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Venezuela Revisited: Foreign Investment, Technology, and Related Issues

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VENEZUELA REVISITED: FOREIGN INVESTMENT, TECHNOLOGY, AND RELATED ISSUES

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*Franklin T. Hoet-Linares***

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I. HISTORY OF FOREIGN INVESTMENT IN VENEZUELA

A brief history of foreign investment in Venezuela is necessary to understand recent changes in Venezuelan foreign investment policy. The development of selected industrial sectors, including principally petroleum and mining, but also agriculture, electric power, manufacturing, banking, and insurance, has played a significant role in shaping Venezuelan foreign investment policy. The laws, policies, and their application can then be reviewed in practical terms to provide the practitioner with an understanding of the stated objectives of the host government within the context of Third World movements toward greater control over economic activities.

A. *Petroleum*

The petroleum industry has been the cornerstone of Venezuela's economy for fifty years. It has been the principal source of Government revenues and foreign exchange receipts, and it has provided the stimulus for extensive industrial and social change. In 1979 the petroleum industry accounted for twenty-two percent of the Gross Domestic Product, sixty-nine percent of total Government revenues, and ninety-six percent of the total value of exports.¹ The petroleum sector will continue to provide most domestic income, even after Government projects begin operating at full capacity sometime in the late 1980s, as projected by the Government's Sixth National Development Plan (1981-1985)(VI NDP).² Venezuelan oil has traditionally been drawn from three major petroliferous zones: the Lake Maracaibo region,³ near Venezuela's northwestern border with Colombia; the Orinoco River Basin in the eastern region; and the Apure-Barinas Basin in the southwest. Proven national reserves in these three fields amounted to nineteen billion barrels in 1981, approximately fifty-five percent of which consisted of extremely heavy-gravity crudes.⁴ Geologists have estimated that up to forty-eight billion

1. BUSINESS INTERNATIONAL CORPORATION, INVESTING, LICENSING & TRADING CONDITIONS ABROAD: VENEZUELA 2 (1980).

2. Address by Guillermo Rodriguez Eraso, president of Lagoven, S.A., before the Venezuela-American Association of New York, in New York City (Jan. 18, 1981) [hereinafter cited as Rodriguez Eraso].

3. This region accounts for 75% of Venezuela's oil output.

4. Rodriguez Eraso, *supra* note 2. If the current rate of consumption remains constant, Venezuela's proven reserves will last twenty years. Address by Frank-

barrels more can be added to proven reserves without considering the heavy-gravity Orinoco (tar) Belt.⁵ Recent surveys of the Orinoco River Basin reveal that the Belt may hold as much as three trillion barrels of heavy viscous oil—a quantity unmatched anywhere in the world.⁶ The recovery factor in the tar Belt could exceed an economically viable thirty percent with the use of newly proven technology. Technology is also available to upgrade the eight degree API gravity heavy oil to an attractive twenty-six to twenty-eight degree medium-gravity oil by extracting coke, vanadium, and sulphur impurities. Future production from the Orinoco Belt is estimated at 125,000 barrels per day (b.p.d.) by 1988 and one million b.p.d. by the year 2000.⁷ Conservative estimates reveal that this will require an investment of twenty million dollars in addition to ten billion dollars in supporting infrastructure.⁸ Including inflation, this estimate could easily require a fifty billion dollar investment by the year 2000.

In spite of the nation's history as a leading oil producer, Venezuela's oil potential remains largely untapped. Although the Gulf of Venezuela has never been drilled, a recent seismic survey revealed the presence of extremely promising reserves,⁹ which may have precipitated border disputes with Colombia. The continental shelf along the Caribbean coast and the Delta Amacuro area on the Atlantic coast south of Trinidad are also thought by many geologists to contain large amounts of oil.

Venezuelan oil was first discovered in 1914, but World War I delayed exploration and drilling efforts. Commercial petroleum production began in 1922 when a well in the State of Zulia blew out of control and produced 900,000 barrels of petroleum in a little more than a week. Traditionally, there were few restrictions on foreign investment in the petroleum sector. Initial concessions to United States companies were quite generous, as were subsequent concessions to English and Dutch companies. The Venezuelan Government was determined to increase domestic production of oil through a policy of *desarrollo hacia afuera* (an

lin Hoet-Linares before the Center for World Peace Through Law, in São Paulo, Brazil (Aug. 16, 1981).

5. Rodriguez Eraso, *supra* note 2.

6. *Id.* See also FOREIGN AREA STUDIES OF THE AMERICAN UNIVERSITY, AREA HANDBOOK FOR VENEZUELA, 146 (1977)[hereinafter cited as AREA HANDBOOK].

7. Amador, *An Injection of Optimism*, BUS. VENEZUELA, Mar.-Apr. 1980.

8. *Id.*

9. See Rodriguez Eraso, *supra* note 2.

outward-oriented development path)¹⁰ and believed that this was facilitated by increasing the number of oil concessions to foreign companies.¹¹ In the late 1930s the Government attempted to exert greater control over the original concessions. A more restrictive foreign investment policy gradually developed over the next forty years, culminating in the enactment of the 1976 Petroleum Nationalization Bill. The foreign companies were in no position to resist; the advent of World War II and the example of the Mexican petroleum nationalization in 1938 made Venezuela's petroleum vital to the United States and its allies. In 1943 a new hydrocarbons law was enacted which established the principle of reversion of concessions to the state within forty years and increased the Government's royalties from eleven to seventeen percent.¹² In 1948 Venezuela's share was increased to fifty percent, and in 1958, to sixty percent. Angered by President Eisenhower's oil import quota system of 1959, Venezuela began to assert more active control over the petroleum industry. A state-owned petroleum company, Corporación Venezolana de Petroleo (CVP) was formed. That year also marked Venezuela's vital participation in the formation of the Organization of Petroleum Exporting Countries (OPEC).¹³

In 1970 a law was enacted authorizing Venezuela to unilaterally determine oil export prices. A new Reversions Law was enacted in 1971, calling for the return of all existing concessions to Venezuela after their expiration dates.¹⁴ Finally, upon taking office in 1974, President Perez announced his plan to nationalize the oil industry. On January 1, 1976, Venezuela's Petroleum Nationaliza-

10. See Radway, *The Next Decade in Latin America: Anticipating the Future from the Past*, 13 CASE W. RES. J. INT'L L. 3, 6 (1981).

