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# Venezuela: How a Hydrocarbons Law Crippled an Oil Giant

By STACY RENTNER\*

## Introduction

February 2003 marked the end of a nine-week national strike in Venezuela that had begun in early December 2002 and was designed to oust its president, Hugo Chavez Frías.<sup>1</sup> Chavez was elected with 56% of the vote in 1998,<sup>2</sup> and reelected with 60% of the vote in 2000,<sup>3</sup> reaching popularity highs, according to opinion polls, of nearly 80% during his presidency.<sup>4</sup> How is it possible that in such a short period of time, the country changed its attitude from almost unanimous support for Chavez to such an overwhelming desire for him to resign the presidency that it was willing to cripple its economy with a national work stoppage? Such a complex situation cannot be explained by pointing to any one factor; however, the Hydrocarbons Law decreed by President Chavez in 2001 seemed to provide the catalyst for this dramatic turn of events.

Venezuela was the world's largest exporter of oil from 1908 to 1935,<sup>5</sup> and since that time the oil sector has been the driving force of the country's economy. Venezuela depends on revenues from its

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1. *Venezuela Re-opens After Strike*, BBC NEWS (Feb. 3, 2003), at <<http://news.bbc.co.uk/2/hi/americas/2721325.stm>>.

2. POLITICAL DATABASE OF THE AMERICAS, VENEZUELA: PRESIDENTIAL ELECTIONS, 1998, at <[www.georgetown.edu/pdba/Elecdata/Venezuela/pre98.html](http://www.georgetown.edu/pdba/Elecdata/Venezuela/pre98.html)> (visited Dec. 5, 2003).

3. POLITICAL DATABASE OF THE AMERICAS, VENEZUELA: PRESIDENTIAL ELECTIONS, 2000, at <[www.georgetown.edu/pdba/Elecdata/Venezuela/pres2000.html](http://www.georgetown.edu/pdba/Elecdata/Venezuela/pres2000.html)> (visited Dec. 5, 2003).

4. Adam Easton, *Venezuela's Escalating Oil Dispute*, BBC NEWS (Apr. 7, 2002), at <<http://news.bbc.co.uk/2/hi/world/americas/1915859.stm>>.

5. *Timeline: Venezuela*, BBC NEWS, at <<http://news.bbc.co.uk/1/hi/world/americas/1229348.stm>> (visited Jan. 24, 2004).

state-owned oil sector to operate virtually every facet of its government,<sup>6</sup> relying on oil revenues for approximately 50% of government revenue, 30% of gross domestic product and 80% of exports.<sup>7</sup> Although Chavez's popularity had been waning for many reasons, the final blow the country would endure was the November 13, 2001 passage of the new *Decreto con Fuerza de Ley Orgánica de Hidrocarburos* (Hydrocarbons Law) on, which outlined the new structure of and regulations pertaining to Venezuela's oil industry.<sup>8</sup>

This note will analyze the Hydrocarbons Law—including its provisions and the legal procedure pursuant to which it was enacted—against the background of the political and economic situation of Venezuela. Part I outlines the current situation in Venezuela, including a description of the national work stoppage and the events leading up to and following it. Part II describes the evolution of the legal structure of the oil industry preceding the election of Chavez. Part III details the major legal developments since Chavez's election to the presidency, including the *Constitución de la República Bolivariana de Venezuela*, 1999 (Constitution of the Bolivarian Republic of Venezuela, 1999 or Constitution of 1999), the Enabling Law of 2000 and finally, the Hydrocarbons Law. The purpose of this analysis is to attempt to determine how the enactment of the Hydrocarbons Law culminated in a state of societal disarray in Venezuela.

## I. Current Situation in Venezuela

Although Chavez has faced numerous strikes by the oil workers of the state-owned oil company, *Petróleos de Venezuela, S.A.* (PdVSA), since taking office in 1999,<sup>9</sup> the strike ending in February 2003 was by far the most damaging to Venezuela's economy.<sup>10</sup> This

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6. ALAN GELB AND ASSOCIATES, *OIL WINDFALLS: BLESSING OR CURSE?* 289-311 (1988).

7. Marc Lifsher, *Oil Producers Balk as Venezuela Tightens Terms on Investment*, WALL ST. J., Nov. 15, 2001, at A21.

8. *Gaceta Oficial de la República Bolivariana de Venezuela* No. 37.323, Nov. 13, 2001 [hereinafter *Hydrocarbons Law*].

9. See, e.g., *Oil Workers Win in Venezuela*, BBC NEWS (Oct. 15, 2000), at <<http://news.bbc.co.uk/2/hi/world/americas/973027.stm>>; *Venezuelan Oil Workers Call Strike*, BBC NEWS (Mar. 27, 2001), at <<http://news.bbc.co.uk/2/hi/world/americas/1245063.stm>>; *New Law Sparks Venezuelan Oil Row*, BBC NEWS (Dec. 1, 2001), at <<http://news.bbc.co.uk/1/hi/business/1686157.stm>>.

