with Venezuela. However, Executive Orders 13850 (sectoral) and 13884 (government) allow it to sanction third parties for "materially assisting" the government of Venezuela. In practice, this means that the U.S. has the authority to bar U.S. persons from doing business with nationals of other countries that have conducted transactions with Venezuela and its state-owned companies. The U.S. has sanctioned several foreign firms, including Russia's Rosneft and two Mexican firms involved in oil-for-food deals, pursuant to these orders.

More importantly, the deterrent effect of the threat of secondary sanctions has been crucial in convincing many other firms to stop dealing with Venezuela. The U.S. government regularly communicates with firms in Europe and Asia to clarify what dealings would lead them to be considered for secondary sanctions, and most of these firms scrupulously adhere to U.S. advice on permitted transactions.

Recognition of Guaidó presidency. On January 23, 2019, the Trump administration announced that it would recognize National Assembly President Juan Guaidó as interim president of Venezuela. This decision was based on the National Assembly's interpretation of Article 233 of Venezuela's constitution and the U.S. prior decision not to recognize Maduro's 2018 re-election. Two days later, the Secretary of State gave the Guaidó administration the certification needed to control the bank accounts of the Government of Venezuela. Courts have subsequently confirmed that Guaidó appointees are entitled to the control of financial and fixed assets in the United States belonging to the Venezuelan state or to Venezuelan state-owned enterprises, including PDVSA and CITGO.

The recognition of an alternate government had the same effect as sanctioning the Maduro government because it made any transaction with the Maduro administration illegal – as Maduro appointees have no authority to manage Venezuelan assets in the U.S. Therefore, there is a sense in which economic sanctions against Venezuela are essentially redundant: even if they were lifted, Maduro would still have no access to U.S. financial or oil markets.[3] At the same time, and somewhat counterintuitively, this means that it is the Guaidó administration and not Maduro's, which is sanctioned. From a legal standpoint, Maduro is nothing more than a former president of Venezuela.

[3] One important exception is those state-owned firms to which Guaidó has not yet appointed boards, such as PDVSA-controlled oil joint ventures. These remain under the control of Maduro appointees.

General and specific licenses and other exceptions. There are currently 35 active general licenses, as well as additional number of specific licenses whose list has not been made public. These licenses establish exceptions to the restrictions imposed by the sanctions' regime. They include the allowance of transactions related to humanitarian assistance, operations of CITGO and other entities controlled by the Guaidó administration, authorization to divest of some Venezuelan financial securities in the secondary debt market, operations of U.S. firms involved in the oil sector, and operations of international organizations and U.S. nationals in Venezuela.

Generally speaking, these restrictions are limited and have been curtailed over time. There are also exceptions to the sanctions regime that are not codified but are a matter of policy. For example, the current U.S. policy is not to impose secondary sanctions on non-U.S. firms that restrict their trade to swaps of oil for diesel or debt repayments.[4]

Other decisions or regulations. Additional decisions of the executive and legislative branches have also raised the cost of doing business with Venezuelan authorities. For example, a 2017 advisory from the Financial Crimes Enforcement Network (FinCEN) warned financial institutions that all Venezuelan government agencies "appear vulnerable to public corruption and money laundering" and that both official and non-official transactions originating in Venezuela should be subject to additional scrutiny. Directives like this have contributed to a generalized phenomenon known as over-compliance, where financial institutions deny or block transactions that are not strictly prohibited as a result of the high costs of ensuring compliance and the associated reputational and regulatory risks of compliance failures. Similarly, although personal sanctions are only supposed to apply to personal transactions, the Office of Foreign Assets Control (OFAC) has published guidance recommending limiting interactions with SDNs even if acting in their government capacity. Legislative actions such as the 2014 Venezuela Defense of Human Rights and Civil Society Act and the 2019 VERDAD Act direct the executive branch to sanction officials involved in certain acts.