11. See generally Rossi-Guerrero, *The Transition from Private to Public Control in the Venezuelan Petroleum Industry*, 9 VAND. J. TRANSNAT'L L. 475 (1976); CONTEMPORARY VENEZUELA AND ITS ROLE IN INTERNATIONAL AFFAIRS (R. Bond ed. 1977)[hereinafter cited as CONTEMPORARY VENEZUELA].

12. Law of Hydrocarbons of Mar. 13, 1943 and its Regulations of Aug. 1943.

13. Law of May 26, 1961 (approving the Agreement forming the Organization of Petroleum Exporting Countries (OPEC)); Decree 260 of Apr. 19, 1960 (creating CVP), designated by Organic Law Reserving to the State the Industry and Commerce of Hydrocarbons, Aug. 29, 1975, art. 6, at 1493-94, translated in 14 INT'L LEGAL MATERIALS 1492 (1975). See generally Faud, *Venezuela's Role in OPEC: Past, Present and Future*, in CONTEMPORARY VENEZUELA, *supra* note 11.

14. Hydrocarbons Reversion Law (concerning property subject to reversion in hydrocarbon concessions), GACETA OFICIAL No. 29,571, July 30, 1971.

tion Bill went into effect.¹⁵ The Nationalization Bill created a petroleum holding company, Petroleos de Venezuela, S.A. (now PDVSA, formerly called PETROVEN), to plan, coordinate, and supervise the industry.¹⁶ The Petroleum Nationalization Bill permits Venezuela to sign agreements and contracts with private companies for technical assistance.¹⁷ Major former concessionaires and other specialized firms continue to supply PDVSA with necessary technical support through such service contracts. When the Nationalization Bill went into effect, PDVSA maintained fourteen affiliates. PDVSA currently has only four integrated operating affiliates: Lagoven, Maraven, Meneven and Corpoven.

B. Mining

1. Iron Ore

Although foreign investment in the mining sector has never matched that of the petroleum sector in Venezuela, two major United States corporations were active in the exploitation of iron ore before the January 1, 1975 nationalization of iron ore concessions.¹⁸ Subsidiaries of U.S. Steel Corporation (the Orinoco Mining Company) and Bethlehem Steel (the Iron Mines Company) extracted iron ore from two large mines located in the Guyana Highlands. When the Perez Government nationalized the mines in 1975, the two United States companies entered into iron ore supply contracts with the Government. These companies also executed technical assistance agreements for the maintenance, purchasing, and engineering of the industry. The Ministry of Energy and Mines (formerly Mines and Hydrocarbons) is presently responsible for its management and administration. Output of iron ore was estimated at 17.5 metric tons in 1976,¹⁹ but aluminum had displaced iron ore as the nation's second most important export by 1980.

15. Organic Law, *supra* note 13. See also Radway, *Venezuela: Certain Legal Considerations for Doing Business*, 8 CASE W. RES. J. INT'L L. 289, 293-95 (1976).

16. Organic Law, *supra* note 13.

17. *Id.* art. 5.

18. Decree of President Carlos Andres Perez, announcing the nationalization of Venezuelan iron ore concessions, *published in* VENEZUELA TODAY, Sept. 1975, at 3. See also Radway, *supra* note 15, at 293-95.

19. See U.S. DEP'T OF COMMERCE, FOREIGN ECONOMIC TRENDS AND THEIR IMPLICATIONS FOR THE UNITED STATES: VENEZUELA, No. 77-147 (Nov. 1977).

2. Bauxite

There has historically been very little foreign investment in bauxite mines. However, the development of the industrial complex of Ciudad Guyana, in a region largely endowed with minerals, has made Venezuela a substantial aluminum producer. Through its regional corporation (Corporacion Venezolana de Guyana (CVG)) and the technical assistance of the Reynolds Metal Corporation, the Government has established an integrated steel mill and an aluminum plant (VENALUM) within the Ciudad Guyana complex.²⁰ The Venezuelan Government expressly encourages foreign investors to form joint ventures with state entities in this sector, but experience to date has not been favorable.²¹ For example, the Zulia Steel Project is now forty-nine percent foreign-owned, although it was originally slated to be wholly state-owned. In the 1975 nationalization, Siderurgica de Orinoco S.A. (SIDOR) became part of the CVG. CVG now manages both the iron-steel expansion and the bauxite-aluminum development project.

3. Other Minerals and Chemicals

Gold and diamonds are mined principally in the vicinity of Ciudad Guyana. With the exception of the colonial era, there has been very little foreign interference with these mines. Venezuela has been the world's eighth largest diamond producer since 1974. In 1978 the production value of these two minerals totaled fifty-one million dollars. Coal and salt are also mined in Venezuela. Government officials have discussed development of the country's "immense coal reserves" in conjunction with the proposed integrated steel plant in Zulia.²² Although industry sources have not been convinced that the grade of coal is suitable for steelmaking, the estimated one million tons of coal to be produced through 1986 is destined for a Zulia coke plant and a thermoelectric power plant.