10. *Venezuela Re-opens After Strike*, *supra* note 1.

oil sector strike was not only the longest, but it was also accompanied by a national work stoppage in all areas of the economy.<sup>11</sup> The strike followed on the heels of an attempted coup against Chavez, which led to his temporary resignation in April 2002.<sup>12</sup> Chavez was forced to resign as a result of earlier strikes initiated by the *Confederación de Trabajadores de Venezuela* (Workers' Confederation of Venezuela or CTV), the country's largest trade union,<sup>13</sup> and oil workers at PdVSA,<sup>14</sup> which culminated in the coup attempt by the Venezuelan military.<sup>15</sup> However, Chavez was reinstated only forty-eight hours later, following massive street protests by his supporters and support from certain factions of the Venezuelan army.<sup>16</sup>

In late November 2002 Chavez's opposition again called for a general strike, to begin in December, in an effort to force the president to hold a referendum on whether he should resign from office.<sup>17</sup> The general strike included oil workers and executives, teachers, members of the press, business owners and workers from virtually all walks of life,<sup>18</sup> and did not end until the first days of February 2003.<sup>19</sup> During the strike, Venezuelan oil production dipped to 50% of pre-strike averages.<sup>20</sup> This was a major contributing factor to an increase in gasoline prices in the United States,<sup>21</sup> which depends on Venezuela for about 13% of its daily oil imports.<sup>22</sup> It is not surprising that the political situation in Venezuela has such a strong impact on global gas prices, considering that Venezuela is the world's fourth-largest oil exporter and is the third-largest producer within the

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11. *Id.*

12. *Venezuela President Forced Out*, BBC NEWS (Apr. 12, 2002), at <<http://news.bbc.co.uk/1/hi/world/americas/1925161.stm>>.

13. *Venezuela Strike is Extended*, BBC NEWS (Apr. 11, 2002), at <<http://news.bbc.co.uk/1/hi/business/1922289.stm>>.

14. *Venezuela Oil Dispute Escalates*, BBC NEWS (Apr. 5, 2002), at <<http://news.bbc.co.uk/1/hi/business/1912201.stm>>.

15. *Venezuela President Forced Out*, *supra* note 12.

16. Tom Gibb, *Analysis: After the Would-be Coup*, BBC NEWS (Apr. 14, 2002), at <<http://news.bbc.co.uk/1/hi/world/americas/1929498.stm>>.

17. *Venezuela Heads Towards Fresh Strike*, BBC NEWS (Nov. 22, 2002), at <<http://news.bbc.co.uk/1/hi/world/americas/2501411.stm>>.

18. *Venezuela Re-opens After Strike*, *supra* note 1.

19. *Id.*

20. Alexei Barrionuevo, *How Technicians at Oil Giant Turned Revolutionaries*, WALL ST. J., Feb. 10, 2003, at A1.

21. Briony Hale, *Analysis: Venezuela's Oil Industry*, BBC NEWS (Dec. 6, 2002), at <<http://news.bbc.co.uk/1/hi/business/2549589.stm>>.

22. *Id.*

Organization of Petroleum Exporting Countries (OPEC).<sup>23</sup> It is estimated that the strike cost Venezuela over \$7.6 billion in revenues and lost production,<sup>24</sup> and resulted in the termination of over 18,000 striking oil sector employees by Chavez's government.<sup>25</sup>

In an effort to prevent any further violence in Venezuela relating to Chavez's rule, in May 2003, the Organization of American States (OAS) brokered an agreement between Chavez's government and its opposition.<sup>26</sup> In the OAS agreement, the parties stipulated, "resolution of the crisis should be achieved through application of Article 72 of the Constitution [of 1999]."<sup>27</sup> Article 72 of the Constitution of 1999 establishes the mechanism by which a national referendum may be held at the midway point of the president's term in office,<sup>28</sup> which was August 19, 2003, for Chavez.<sup>29</sup> After a failed attempt in September 2003 to begin the referendum process, the *Consejo Nacional Electoral* (National Electorate Council or CNE), on October 1, 2003, accepted an application from Chavez's opposition to begin the referendum process, allowing the opposition the opportunity to collect the signatures required by the Constitution of 1999 to hold a referendum on Chavez's rule.<sup>30</sup> However, Chavez's supporters have convinced the CNE to launch an investigation into possible "irregularities" in the application process.<sup>31</sup> In the event that the investigation does not reveal any irregularities and the opposition

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23. Bhushan Bahree & Marc Lifsher, *The Other Crisis Facing Venezuela*, WALL ST. J., Apr. 18, 2002, at A9.

24. *Venezuela Says Strike Has Cost It \$7.6 Billion*, WALL ST. J., Feb. 28, 2003, at A7.

25. Mike Ceaser, *Venezuela's Economic Legacy*, BBC NEWS (June 29, 2003), at <<http://news.bbc.co.uk/1/hi/business/3026742.stm>>.