[4] This exception is currently under review and is expected to be closed in October, according to reports from several news agencies based on administration sources. See Argus Media, "US rethinking Venezuela diesel swaps." July 23, 2020

Table 1 – Key Venezuela Sanctions Decisions

Decision	Date	Description
Executive Order 13692	8-Mar-15	Creates framework for sanctioning individuals contributing to the situation in Venezuela.
Executive Order 13808	24-Aug-17	Precludes any financing or payment of dividends to the Government of Venezuela or its controlled entities. Although some exceptions were built in for short-term financing and humanitarian lending, these would be closed as a result of the imposition of sectoral sanctions.
FinCEN Directive 2017	20-Sep-17	Advises financial institutions of "widespread public corruption" in Venezuela and the methods "Venezuelan senior political figures and their associates" could be using to move gains from corruption.
Executive Order 13850	1-Nov-18	Blocks property originating in the gold sector of Venezuela or any other sector determined by the U.S. government.
Recognition of Guaidó government	23-Jan-19	Recognizes Juan Guaidó as Venezuela's legitimate president; State Department certification hands over control of accounts.
PDVSA designation	28-Jan-19	Designation of PDVSA as a Specially Designated National sanctioned for operating in the Venezuelan oil sector pursuant to EO 13850.
Treasury Determinations by Sector	Jan 28, 2019 to September 9, 2019	Three determinations have been issued, sanctioning the oil, finance and security and defense sectors of the Venezuelan economy pursuant to section 1(a)(i) of E.O. 13850, as amended by EO 13857.
Executive Order 13884	5-Aug-19	Bars any transaction with the Government of Venezuela or its controlled entities. Also impedes asset seizures by creditors.
General licenses 2-35	August 5, 2019 to July 15, 2020	General licenses grant limited exceptions to the sanctions program. These include authorization for key U.S. oil sector companies to operate in Venezuela, authorization for U.S. citizens to conduct certain specific transactions necessary for their day-to-day operations, authorization for PDV Holding and CITGO Holding to operate under Guaidó control, among others.

A POTENTIAL ROADMAP FOR VENEZUELA SANCTIONS FLEXIBILIZATION

Venezuela's sanctions policy needs a radical redesign. While the need for sanctions on the Maduro regime is widely recognized and a source of both international and domestic bipartisan consensus, it is also by now evident that the current administration's sanctions approach has been ineffective at generating the incentives conducive to recovering Venezuelan democracy while there is ample evidence that the overly broad sanctions regime is having significant collateral effects on ordinary Venezuelans.

These realities call for a broad re-think of Venezuela sanctions. Sanctions must first and foremost be part of a broader strategy with well-defined objectives. The current administration's approach has been that of applying "maximum pressure" to attempt to force a break in the governing coalition. Yet sanctions are an ineffective tool for achieving regime change because the costs of relinquishing power will always exceed the benefits of sanctions relief.[5] However, sanctions could be effectively used to create incentives for a negotiated transition in the context of a strategy of re-democratization in which credible guarantees are given to the actors that may lose an electoral contest.

We take two factors as given in proposing a possible new design: (i) that the U.S. will continue to recognize Juan Guaidó as interim president of Venezuela when the current National Assembly's term expires on January 5th[6]; (ii) that a scenario in which Maduro voluntarily leaves the presidency before the end of his presidential term in 2025 is improbable regardless of U.S. policy choices.

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[5] For a concise explanation of this point, see David Cohen and Zoe Weinberg "Sanctions Can't Spark Regime Change." *Foreign Affairs*, April 2019.

[6] What to do with the recognition of Guaidó on January 5th is a complex issue which likely merits a separate note. Nevertheless, unless there are significant changes in the *status quo*, it appears to us that maintaining Guaidó recognition at that moment will be the only reasonable choice. The reason is that it is clearly a better option than recognizing Maduro, and it is unclear that there are any other feasible alternatives. However, the strategy that we lay out intends to find a way to conduce the country to internationally recognized parliamentary elections, which would offer a solution to the quandary by transferring the recognition decision to the next Legislature.

Given these premises, a strategy for flexibilization would aim to reform the current sanctions regime to allow for broad humanitarian exceptions while using the remaining sanctions as leverage to induce the holding of free and fair parliamentary elections. Since most economic sanctions are redundant given the recognition of Guaidó, any humanitarian exceptions would require coordination between the parties (i.e., Guaidó and Maduro) through a humanitarian agreement.

If free and fair parliamentary elections are held, the international community should commit to recognizing the head of state that the incoming National Assembly decides to recognize – which could be Guaidó, Maduro, or someone else, depending on the election result. In other words, the legislative elections could also serve as a way to confer legitimacy on either of the two leaders, thus serving as a quasi-presidential election and opening up a mechanism for a democratic resolution of the country's political crisis.