C. Agriculture

Before the petroleum boom, Venezuela's economy was based principally upon agriculture. There has been very little foreign in-

20. AREA HANDBOOK, *supra* note 6, at 153.

21. See BUSINESS INTERNATIONAL CORPORATION, *supra* note 1, at 4.

22. See U.S. DEP'T OF COMMERCE, *supra* note 19, at 12.

vestment in the agricultural sector, with the exception of United States investment in the food processing area. Agriculture supplies approximately six percent of the Gross National Product and employs twenty percent of the labor force. Total agricultural production rose to a peak in 1976, but it failed to keep pace with population growth. Food imports have subsequently become vital to the country's food consumption. The use of imports, coupled with urban migration has forced the Government to take a more active role in financing agricultural projects. The Fifth National Plan (V NPD) (1975-1980) included a goal to become self-sufficient in most food items, and the VI NDP has continued to stress agricultural infrastructure; nonetheless, the increase in food imports is projected to continue.

D. *Electric Power*

Venezuela is one of the leading producers of electric power in Latin America after Brazil, Mexico, and Argentina. The former Canadian and American Electric Power Company was nationalized and is now known as EDELCA, and the former Canadian International Power Company is now ENELVEN. The Guri Dam on the Caroni River in eastern Venezuela, designed and built largely by United States engineering companies, began generating in 1968. A multi-billion dollar expansion of the Guri Dam, designed primarily by Brazilian and United States engineers, has been delayed, but it will eventually produce nine million kilowatts. Other large hydroelectric projects, several thermal plants, and high-voltage transmission facilities have recently been constructed.

E. *Manufacturing*

The manufacturing sector, which has undergone annual growth of twelve to fifteen percent in recent years, is currently the fastest growing sector of the Venezuelan economy. Tires, pharmaceuticals, textiles, and glass have been produced for approximately thirty years with foreign capital. More recently, metalworking, electrical equipment, petrochemical, chemical, and the automotive industries have been growing rapidly. Metalworking, petrochemical, and automotive industries are presently subject to a subregional industrial sectorial development scheme, and other coordination is planned. Approximately sixty percent of the direct foreign investment in this sector is supplied by the United

States. Expansion of aluminum production has now been integrated with the development of bauxite deposits, and petrochemical and automotive plants are being added in greater numbers.

F. *Banking and Insurance*

Foreign banks played a prominent role in Venezuela's commercial banking system until 1970, when the Government enacted a Bank Reform Law requiring all commercial banks to reduce foreign ownership to twenty percent and prohibiting new foreign investment in this sector.^{22,1} In light of existing capital markets legislation, rules facilitating leasing and other financial market activity, foreign financial institutions have been creative in finding ways to maintain relationships with borrowers in the public and private sectors, and they have extended their occasionally excessive exposure in Venezuela.²³ In 1981 Venezuela allowed the Banco do Brasil to open a wholly Brazilian owned branch in Caracas in exchange for the Brazilian Government's grant of a reciprocal privilege to Venezuela.

The 1965 Law regulating insurance and reinsurance companies required a minimum of fifty-one percent domestic ownership in all such companies.²⁴ The 1975 Insurance and Reinsurance Law limits foreign holdings in these companies to twenty percent.²⁵ Before this law took effect, Pan-American Life Insurance, American International Underwriters Corp., AFIA World Insurance of the United States, Confederation Life of Canada, and numerous British, Swiss, and Argentine companies were all operating pursu-

22.1 Partial Reform of the General Law on Banks and other Credit Institutions, GACETA OFICIAL EXTRA. No. 1,454, Dec. 30, 1970. Also, ANCOM Decision 24 states that "new direct foreign investment shall not be permitted in the sector of insurance, commercial banking, and other financial institutions." ANCOM Decision 24, Common Regime of Treatment of Foreign Capital and of Trademarks, Patents, Licenses, and Royalties, Dec. 31, 1970, reprinted in 11 INT'L LEGAL MATERIALS 126 (1972) [hereinafter cited as Common Regime]. All references to the ANCOM Code or Decision 24 include the modifications contained in Decisions 37, 37a, 70, 103, and 109.

23. Asheshov, *Trying to Clean Up the Venezuelan Mess*, INSTITUTIONAL INVESTOR, Apr. 1980, at 68.

24. Law of July 2, 1965 (concerning insurance and reinsurance companies) GACETA OFICIAL EXTRA. No. 984, July 9, 1975.

25. Decree-Law 870 of Apr. 22, 1975 (concerning insurance and reinsurance companies) GACETA OFICIAL EXTRA. No. 1743, May 22, 1975. See generally Shelp, *The Proliferation of Foreign Insurance Laws: Reform or Regression?*, 8 L. & POL'Y INT'L BUS. 701 (1976).

ant to forty-nine percent foreign ownership arrangements.²⁶

G. *Analysis of New Investment Since 1974*

Annual data is not available concerning newly authorized foreign investment after the new legal regime became effective in 1974. The commencement of the new regime coincided with sharp increases in the per-barrel price of oil. As a result, Venezuela's annual revenues increased sharply in 1975 and 1976, and less sharply during the next three years. In 1975 and 1976 iron ore and petroleum industries were nationalized amid euphoric pronouncements by senior Government officials that the country possessed adequate oil reserves and did not require foreign investment. Despite publicity indicating the smooth and successful nationalization of the basic extractive industries, many problems remained unresolved. Lawsuits were brought for back taxes owed to the Venezuelan Government against several major companies. The Venezuelan Tax Court has recently entered a decision against at least two of these companies, and appeals are pending before the Supreme Court of Venezuela. In addition, a major United States truck manufacturer had entered into an agreement with the Venezuelan Government for approval of a diesel plant to be built in eastern Venezuela. After a visit by the King of Spain, however, a Spanish company was designated to build the diesel engine plant.²⁷

These events have not encouraged United States and other foreign investors to channel their capital into Venezuela. Through the end of 1978 and into 1979, the Perez administration published figures showing authorized new foreign investment in Venezuela as high as 4.2 billion dollars.²⁸ Careful analysis, however, and a distinction among "authorized" new foreign investment, registered new foreign investment, and reinvestment figures indicate that new foreign investment in 1978 actually amounted to

26. Law of July 2, 1965 (concerning insurance and reinsurance companies), GACETA OFICIAL EXTRA. No. 984, July 9, 1975.

27. Mann, *Locking Out Foreign Investment: Government Attitudes Turn Off Foreign Capital*, BUS. VENEZUELA, Jan.-Feb., 1980, at 11. See also Pate, *Anpact's Abominable Snow Job: Rigging the Figures to Justify Decision 24*, BUS. VENEZUELA, Jan.-Feb., 1980, at 15.