26. *Pact to End Venezuela Violence*, BBC NEWS (May 29, 2003), at <<http://news.bbc.co.uk/1/hi/world/americas/2948724.stm>>.

27. AGREEMENT BETWEEN THE REPRESENTATIVES OF THE GOVERNMENT OF THE BOLIVARIAN REPUBLIC OF VENEZUELA AND THE POLITICAL AND SOCIAL GROUPS SUPPORTING IT, AND THE COORDINADORA DEMOCRÁTICA AND THE POLITICAL AND CIVIL SOCIETY ORGANIZATIONS SUPPORTING IT, May 23, 2003, art. 12, available at <[www.oas.org](http://www.oas.org)>.

28. CONSTITUCIÓN DE LA REPÚBLICA BOLIVARIANA DE VENEZUELA, 1999 art. 72 [Constitution of the Bolivarian Republic of Venezuela, 1999] [hereinafter CONSTITUTION OF 1999].

29. *Venezuela Sets Chavez Poll Limit*, BBC NEWS (Aug. 4, 2003), at <<http://news.bbc.co.uk/1/hi/world/americas/3124593.stm>>.

30. *Aceptan Peticiones de Referendum Revocatorio en Venezuela*, CNN EN ESPAÑOL (Oct. 1, 2003), at <<http://cnnespanol.com/2003/americas/10/01/venezuela.referendos/>>.

31. *Id.*

gathers the requisite signatures of 20 percent of registered voters, the CNE anticipates that it would be at least four months before a referendum could take place.<sup>32</sup>

Innumerable factors have contributed to the current situation in Venezuela, including Chavez's far left-leaning and authoritarian political policies,<sup>33</sup> and relationships with unpopular figures, such as Fidel Castro and Saddam Hussein.<sup>34</sup> Chavez has also been widely accused of mismanagement of the economy<sup>35</sup> and of the state-owned oil company.<sup>36</sup> However, the catalyst, which precipitated the strike of 2002-2003 and touched off the referendum efforts, was the enactment of the Hydrocarbons Law by Chavez. The Hydrocarbons Law has outraged the business community, partially due to the circumstances under which it was enacted and partially due to the language of its provisions.

## II. Historical Legal Framework of the Oil Sector

The modern era of Venezuela's oil industry began with its nationalization on January 1, 1976. After many years of increasing governmental control over the oil sector, Venezuela nationalized its oil industry by passing the *Ley Orgánica que Reserva al Estado la Industria y Comercio de los Hidrocarburos* (Organic Law Reserving the Hydrocarbons Industry and Commerce to the State) (LOREICH).<sup>37</sup> LOREICH created the state-owned oil company, PdVSA, which was formed as a private commercial enterprise with the Republic of Venezuela as its sole shareholder and was granted a monopoly over every aspect of oil extraction and production.<sup>38</sup> In addition to nationalizing the oil industry and creating PdVSA, LOREICH severely limited opportunities for private investment in the sector and erected massive administrative barriers to the possibility.<sup>39</sup>

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32. *Id.*

33. *Country Profile: Venezuela*, BBC NEWS, at <[http://news.bbc.co.uk/2/hi/americas/country\\_profiles/1229345.stm](http://news.bbc.co.uk/2/hi/americas/country_profiles/1229345.stm)> (visited Dec. 5, 2003).

34. Marc Lifsher, *Government Drill: In Under 48 Hours, Venezuelans Have Enough of a Coup*, WALL ST. J., Apr. 15, 2002, at A1.

35. *Venezuela Heads Towards Fresh Strike*, *supra* note 17.

36. Marc Lifsher, *Oil Workers Threaten Strike in Venezuela*, WALL ST. J., Mar. 13, 2002, at A12.

37. Uisdean R. Vass & Adriana Lezcano, *The New Venezuelan Legal Regime for Natural Gas: A Hopeful New Beginning?*, 36 TEX. INT'L L.J. 99, 103 (2001).

38. *Id.*

39. Jay G. Martin, *Venezuela as an Opportunity for Investment in the Petroleum*

A result of these policies and nationalization was the flight of foreign capital from the country.<sup>40</sup> However, since nationalization occurred in the midst of an oil boom lasting from 1972 to 1977<sup>41</sup> (causing the price of Venezuelan oil to quadruple<sup>42</sup> and creating an influx of "petrodollars" into Venezuela), the Venezuelan government was not particularly concerned with the loss of foreign investment.