Step 1: Rapidly increase humanitarian assistance through channels that are currently functioning. We should recognize that any flexibilization of sanctions is unlikely to have immediate effects on Venezuela's economic crisis. Therefore, it is urgent to find direct ways to ramp up humanitarian assistance that can be effectively deployed in the country in the near term. Up to now, the U.S. has maintained its insistence that the World Food Program (WFP) oversee any large-scale humanitarian assistance program in the country. The Maduro administration is wary of the WFP, which it sees as controlled by the United States.[7] The Red Cross, the United Nations Office for the Coordination of Humanitarian Affairs, and the Pan American Health Organization, in contrast, have deployed significant presence in the country and are seen as more impartial than the WFP by Maduro government authorities. They also work with a network of local human rights NGOs such as Caritas, which are highly respected. The US should rapidly expand assistance through these programs without necessarily abandoning the longer-term objective of achieving a foothold for the WFP.

[7] The United Nations traditionally appoints a U.S. nominee as Executive Director of the World Food Program (WFP). The post is currently held by David Beasley, a former South Carolina Republican governor nominated by the Trump administration in 2017.

Step 2: Revoke redundant government and financial sanctions and issue Asset Protection Order: Executive Order 13808 (financial sanctions) and 13884 (government sanctions) are essentially redundant. This is because they restrict the Guaidó government (which is the only one that can issue debt or control funds in the U.S.) and impede transactions of which the most relevant would involve PDVSA, which is sanctioned pursuant to is designation under Executive Order 13850 (sectoral sanctions). Lifting government and financial sanctions offer the possibility of extending a largely symbolic olive branch to the Maduro government at no cost, while also serving to signal that a new administration would be willing to consider other, less symbolic, sanctions relief if Maduro were willing to take more steps towards democratization. The lifting of these orders could also be presented as a response to concessions by the Maduro regime, such as the recent freeing of political prisoners. However, one important effect of lifting 13884 is that it could allow creditors to proceed with attachment or foreclosure of CITGO and other assets of the Venezuelan government. For this reason, the U.S. should simultaneously issue an asset protection order, which should be modeled on Executive Order 13303 issued in 2003 to protect Iraqi assets from attachment.

Step 3: Approve broad-ranging conditional humanitarian exceptions. Executive Order 13850 (sectoral sanctions) should be amended to allow for broad humanitarian exceptions allowing U.S. persons to enter into transactions with entities designated under these orders under the condition that funds obtained through permitted transactions be deposited in accounts approved by the Treasury Department for their use under a humanitarian agreement. Since any such accounts would be managed by the Guaidó administration, there is no danger of this amendment opening the door to direct control by the Maduro regime. What this decision would do would be to enable these accounts to be used to implement sectoral humanitarian agreements as set forth in the next step. Similar exceptions could be approved for secondary sanctions, while secondary sanction exceptions that are directly linked to humanitarian ends should be kept or re-instituted.[8]

[8] According to press reported, the Trump administration is currently considering imposing secondary sanctions on firms that swap Venezuelan oil for diesel. Diesel imports are key for food transportation. See Washington Office on Latin America, "115 Venezuelan Organizations and Individuals to the U.S. Government: Don't Cut Off Diesel to Venezuela." September 2020.

Step 4: Set up framework for humanitarian agreements, open door for lifting of personal sanctions. Since any accounts of Venezuela in the U.S. financial system are managed by Guaidó appointees, humanitarian exceptions that allow access to funds in the country can only be used via agreements between the Guaidó and Maduro governments. The U.S. should spearhead an effort – preferably in coordination with Europe and international organizations – to create a framework for the negotiation of these agreements under adequate international monitoring to ensure that the funds obtained through them are channeled towards genuinely humanitarian ends. For example, an administrative board integrated by an equal number of representatives of the Maduro and Guaidó administrations could be created to run a humanitarian program funded by revenues accessed through sanctions relief, subject to the oversight of the United Nations system.[9] The humanitarian licenses granted in step 3 could only be used for transactions approved by this Administrative Board. To incentivize participation by the Maduro regime, the U.S. could commit to lifting some personal sanctions on the condition of participation in the humanitarian agreement.