28. VENEZUELAN-AMERICAN CHAMBER OF COMMERCE & INDUSTRY, UPDATE REPORT 4 (June 1979).

approximately 45.3 million dollars.²⁹ 1979 figures indicate eighty-three million dollars in foreign investment,³⁰ and 1980 figures were up eighty-four percent over the previous year.³¹ Thus, it is important to distinguish among Government statements concerning foreign investment, actual registered investment (as opposed to "authorized" investment), and reinvestment figures which generally indicate that existing firms are merely trying to maintain their current investment, but not expand.

II. MOVEMENT TO CONTROL NATURAL RESOURCES AND ECONOMIC ACTIVITY

A. *Economic Integration Movements*

In an effort to promote economic activity in Latin America, Venezuela joined with seven other Latin American nations to form the Latin American Free Trade Association (LAFTA) in 1960.³² The goal of LAFTA was to gradually eliminate intraregional trade barriers in order to accelerate the economic development processes of member nations. These nations hoped to achieve a Latin American Common Market by 1985. In 1980, with the goals of LAFTA largely unattained, a series of negotiations culminated in a revised approach, and the Latin American Integration Association (LAIA) replaced LAFTA.³³ Although Venezuela retained its membership, its trade relationships with the group are not very significant.³⁴

Disparities between the more developed nations of LAFTA (Argentina, Brazil, and Mexico) and the smaller nations (Colombia, Ecuador, Peru, Chile, Venezuela, and Bolivia) led to the formation of what was once regarded as the most successful Latin

29. *Id.*

30. Mann, *Venezuela Woos Investors*, N.Y. Times, July 15, 1980, at 1, col. 3.

31. VENEZUELAN-AMERICAN CHAMBER OF COMMERCE & INDUSTRY, OUTLINE REPORT ON VENEZUELA 4 (Apr. 1981).

32. Treaty Establishing a Free Trade Area and Instituting the Latin American Free Trade Association (Montevideo Treaty), Feb. 18, 1960, 30 U.N. ECOSOC, Supp. 4, U.N. Doc. E/333 E/CN 12/AC. 45/13/Rev. 1 (1960), reprinted in INTER-AMERICAN INSTITUTE OF INTERNATIONAL LEGAL STUDIES, INSTRUMENTS RELATING TO THE ECONOMIC INTEGRATION OF LATIN AMERICA 207 (1968). See also Radway, *supra* note 15.

33. Agreement Creating the Latin American Integration Association, signed at Acapulco, Mexico, June 27, 1980.

34. BUSINESS INTERNATIONAL CORPORATION, *supra* note 1, at 22.

American integration movement—the Andean Common Market (ANCOM). ANCOM, a subregional group, was established by the governments of Colombia, Ecuador, Chile, Peru, and Bolivia by the Agreement of Cartagena on May 26, 1969.³⁵ Venezuela entered the Andean Pact by signing the Consensus of Lima on February 13, 1973 and Chile later withdrew in 1976.³⁶ Despite Venezuela's active participation in the organizational meetings of ANCOM, and its membership in the Andean Development Corporation (CAF), the Caldera administration hesitated in joining the group. This hesitation was due, in part, to unresolved differences between the Venezuelan public and private sectors regarding the need for and treatment of foreign investment.³⁷ In 1974 the Consensus of Lima became effective, and under the new leadership of President Perez, Venezuela issued regulations conforming to chapter III of Decision 24, ANCOM's most significant provision.³⁸

B. *United Nations Charter on Economic Rights and Duties of States*

A major objective of Decision 24 and the Venezuelan imple-

35. Treaty of Cartagena, May 26, 1969, reprinted in 8 INT'L LEGAL MATERIALS 910 (1969). The Treaty of Cartagena is an Agreement of Andean Subregional Integration. See generally Ebb, *Transfer of Foreign Technology in Latin America: The Birth of Antitrust Law*, 43 FORDHAM L. REV. 719 (1974); Furnish & Atkin, *Andean Group's Program for Industrial Development of the Metalworking Sector: Integration with Due and Deliberate SPID*, 7 LAW AM. 29 (1975); Lisocki, *The Andean Investment Code*, 49 NOTRE DAME L. REV. 317 (1973); Perenzin, *Multinational Companies Under the Andean Pact: A Sweetener for Foreign Investors*, 7 INT'L LAW. 396 (1973); Schill, *The Mexican and Andean Investment Codes: An Overview and Comparison*, 6 LAW & POL'Y INT'L BUS. 437 (1974); Schliesser, *Recent Developments in Latin American Foreign Investment Laws*, 7 INT'L LAW. 357 (1973); Note, *Technology Trade and the Law: A Preliminary Exploration*, 6 LAW & POL'Y INT'L BUS. 85 (1974).

36. The Consensus of Lima is the final act of the negotiations concerning Venezuela's entry into the Cartagena Agreement, Feb. 13, 1973, reprinted in 12 INT'L LEGAL MATERIALS 344 (1973). See also text accompanying note 10 *supra*; note 51 *infra*.