Following a downturn in oil revenues during the period 1977-1979, Venezuela experienced another sharp increase in oil prices, lasting through 1981.<sup>43</sup> When this second boom ended, the Venezuelan economy collapsed. With the lowering of oil prices causing decreased oil revenues and a devaluation of the Venezuelan currency, living standards dropped and the government could no longer fund many social programs.<sup>44</sup>

In 1989, president Carlos Andres Perez came to power<sup>45</sup> and was saddled with the problems of a severely damaged economy, suffering from years of declining oil revenues and nearly exhausted international reserves.<sup>46</sup> Perez introduced austerity measures in an attempt to improve the condition of the ailing economy, which included raising domestic petroleum prices (the state had previously been selling petroleum internally at far below market rates), removing protectionist barriers and restrictions on foreign investment, decreasing indirect subsidies on consumer goods and, most importantly, moving toward more privatization in the state-owned oil industry.<sup>47</sup>

The opening of the oil sector to increased private investment was called the *Apertura Petrolera* (Oil Opening) and was implemented through three rounds of privatization, each involving contracts to

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*Industry*, 20 ENERGY L. J. 325, 328 (1999).

40. *Id.*

41. ALAN GELB AND ASSOCIATES, *supra* note 6, at 127.

42. *Id.* at 293.

43. *Id.* at 127, 129.

44. Mario J. Garcia-Serra, *The "Enabling Law": The Demise of the Separation of Powers in Hugo Chavez's Venezuela*, 32 U. MIAMI INTER-AM. L. REV. 265, 267 (2001).

45. POLITICAL DATABASE OF THE AMERICAS, VENEZUELA: CHRONOLOGY OF PRESIDENTS, at <[www.georgetown.edu/pdba/Executive/Venezuela/pres.html](http://www.georgetown.edu/pdba/Executive/Venezuela/pres.html)> (visited Dec. 5, 2003).

46. LIBRARY OF CONGRESS COUNTRY STUDIES, VENEZUELA: A COUNTRY STUDY, at <[www.memory.loc.gov/frd/cs/vetoc.html](http://www.memory.loc.gov/frd/cs/vetoc.html)> (visited Dec. 5, 2003).

47. MOISES NAIM, PAPER TIGERS AND MINOTAURS: THE POLITICS OF VENEZUELA'S ECONOMIC REFORMS 45-54 (Rebecca Krafft ed., 1993).

foreign investors at minimum investment levels.<sup>48</sup> The *Apertura* began to turn around the ailing oil sector and resulted in a 55% increase in output from 1990 to 1997.<sup>49</sup> However, the majority of Venezuelans, close to 70% of whom continue to live at a critical poverty level,<sup>50</sup> did not view the decreased subsidies on goods and increases in petroleum prices as measures that would repair the ailing economy, but rather as a drain on the pocketbooks that had already suffered so much in the deflated economy of the previous decade.<sup>51</sup> Perez's popularity declined and the growing dissatisfaction with his economic reforms culminated in a general strike and rioting, which followed a raise in bus fares caused by an increase in gasoline prices.<sup>52</sup> Shortly thereafter, in 1992, the current president, Hugo Chavez, led an attempted military coup against Perez. Although the coup failed, Perez was eventually removed from office.<sup>53</sup> With his removal from office, many of Perez's reform programs were terminated, although the improvements in the oil sector resulting from the *Apertura* were still being enjoyed.<sup>54</sup>

Throughout the 1990s, PdVSA was run much like a private sector company in terms of profitability and was among the most efficient oil companies in the world.<sup>55</sup> PdVSA continued the process of *Apertura* and began to acquire refining and marketing operations in the United States, Europe and Asia.<sup>56</sup> Foreign investment in Venezuela increased and the Energy Information Agency and the United States Department of State praised the progress Venezuela had made through the opening of its oil sector.<sup>57</sup> One commentator wrote in 1999, "Venezuela has re-fashioned itself into a country ripe

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48. Martin, *supra* note 39, at 328-29.

49. *Id.* at 328.

50. Lowell Fleischer, *Venezuela Alert: The Economy Continues to Deteriorate*, HEMISPHERE FOCUS (Oct. 2, 2002), available at <[www.csis.org/americas/pubs/h021003\\_14.htm](http://www.csis.org/americas/pubs/h021003_14.htm)>.

51. NAIM, *supra* note 47, at 59-62.

52. *Id.*

53. *Analysis: Venezuela Awaits New Order*, BBC NEWS (July 27, 1999), at <<http://news.bbc.co.uk/1/hi/world/americas/404777.stm>>.

54. Martin, *supra* note 39, at 328.

55. In 2000, PdVSA had daily oil production levels similar to those of Pemex, the state-owned oil company of Mexico, despite having roughly one-third the employees of Pemex. Barrionuevo, *supra* note 20.