Step 5: Make broader sanctions relief conditional on internationally monitored parliamentary elections. The U.S. should commit to fully lifting economic sanctions if and when Venezuela holds free and fair parliamentary elections. If the elections currently scheduled for December 6th, 2020 have not yet taken place at the moment at which this strategy is implemented; a strong message could be sent to the Maduro regime that it should delay elections to ensure international recognition of the new Assembly – provided that the elections are free and fair. If elections have already been held, the condition should be that these elections be repeated.[10] Conditions for free and fair elections should include international monitoring, lifting of bans on candidates and parties, the release of all political prisoners, no use of public resources in the campaign, and appointment of credible electoral authorities. The U.S. could then condition recognition of a Venezuelan government on whatever decision the new National Assembly takes in this regard.[11]

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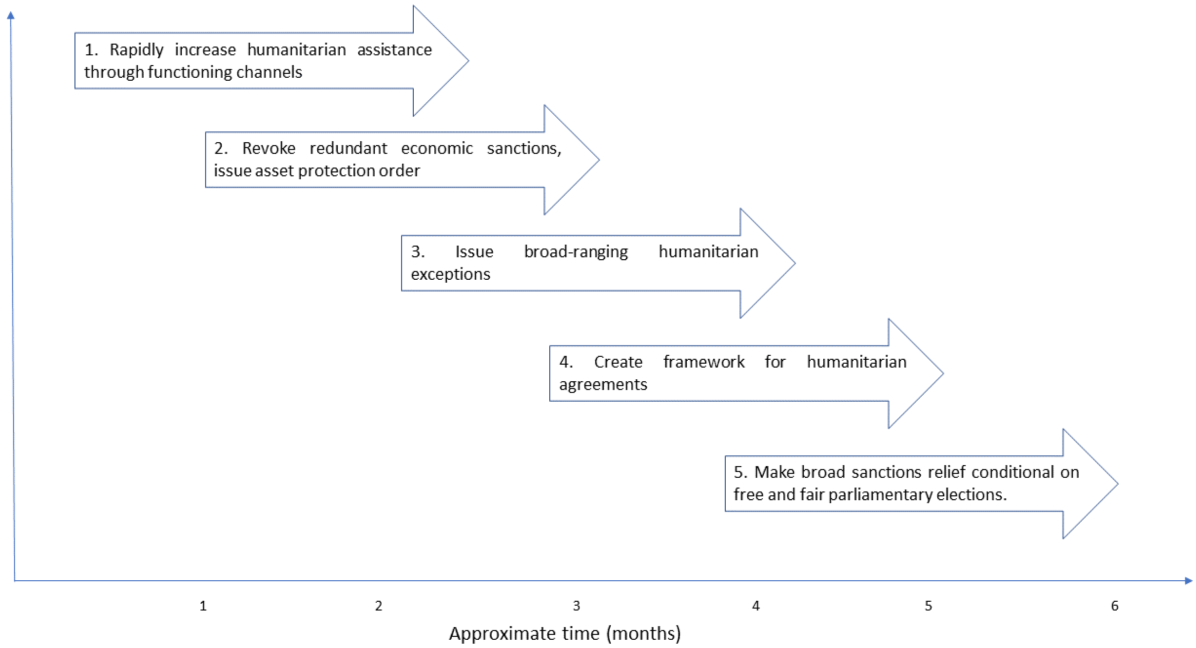
[9] For a detailed description of such a proposal, see Oil for Venezuela A Humanitarian Oil Agreement for Venezuela. October, 2019.

[10] Interestingly, there is a constitutional mechanism that allows the president to dissolve the National Assembly if it rejects three vice-presidential appointments (Article 240 of the Constitution). This mechanism could be used to call for new parliamentary elections without disputing the validity of the ones scheduled for December of this year.

[11] In other words, it will be up to the National Assembly to decide whether it continues to invoke Article 233 and appoints its leader as interim president. Therefore, recognition of the elections does not imply revoking recognition of Guaidó. Were the opposition to win control of the Assembly and its legislators re-elect Guaidó and

The holding of free and fair parliamentary elections could also be put forward as a pre-condition for a more general lifting of personal sanctions. We note that this is a vastly different approach from current U.S. policy, which contends that free and fair elections are not possible with Maduro in power.[12]

Figure 1: Potential sanctions flexibilization timeline.



reaffirm their invocation of Article 233, then the U.S. would continue to recognize Guaidó. If the government were to win and the new Assembly decided to recognize Maduro, then the U.S. would have a good reason to recognize Maduro. Other scenarios would be possible depending on the make-up of the new National Assembly.

[12] See, for example, Assistant Secretary Kozak's September 8th tweet, which states that " There can only be free & fair elections once Maduro is gone."