37. See Radway, *supra* note 15, at 292.

38. ANCOM Decision 24, Common Regime of Treatment of Foreign Capital and of Trademarks, Patents, Licenses, and Royalties, Dec. 31, 1970, reprinted in 11 INT'L LEGAL MATERIALS 126 (1972) [hereinafter cited as Common Regime]. All references to the ANCOM Code or Decision 24 include the modifications contained in Decisions 37, 37a, 70, 103 and 109.

mentation of the Decision through Decrees 62 and 63 was to insure national sovereignty over each member nation's natural resources and domestic economic activities. It has been suggested that ANCOM had an influence on the deliberations of various United Nations committees which in 1974 culminated in the vote by 120 member nations of the General Assembly to adopt the Charter on Economic Rights and Duties of States.³⁹ In the preamble of the resolution adopting this important charter, the Assembly stressed that "the Charter shall constitute an effective instrument towards the establishment of a new system of international economic relations based on equity, sovereign equality, and interdependence of the interests of developed and developing countries."⁴⁰ The fundamental purpose of the Charter was to promote equity and cooperation among all states, irrespective of their economic and social systems. Article 2 states, *inter alia*, "Every State has and shall freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities."⁴¹ It goes on to explicitly provide the basis for the power of each state to regulate and control foreign investment within its borders, to regulate and supervise the activities of transnational corporations, and to nationalize, expropriate, or transfer ownership of foreign property within its borders.⁴²

C. *Nationalization of Hydrocarbons and Mining Properties*

Encouraged by the continuing United Nations debate over national sovereignty over national resources, and by populist rhetoric from Mexican President Luis Echeverria Alvarez (and previously from former Chilean President Salvador Allende Gossens), President Perez announced in 1975 Venezuela's nationalization of its hydrocarbon and mining properties.⁴³ Because of a forty-year gradual nationalization policy in the petroleum sector, the public transfer of ownership appeared to occur smoothly as many former foreign concessionaires remained with supply contracts and tech-

39. Bledel, *The Latin American Development Process and New Legislative Trends*, 10 GA. J. INT'L & COMP. L. 325 (1980). Charter of Economic Rights and Duties of States, G.A. RES. 3281, 29 U.N. GAOR, SUPP. (no. 31), U.N. Doc. A/9631 (1974) [hereinafter cited as Charter of Economic Rights].

40. Charter of Economic Rights, *supra* note 39, at Preamble.

41. *Id.* art. 2.

42. *Id.* art. 2(a)-(c).

43. See Organic Law, *supra* note 13.

nical assistance agreements. Privately, however, it appears that some of the financial and legal questions remain unanswered. Another interesting aspect of this nationalization was the role of the United States Government as a mediator. There is a long-standing tradition in Venezuela and throughout Latin America that foreign nationals are obliged, as a condition of investment, to waive their right of sovereign "cover." The "Calvo Doctrine" has required foreign investors to agree not to seek intervention by their home governments in the event of an investment dispute.⁴⁴ This policy is expressed in article 127 of the Venezuelan Constitution.⁴⁵ Thus, the intervention of United States Government officials at the request of the Venezuelan Government is more evidence of the decline of the Calvo Doctrine, which has perhaps outlived its most useful period.

Joint ventures between national companies⁴⁶ and foreign companies⁴⁷ are generally approved, especially in service contracts to further the exploitation of national resources. Recently, joint ventures have been particularly encouraged in activities in which the sophisticated technology involved does not yet exist within the national Venezuelan companies.

III. LEGAL FRAMEWORK FOR FOREIGN INVESTMENT

A. ANCOM's Decision 24

Decision 24 was ratified by the original members of ANCOM in December 1970, and it became effective in Venezuela on January 1, 1974. It established the framework for control of foreign capital, treatment of foreign technology, control over foreign banks, and access to local credit for foreign and mixed companies.⁴⁸ Decision 24 was designed to promote indigenous capital formation,

44. See generally D. SHEA, *THE CALVO CLAUSE: A PROBLEM OF INTER-AMERICAN AND INTERNATIONAL DIPLOMACY* (1955).

45. *Constitution*, 1961, art. 127 (Venez.).

46. This includes companies with national capital of 80% or more. See Common Regime, *supra* note 38, art. 1.

47. This includes companies with national capital of less than 51%, or a higher amount if that percentage is not reflected in the technical, financial, administrative and commercial management of the company. *Id.*

48. Mixed companies are those companies with national capital between 51% and 80%, provided that proportion is reflected in the disciplines listed in article 1 of the Common Regime for Treatment of Foreign Capital and of Trade-marks, Patents, Licenses and Royalties. See note 38 *supra*.

to protect ANCOM from foreign domination, and to prevent internal competition among its member countries to attract foreign capital and technology.⁴⁹ The principal focus of Decision 24 was to regulate, through agencies to be established in each country, the flow of vital new foreign capital and technology into the region and to direct its allocation without affecting the outflow of existing capital.

Article 6 of the Code mandates the establishment of a "competent national authority" in each member nation which shall fulfill the commitments of national participation in the technical, administrative, financial, and commercial management; control the capitalization of local companies; authorize the "exceptional" purchase of shares of such companies by foreigners; authorize profit or dividend remittances abroad; approve license agreements for the use of patents, trademarks, unpatented know-how, and other forms of technology transfer agreements; centralize the statistical and accounting information; and control registrations connected with direct foreign investment.

In August 1976, five of the six ANCOM member nations⁵⁰ met in Sochagota, Colombia to discuss the proposed liberalization of Decision 24. Effective October 1976, these five member nations agreed to certain key changes.⁵¹ The most important of these changes, embodied in Decisions 103⁵² and 109,⁵³ increased the allowable profit remittance ceilings for foreign investors from fourteen to twenty percent of the net registered capital base. Local governments were empowered to fix an even higher rate without

49. *Id.*

50. At this meeting Venezuela, Colombia, Ecuador, Bolivia, and Peru discussed ways to keep the subregional group intact, despite Chile's demands that the foreign investment rules be relaxed to an extent unacceptable to these five members.