56. Vass & Lezcano, *supra* note 37, at 104.

57. Martin, *supra* note 39, at 330, 336, 343.



for foreign investment in petroleum."<sup>58</sup> However, with the election of Chavez in 1998, foreign investors began to grow wary of injecting further capital into the Venezuelan economy.<sup>59</sup> Not only was the international business community skeptical of his past involvement in the attempted military coup in 1992, but also of his opposition to continuing the *Apertura* program in Venezuela's oil sector, which he began to voice early in his campaign.<sup>60</sup>

### III. Creation of the Hydrocarbons Law

#### A. Constitution of 1999

Upon his election to the presidency, Chavez's first major political goal was to revamp the government and draft a new constitution (the previous constitution had been in effect since 1961 with amendments in 1983).<sup>61</sup> On April 25, 1999, a referendum was held on whether the country should draft a new constitution. The referendum resulted in 92% of voters approving the measure (although voter turnout was only 39%).<sup>62</sup> On July 25, 1999, the people of Venezuela voted to choose representatives for the Constituent Assembly, which would be responsible for drafting the new constitution.<sup>63</sup> Supporters of Chavez—among them Chavez's wife, brother, Chief of Staff and twenty of his former military colleagues—succeeded in winning 123 of the 131 seats in the Constituent Assembly.<sup>64</sup> On December 15, 1999, the Constitution of 1999 was approved by a 70% majority (although voter turnout was again below 50%).<sup>65</sup>

The most important provisions of the Constitution of 1999 relating to the petroleum industry are Articles 12, 302 and 303. Article 12 reserves ownership of the country's hydrocarbons still in

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58. *Id.* at 328.

59. *Id.* at 338-42.

60. *Id.*

61. See CONSTITUCIÓN DE LA REPÚBLICA DE VENEZUELA, 1961 CON LAS REFORMAS DE 1983 [Constitution of the Republic of Venezuela, 1961 with the amendments of 1983].

62. Peter Greste, *Venezuela Backs Political Overhaul*, BBC NEWS (Apr. 26, 1999), at <<http://news.bbc.co.uk/1/hi/world/americas/328045.stm>>.

63. *Venezuela Voting for New Assembly*, BBC NEWS (July 25, 1999), at <<http://news.bbc.co.uk/1/hi/world/americas/403181.stm>>.

64. Garcia-Serra, *supra* note 44, at 273.

65. *Venezuela Backs New Constitution*, BBC NEWS (Dec. 16, 1999), at <<http://news.bbc.co.uk/1/hi/world/americas/566096.stm>>.

reservoir (unextracted petroleum products) to the state.<sup>66</sup> This is not abnormal for petroleum-exporting countries to do, even those that do not exercise state ownership over the oil industry.<sup>67</sup> Article 302 reserves to the state the right to manage virtually every aspect of the petroleum industry through the passage of appropriate legislation; Article 303 decrees that ownership of all of the shares of PdVSA will remain property of the state, but excludes shares in affiliates of PdVSA.<sup>68</sup>

While on its face the Constitution of 1999 may not appear to allow for significant private participation in the Venezuelan oil industry, commentators were hopeful that in its implementation it would prove slightly more favorable to private investors than the previous constitution of 1961.<sup>69</sup> This hope was based partially on the language of Article 303, which excluded affiliates of PdVSA from the requirement that the state continue to be the primary shareholder in oil companies.<sup>70</sup> However, this exclusion has, in fact, not proved to be particularly important in the five years that the Constitution of 1999 has been in effect. Expectations for increased privatization of the petroleum industry were based primarily on Article 302. Commentators pointed out that since the Constituent Assembly had not expressly excluded private investors from the oil industry, but rather deferred the question for legislation, it seemed likely that a new hydrocarbons law would allow for more private participation.<sup>71</sup> With the passage of the Hydrocarbons Law, it seems that Article 302 also provided false hope for proponents of increased privatization of the oil industry.

### **B. Enabling Law of 2000**

The Constitution of 1999 contained, in Article 236(8), an “enabling law” provision,<sup>72</sup> which would allow the National Assembly (which replaced a bicameral Congress under the new constitution) to

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66. CONSTITUTION OF 1999 art. 12.

67. Vass & Lezcano, *supra* note 37, at 105.

68. CONSTITUTION OF 1999 arts. 302-03.

69. Uisdean R. Vass & Leopoldo Escobar, *The Oil & Gas Articles of the New Venezuelan Constitution: The Surprising Fifth Republic*, available at <[http://www.macleoddixon.com/content/eng/publications/329\\_12877.htm](http://www.macleoddixon.com/content/eng/publications/329_12877.htm)> (visited Dec. 5, 2003).

70. *Id.*

71. *Id.*

72. CONSTITUTION OF 1999 art. 236(8).

empower the president with the authority to rule by decree, or enact laws without requiring the approval of the National Assembly.<sup>73</sup> An enabling law is designed to allow the president to act within a limited scope, for a limited period of time, to quickly enact measures, particularly in times of economic emergency.<sup>74</sup> In November 2000, the National Assembly adopted an enabling law authorizing Chavez to rule by decree in a broad range of areas—including finance, economy, society, infrastructure, security and technology—for a period of one year.<sup>75</sup> Although enabling laws had been enacted on six earlier occasions throughout Venezuela's history, the Enabling Law of 2000 reached far beyond any of the previous ones, both in its broad scope of authority, touching almost every aspect of Venezuelan life, and in its prolonged duration of one year.<sup>76</sup>