51. Chile announced its intention to withdraw from ANCOM at this time, citing, among other reasons, a need to ease foreign investment restrictions much further than the other countries in the group were willing to permit. In the opinion of these authors, this decision enabled Chile to initiate a remarkable period of economic recovery and growth, while, by comparison, the ANCOM five have lagged ever since.

52. ANCOM Decision 103, Reform to the Common Rules for Treatment of Foreign Capital and of Trademarks, Patents, Licenses and Royalties, 20th Period of the Ordinary Session of the Commission, Aug. 4 & Oct. 30, 1976, Lima, Peru.

53. ANCOM Decision 109, 20th Period of the Ordinary Session of the Commission, Aug. 4 & Oct. 30, 1976, Lima, Peru.

obtaining prior approval from the Commission in Lima. Finally, the reinvestment ceiling was raised from five to seven percent of registered capital. Under the revised rules, capital from any ANCOM member nation is deemed national when invested anywhere in the Andean region.⁵⁴ Such capital was previously considered to be foreign when originating outside the host country, unless the investment met strict criteria for qualification as part of an Andean multinational company.⁵⁵ In addition, portfolio investments by international lending institutions and public financial institutions of any of the ANCOM member nations are now considered neutral investment (neutral capital).⁵⁶

B. Venezuelan Legislation

1. Decrees 62 and 63 and SIEX

Venezuela began to implement its ANCOM obligations in April 1974. In April 1974, Decrees 62 and 63 were issued to enact new Venezuelan foreign investment laws which were consistent with ANCOM's Decision 24. Decree 62 defined the sectors of economic activity reserved to national companies and barred new direct foreign investment in those sectors.⁵⁷

Decree 63 created the Superintendency of Foreign Investment (known by its Spanish language name of "Superintendencia de Inversiones Extranjeras" or SIEX) within the Ministry of Development. This national agency was organized to implement the purposes set forth in Decision 24.⁵⁸ SIEX is essentially administered by technocrats who conform investment and technology agreements to national economic development goals. These tech-

54. ANCOM Decision 103, *supra* note 52, arts. 1 (a), (b). *Accord*, Venezuelan Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977, art. 27.

55. ANCOM Decision 46, Andean Code on Multinational Enterprises and the Regulations with Regard to Subregional Capital, Dec. 18, 1971, *reprinted in* 11 INT'L LEGAL MATERIALS 357 (1972).

56. Decree 567, GACETA OFICIAL No. 31,960, Apr. 10, 1980 (implementing ANCOM Decision 124). The three international finance institutions (IFIs) named are the Andean Development Corporation (CAF), the Inter-American Development Bank (IDB), and the International Finance Corporation (IFC) of the World Bank.

57. Decree 62, GACETA OFICIAL EXTRA. No. 1,650, Apr. 29, 1974, art. 1, *reprinted in* 13 INT'L LEGAL MATERIALS 1220 (1974).

58. Decree 63, GACETA OFICIAL Nos. 1,650 & 30,412, May 31, 1974, *reprinted in* 13 INT'L LEGAL MATERIALS 1221 (1974). For detailed discussions of sectors reserved to national companies, see Radway *supra* note 15.

nocrats have considerable discretion in approving new investments, agreements involving the transfer or importation of foreign technology, access to local credit for foreign investors, and related issues pursuant to the rules and regulations. Other agencies have jurisdiction over particular sectors, such as the Ministry of Energy and Mines (oil, gas, and petrochemicals),⁵⁹ the Superintendencies of Banks and Insurance,⁶⁰ and the Venezuelan Tourism Corporation.⁶¹ In reality, however, SIEX is the principal door through which foreign investments must enter the country.⁶² Venezuela's entry into ANCOM strengthened the group's position on foreign investment. Although many foreign investors believed that Venezuela would attempt to mitigate the rigidity of the ANCOM Foreign Investment Code, it nonetheless enacted the Code in a very strict form. Many believe that these rules were applied more rigidly by the Venezuelan Government than by any other member country.

2. Decrees 2031 and 2442 and the Law on Transformation of Companies

In 1977, Venezuelan Decrees 2031⁶³ and 2442⁶⁴ replaced Decrees 62 and 63, respectively, incorporating the changes brought by ANCOM Decisions 103 and 109 in 1976. Decree 2442 reaffirmed the rules for investment approval, profit (dividend) remittances, reinvestments, technology transfers, and access to local credit as modified by the 1976 changes. This statute additionally permits national companies to convert to mixed status through capital increases, even in sectors reserved to national companies.⁶⁵ Foreign-owned firms are also permitted to comply with equity fade-out requirements through capital increases.⁶⁶ More flexibility was thus introduced to attract new foreign investment.

All foreign investments made prior to January 1, 1974, (pre-

59. Decree 1225, Oct. 21, 1975. A bill is presently being drafted to expand the jurisdiction of the Ministry of Energy and Mines.

60. Decree 2031, art. 3, para. 2, GACETA OFICIAL No. 31,171, Feb. 9, 1977.

61. Decree 2810, Aug. 22, 1978.

62. Address by Franklin Hoet-Linares, before the Coral Gables, Florida, Chamber of Commerce (July 9, 1980)[hereinafter cited as Hoet-Linares].

63. Decree 2031, art. 3, para. 2, GACETA OFICIAL No. 31, 171, Feb. 9, 1977.

64. Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977.

65. *Id.* art. 52.