Chavez claimed that the Enabling Law was necessary to remedy Venezuela's severe economic problems without overburdening the legislature, while his critics argued that matters dealing with the oil sector were beyond the scope of what a president should be entitled to govern outside of the normal legislative process.<sup>77</sup> However, the Enabling Law was passed by a democratically-elected National Assembly, whose responsibility it was to delineate the scope of the powers it granted to the president at a level it felt necessary to enable him to attempt to remedy the dire economic situation in Venezuela. Additionally, it should be noted that the National Assembly was both the body that authorized the Enabling Law, and that was handing over its own legislative powers to the president. It has been argued that the passage of such a wide-ranging enabling law was outside the scope of the National Assembly's powers and should have been struck down by the Supreme Tribunal of Justice, Venezuela's highest court, as a violation of separation of powers.<sup>78</sup> However, the issue was never presented before the Tribunal. It was pursuant to the powers granted to him under the Enabling Law of 2000 that Chavez enacted the Hydrocarbons Law.<sup>79</sup>

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73. Garcia-Serra, *supra* note 44, at 276.

74. *Id.* at 274-75.

75. *Id.* at 276.

76. *Id.* at 274-75, 281.

77. *Venezuela's Chavez Gets Sweeping Powers*, BBC NEWS (Nov. 7, 2000), at <<http://news.bbc.co.uk/1/hi/world/americas/1011993.stm>>.

78. Garcia-Serra, *supra* note 44, at 277.

79. Hydrocarbons Law, *Habilitacion* [Authorization].

### C. *Hydrocarbons Law of 2001*

The Hydrocarbons Law was one of forty-nine laws enacted by Chavez during his grant of unilateral legislative power under the Enabling Law,<sup>80</sup> and was decreed hours before Chavez's enabling powers were to expire.<sup>81</sup> The Hydrocarbons Law completely restructured the petroleum sector, replacing the Hydrocarbons Law of 1943, which had previously governed the sector.<sup>82</sup> A single-handed restructuring of the central industry of Venezuela, of a magnitude not seen in almost sixty years, would clearly seem to go beyond the purview of the limited emergency power that an enabling law is intended to bestow upon the president.<sup>83</sup> However, although Chavez's opposition,<sup>84</sup> including Venezuela's top business leaders,<sup>85</sup> have threatened to challenge the constitutionality of the Hydrocarbons Law in the Supreme Tribunal of Justice, the Law has now been in effect for over two years and has not yet been challenged. In addition to the questionable constitutionality of both the Hydrocarbons Law and the Enabling Law, Venezuela's business community resents the procedure by which the Hydrocarbons Law came into effect. Although the government allowed private sector business leaders to voice their opinions on the development of the Law, their suggestions were largely ignored.<sup>86</sup>

Among the most controversial measures included in the Hydrocarbons Law are Articles 22 and 44. Article 22 requires that the state maintain over 50 percent participation in all new petroleum projects.<sup>87</sup> Under the preexisting legal structure, any new projects involving private investors were to be accomplished through joint ventures with the state-owned oil company, PdVSA.<sup>88</sup> Under Article

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80. Lifsher, *supra* note 7.

81. *Venezuelan Union to Join Bosses' Strike*, BBC NEWS (Dec. 5, 2001), at <<http://news.bbc.co.uk/1/hi/world/americas/1692860.stm>>.

82. Hydrocarbons Law, Disposiciones Transitorias [Provisional Regulations].

83. See Garcia-Serra, *supra* note 44, at 276-77.

84. Fabiola Sanchez, *Law Tightens Grip on Venezuela's Oil*, Associated Press, Nov. 28, 2001.

85. *Venezuela 2002: In Search of a Confrontation . . . of Ideas, Interview with Pedro Carmona, FEDECAMARAS*, WASH. TIMES (2002), available at <[www.internationalreports.net/theamericas/venezuela/2002/insearch.html](http://www.internationalreports.net/theamericas/venezuela/2002/insearch.html)>.

86. *Id.*

87. Hydrocarbons Law art. 22.

88. U.S. DEP'T OF STATE, 2001 COUNTRY REP. ON ECON. POLICY AND TRADE PRACTICES: VENEZUELA (Feb. 2002), available at <[www.state.gov/documents/organization/8215.pdf](http://www.state.gov/documents/organization/8215.pdf)>.

22 of the Hydrocarbons Law, none of these joint ventures can be realized without PdVSA having a majority stake.<sup>89</sup> This result is troubling for several reasons. First, it is unlikely that PdVSA has, or will have in the near future, the resources to provide over 50% of the capital required for each new undertaking involving private investors.<sup>90</sup> Even before the general strike began, PdVSA experienced losses in production capacity, from which it did not have the capital to recover.<sup>91</sup> With PdVSA in such a financial condition that it cannot fund its own production, it seems virtually impossible that it would be able to invest in any new projects, much less provide 50% of the capital for all new joint ventures. Thus, foreign investors would be prevented from investing in petroleum operations in Venezuela.