66. *Id.* art. 54.

existing investments) had to be registered with SIEX by December 30, 1974.⁶⁷ Foreign investments which entered the country after that date (new investments) require prior approval and registration. Reinvestments must also be registered with SIEX. Any foreign investor may automatically remit up to the twenty percent dividend ceiling and automatically reinvest up to seven percent without approval. SIEX permission must be obtained by foreign companies if the increase in registered capital exceeds seven percent while there is no limit whatsoever for reinvestment in national and mixed companies. All new industrial projects and expansions of existing ones must be registered with the Ministry of Development in the Registry of Projects.⁶⁸

SIEX may approve foreign investment if the company proposing investment meets at least two of the following criteria:⁶⁹

(1) the new company will incorporate or plan to incorporate in their products a local value-added component of fifty-one percent or more;

(2) it is committed to export products which contain a local value-added component of thirty percent or more;

(3) it will generate a significant amount of national employment;⁷⁰

(4) it will establish the facility in lesser developed regions of the country;

(5) it will incorporate technology considered by SIEX to be convenient for the country;

(6) it offers to transform to a mixed or national company in a shorter period than the fifteen-year term established in Decision 24; and

(7) it pledges to invest or reinvest resources generated within the country in portfolio investments (*valores de fomento en cartera*).⁷¹ These provisions authorize SIEX to approve new for-

67. Ministry of Development Resolution 730, GACETA OFICIAL No. 31,930, Feb. 25, 1980.

68. *Id.*

69. Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977.

70. No specific guideline is available to define "significant." We understand that it is being negotiated on a case-by-case basis.

71. Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977, ch. VI, art. 36, lists the following as approved portfolio investments:

(a) Certificates of direct or indirect public debt.

(b) Mortgage bonds [*cédulas*] issued by mortgage banks in the context of the disposition of the General Law of Banks and Other Credit Institu-

eign investment that is consistent with Venezuela's development goals. Investments incorporating needed technology or manufacturing products currently being imported (import substitutes) are generally afforded top priority. It has been suggested recently that foreign companies may be permitted to establish businesses with up to eighty-five percent of foreign capital if they agree to transform to a mixed company after fifteen years.⁷² In practice, however, this has not happened. National investors, who are accustomed to a minimum of twenty-five to forty percent return on investment, would not be interested in assimilating into companies established by foreign capital with much longer term market objectives and lower short term returns on investment. In fact, these ownership terms will only be authorized for investments in food processing or agriculture.

Decree 2031 reserves certain sectors of economic activity to national companies.⁷³ This clarifies previous legislation regulating domestic marketing (internal commercialization), because it extends the deadline for marketing firms to formalize their intention to divest either by increasing capital or selling existing shares between May 1 and December 30, 1977.⁷⁴ This deadline was subsequently extended to the end of 1979 for firms that requested it.

tions and to those dispositions that are included in other special laws.

(c) Financial bonds issued by finance companies [*sociedades financieras*] regulated by the General Law of Banks and Other Credit Institutions.

(d) Certificates of deposit [time deposits], negotiable or not, which are issued by commercial banks, mortgage banks, finance companies, and savings and loan association entities.

(e) Mercantile obligations [bonds] issued by companies through a public offering, in accordance with the dispositions of the Capital Markets Law, that do not entitle the holder to participate in the technical, financial, administrative or commercial management of the company.

(f) Certificates or obligations issued by the Andean Development Corporation (CAF). SIEX, with the prior consent of the Finance Ministry, may also authorize as portfolio investments [*valores de fomento en cartera*], within the context of this Article, predetermined portfolio investments that are not included in the items above, following a suitable study and evaluation of their characteristics, in conformance with the law. (Translation by the authors.)

72. BUS. WEEK, Nov. 17, 1980, at 65; Financial Times, June 8, 1981, § III (Special Supp.), at VII.

73. Decree 2031, GACETA OFICIAL NO. 31,171, Feb. 9, 1977, art. 1(a)-(d). See also Radway, *supra* note 15, at 295-96.

74. This, however, still does not completely clarify "internal" marketing.

Under certain circumstances SIEX could extend the transformation period or recommend certain conditions for divestment.⁷⁵ Pursuant to the statute, companies engaged in the manufacturing and marketing of Venezuelan goods are considered manufacturers. They therefore need not divest provided the sale of locally manufactured goods generates at least fifty-one percent of their gross sales revenue, the value added locally to the products is at least thirty percent of cost, and the marketing activity is related to the manufacturing endeavor.⁷⁶ Whether national control in those cases requiring transformation must extend to management, in addition to capital, is negotiated on a case-by-case basis.

Decree 2031 requires enterprises engaged in trading goods to become national. Unlike Decree 62, however, this decree does not refer to service companies.⁷⁷ Therefore, companies involved in leasing operations apparently are not required to fade down or out.⁷⁸ Furthermore, companies of mixed status prior to January 1, 1974, do not need to nationalize. International firms, however, will not be allowed to trade stock of local companies, except to or from other foreigners, and if the traded shares are registered on the stock exchange, the sale will not need prior authorization from SIEX. The 1977 law changed the 20-80 rule in the design, consulting, and professional services sectors to allow SIEX to provide an exception when the foreign company is at least fifty-one percent locally owned and contributes technology which would promote the country's development.⁷⁹

To ensure that national companies comply with ANCOM fade-out rules, in August 1975 Venezuela enacted a law governing the transformation of foreign firms into mixed or national firms.⁸⁰ Under Decree 2442, the vast majority of new companies must be at least fifty-one percent locally owned from the inception; otherwise, companies must agree to fade-down (transform) to a maxi-

75. Decree 2031, GACETA OFICIAL No. 31,171, Feb. 9, 1977, art. 2.

76. *Id.* art. 1, para. 3.

77. *Id.* art. 1(c). *See also* Decree 62, GACETA OFICIAL EXTRA. No. 1650, Apr. 29, 1974, art. 1(b).

78. The Superintendent of Banking has maintained this position in practice. No decree or resolution has been passed.

79. *See* Decree 2031, GACETA OFICIAL No. 31,171, Feb. 9, 1977, art. 1(d). *See also* Radway, *supra* note 15, at 296-97.