Secondly, the requirement of such extensive state involvement in petroleum projects defeats many of the policies of the *Apertura*. Under the *Apertura*, Venezuela generated \$20 billion in foreign investment and reached record levels of production.<sup>92</sup> Chavez has blamed the high rate of poverty in Venezuela partially on mismanagement of the oil sector,<sup>93</sup> claiming that oil windfalls during the *Apertura* were diverted from state programs and from the people of Venezuela and that more state control would ensure better management and more money to distribute to the poor. While this is an admirable motivation for including a provision like Article 22 in the new Hydrocarbons Law, it overlooks the fact that if the oil sector loses private investors, the amount of revenues to distribute to the poor will be diminished.<sup>94</sup>

In a further attempt to ensure that more of Venezuela's petroleum revenues ended up in the hands of the poor, Chavez included Article 44 in the Hydrocarbons Law. Article 44 raises the percentage of revenue from oil production required to be paid in royalties to the government from 16.7% to 30%.<sup>95</sup> The almost doubling of the percentage of royalties that private investors must pay to the government could increase the amount of royalties received by the government by as much as 80%.<sup>96</sup> In theory, this would be 80%

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89. Hydrocarbons Law art. 22.

90. Lifsher, *supra* note 7.

91. Fleischer, *supra* note 50.

92. Sanchez, *supra* note 84.

93. *New Law Sparks Venezuelan Oil Row*, *supra* note 9.

94. *Id.*

95. Hydrocarbons Law art. 44.

96. Lifsher, *supra* note 7.

more money from private investors in the oil industry that the government would be able to spend on social programs, and which could be distributed to the poor. However, this rationale again fails to take into account the reaction of foreign investors to a doubled royalty rate. The average royalty rate among all oil-producing countries is 7.1%, and 14.7% among OPEC members.<sup>97</sup> In no other country does the rate exceed 20%.<sup>98</sup> With rates as high as 30% in Venezuela, the disincentive to invest in the Venezuelan petroleum sector, in favor of almost any other oil-producing country, is impossible to ignore.

In addition to the criticisms of the Hydrocarbons Law relating to the discouragement of foreign investment, there have been various other reasons offered for dissatisfaction with it. The Venezuelan-American Chamber of Commerce, a business association which often speaks on behalf of the major U.S. oil companies,<sup>99</sup> pointed out in a letter to Chavez that the Hydrocarbons Law provided no guarantee of property rights for private companies, nor any assurance of the fulfillment of contractual obligations in existing contracts.<sup>100</sup> Some characterize the increased state control effected by the Hydrocarbons Law as one more step in Chavez's bid to acquire dictatorial rule in Venezuela.<sup>101</sup> A Venezuelan economist described the law's central objective as the imposition of "absolute state control over the oil industry."<sup>102</sup> The U.S. Department of State has also expressed its concern over the uncertain impact the Hydrocarbons Law will have on international participation in the Venezuelan oil market, and the devastating effects that it will ultimately have on the ailing Venezuelan economy.<sup>103</sup>

Despite the potential far-reaching effects of the Hydrocarbons Law, Chavez argues that it merely implements provisions of the Constitution of 1999,<sup>104</sup> which was drafted by the democratically-elected Constituent Assembly and voted into law by the people of Venezuela. This is technically true, considering the ambiguity of

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97. Sanchez, *supra* note 84.

98. *Id.*

99. Lifsher, *supra* note 7.

100. Fleischer, *supra* note 50.

101. *Venezuela's Chavez Faces Labour Wrath*, BBC NEWS (Dec. 10, 2001), at <<http://news.bbc.co.uk/1/hi/world/1701778.stm>>.

102. Sanchez, *supra* note 84 (quoting economist Orlando Ochoa).

103. U.S. DEP'T OF STATE, *supra* note 88.

104. Lifsher, *supra* note 7.

Article 302 of the Constitution, which provides only that the state retains management power over the petroleum industry (as exercisable through the passage of appropriate legislation).<sup>105</sup> However, just as commentators had expected that this provision of the Constitution was a hopeful sign for increased privatization of the oil industry,<sup>106</sup> so too, perhaps, did the people of Venezuela who voted in support of the Constitution. In addition, it seems unlikely that the voters of Venezuela envisioned that the legislation referred to in Article 302 would be enacted unilaterally by the president, rather than by the legislature. But, unless the Supreme Tribunal of Justice reviews the Enabling Law of 2000 or the Hydrocarbons Law, the regime created by the Hydrocarbons Law will prevail, having been enacted through a process provided for in the Constitution of 1999.

The Supreme Tribunal of Justice is the branch of government given responsibility for upholding constitutional principles under Article 335 of the Constitution of 1999, and is also the final interpreter of the Constitution.<sup>107</sup> Article 336(1) expressly gives the Supreme Tribunal the power to nullify laws passed by the National Assembly when they do not adhere to the Constitution.<sup>108</sup> Further, under Article 336(3), the Supreme Tribunal is given the ability to nullify any law decreed by the executive which does not conform to constitutional principles.<sup>109</sup> Therefore, the Supreme Tribunal of Justice does possess the requisite power to declare both the Enabling Law of 2000 and the Hydrocarbons Law unconstitutional, under Articles 336(1) and 336(3), respectively. However, one difficulty in bringing a challenge to the Enabling Law of 2000 would be that enabling laws have been used several times before in Venezuela's history, and none were declared unconstitutional.<sup>110</sup> Perhaps a larger difficulty in bringing challenges to either law is that the current Supreme Tribunal of Justice is composed of justices who are largely sympathetic to Chavez and who were elected to twelve-year terms in the same 2000 election where Chavez was reelected with 60 percent of the vote.<sup>111</sup> Therefore, it seems unlikely that the Supreme Tribunal would be sympathetic to constitutional challenges against either the

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105. CONSTITUTION OF 1999 art. 302.

106. See Vass & Escobar, *supra* note 69.

107. CONSTITUTION OF 1999 art. 335.

108. *Id.* art. 336(1).

109. *Id.* art. 336(3).

110. Garcia-Serra, *supra* note 44, at 284.

111. *Id.*

Enabling Law of 2000 or the Hydrocarbons Law, since the majority owes its election largely to Chavez's popularity in 2000.<sup>112</sup> In addition, it does not appear as though any parties have sought to present a constitutional challenge to either of the laws.

Thus far, the effects of the Hydrocarbons Law suggest a dismal future for Venezuela's economy and particularly its oil sector. Following the enactment of the Hydrocarbons Law, in the first quarter of 2002, the Venezuelan economy contracted 4.2% and further sank 10% in the second quarter.<sup>113</sup> Despite the increase in world oil prices in the second quarter of 2002, the 10% contraction included a shrinking of 16.7% in the petroleum sector.<sup>114</sup> While the Hydrocarbons Law had not been in effect for very long, these figures are discouraging. Despite Chavez's efforts to redistribute wealth to the poor, Venezuelan salaries are 20% of what they were in 1980, and the standard of living has fallen to levels lower than in 1962.<sup>115</sup>

### Conclusion

The difficulties present in the Venezuelan economy were not created in a short period of time nor are they apt to be resolved in the near future. Introducing sweeping changes into the legal structure of the petroleum sector may have appeared to president Hugo Chavez and his supporters to be the precise action necessary to begin the process of bridging the gap between rich and poor in Venezuela. Effecting this restructuring under the rationale that the people of Venezuela are entitled to receive more benefits from their country's lucrative oil industry is, perhaps, an admirable undertaking. Or, as some argue, it may merely be the action of a president who is in endless pursuit of authoritarian power. Whatever the motivation behind Chavez's Hydrocarbons Law decree, the creation of the Law appears to have been shortsighted. It has been the cause of extreme domestic unrest, enraging many who foresee decreased levels of private investment and the potential downfall of the oil industry in Venezuela. Ultimately, the Hydrocarbons Law has also proved ineffective in moving toward the accomplishment of Chavez's lofty socialistic ideals, and thus far has proven detrimental to Chavez's remaining supporters amongst the poor, lowering petroleum

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112. *Id.*

113. Fleischer, *supra* note 50.

114. *Id.*

115. *Id.*



revenues, salaries and the standard of living.

It is undeniable that the Enabling Law of 2000, which led to Chavez's acquisition of the power to unilaterally decree the Hydrocarbons Law, was enacted by a democratically-elected body within the framework of constitutional procedures. However, it is questionable whether the scope of the Enabling Law violated the separation of powers embodied in the Constitution of 1999. Additionally, the enactment of the Hydrocarbons Law by Chavez, although technically within the letter of the Constitution, may have exceeded the scope of his powers under the Enabling Law. It is also arguable that allowing the president to unilaterally legislate in order to restructure such an important sector of the economy violates democratic principles, in a nation that has prided itself on its long democratic history.

While there are many unanswered questions pertaining to the legality of these measures, any solution can only be speculative unless and until the Supreme Tribunal of Justice reviews their constitutionality. It seems that the recent unrest in Venezuela stems mainly from the popular sense that Chavez's policy is insulated from any meaningful review. The opponents of these measures may feel that appealing to the Supreme Tribunal of Justice would be a fruitless pursuit, considering the relationship of the justices to Chavez. Since the Hydrocarbons Law was enacted by the president alone, the voters cannot appeal to their elected representatives to consider alternative solutions. The only recourse available to them until August 2003 was to attempt to convince the president to step down, as he had been the lone source of the laws enacted pursuant to the Enabling Law. Ultimately, this was precisely what many Venezuelans tried in vain to accomplish with the national work stoppage and petroleum sector strike, and continue to attempt with their efforts to hold a national referendum. In the end, the Hydrocarbons Law remains in effect—unless and until its constitutionality is challenged in the Supreme Tribunal of Justice. And Chavez remains in power until 2006—unless and until he is voted out in a referendum.