80. Law on Transformation of Foreign Companies, GACETA OFICIAL No. 30,744, Aug. 21, 1975.

imum forty-nine percent foreign equity position.⁸¹ Since 1976, foreign investors may accomplish this divestment by increasing capitalization, rather than by selling shares.⁸² The 1975 Transformation Law requires the transfer to be authorized and approved by SIEX, which has established certain criteria for divestment⁸³ in order to prevent the concentration of wealth in the hands of a few large industrial groups.

81. Companies agreeing to fade-down must do so over a fifteen-year period as set forth in article 28 of ANCOM Decision 24. Companies that export 80% or more of their production to third countries are exempt. *Id.* art. 34. All industrial companies, with the exception of automotive firms, established prior to January 1, 1974 have the option of remaining foreign owned if they elect not to take advantage of the ANCOM trade and tariff liberalization benefits. If they opt for the benefits, they must sign the transformation agreement. *See* Decree 2442, GACETA OFICIAL EXTRA. No. 21,000, Nov. 15, 1977, arts. 49, 51.

82. SUPERINTENDENCIA DE INVERSIONES EXTRANJERAS, VENEZUELA: A GUIDE FOR FOREIGN INVESTMENT AND TECHNOLOGY LICENSING IN THE 1980's, 32-33 (Sept. 1980) [hereinafter cited as GUIDE].

83. *See* Law on Transformation of Foreign Companies, GACETA OFICIAL No. 30,744, Aug. 21, 1975, art. 4. The divestment criteria of Superintendencia de Inversiones Extranjeras (SIEX) include the following:

- (1) The distribution of shares among national investors;
- (2) The right of workers of the company to participate in the transformation process, as well as the participation rights of unions or similar workers' associations, including workers' cooperatives, savings and credit trust companies, pension or retirement funds, or professional technical associations, social protection institutes and, in general, any other similar association;
- (3) An increase in the number of new national shareholders participating;
- (4) The placement of shares for sale through public offer, preferably in accordance with the rules and capital structure requirements set forth in the Capital Markets Law, for the corporations registered with open capital. This law established the *sociedades anónimas inscriptas de capital abierto* (SAICA) as a new legal form in an attempt to encourage broader equity participation by Venezuelan national investors;
- (5) The opportunity to offer shares on the open market (requires prior approval of SIEX).

GUIDE, *supra* note 82.

Although paragraph two requires a portion of the shares to be offered to the workers, it does not specify that these must come from the foreign investor's participation. In practice, SIEX has permitted the offer to come generally from the shareholders, with the workers then acquiring pro-rata interests from nationals and foreigners.

3. Capital Markets: Developments Affecting Financial Institutions

In 1973 the first Capital Markets Law⁸⁴ was enacted to encourage the formation of private capital (converting savings to investment) through Venezuela's existing stock exchange.⁸⁵ This was the first major attempt to improve the national financial structure and encourage capital formation for industrialization and growth. This enactment provided the basis for adequate supervision of the market, protection for minority shareholders, more accurate financial information for investors, and tax incentives to encourage companies to go public.

Following the promulgation of this Capital Markets Law in 1974, the Government established three new development institutions designed to channel medium- and long-term funds to the private and public sectors. The Venezuelan Investment Fund is the most important of these. It was created to invest excess oil profits abroad until they could productively serve domestic industries. Venezuela also established the Agricultural and Industrial Credit Funds for the disbursement of loans encouraging the expansion of the agricultural and industrial sectors.⁸⁶

In 1975 three major Venezuelan events affected the domestic capital market. First, Venezuela's chief development bank, the Corporación Venezolana de Fomento (CVF), was reorganized. It now concentrates exclusively on industrial development rather than on working capital loans. CVF's activities include promoting and creating new industrial and agro-industrial enterprises, providing technical assistance, and acting as a holding company. Most CVF loans are long term and are granted for medium-scale basic industries and large projects. The Banco Industrial de Ven-

84. Venezuelan Capital Markets Law, GACETA OFICIAL EXTRA. NO. 1,566, Jan. 31, 1973.

85. The general public represents only a small percentage of buyers. The main buyers of publicly traded securities are trust funds, savings funds, banking institutions, money desks and certain investment firms. See generally Wiles, *The Venezuelan Capital Markets Law*, 8 INT'L LAW. 303 (1974).

86. Loans granted under both the Agricultural Fund and the Industrial Credit Fund are made for extended periods at concessionary rates. Medium-sized Venezuelan and mixed companies are eligible. Another investment fund exists, Corporación de la Pequeña y Mediana Industria, which also provides concessionary financing for small and medium-sized companies to acquire capital goods. It is expected that all of these industrial credit organizations will be nationalized and centralized in Banco Industrial de Venezuela.

ezuela (BIV), CVF's subsidiary, is an important source of industrial credit. It provides short- and medium-term financing (up to five years) for manufacturing, commerce, transport, storage, and other activities in the industrial, mining, and petroleum sectors.⁸⁷ Second, a strong commercial paper market began to develop in Venezuela. In 1975 Sociedad Financieras Valinvença and Union were established to develop a primary market for securities and commercial paper. Valinvença has modeled the commercial paper market after Argentina's acceptance market, while Union initiated the repurchase agreement market. Finally, a second Capital Markets Law was enacted in 1975. The object of this legislation was to allocate share ownership as widely as possible. The Government promoted this objective by introducing generous tax incentives encouraging firms to become public (open capital) companies or *sociedades anónimas inscriptas de capital abierto* (SAICAs). In order to qualify as SAICAs under the 1973 law, companies were required to distribute fifty percent of their stock among at least fifty shareholders for each one million bolivares of paid-in capital. This requirement proved unrealistic for a nation in which the most widely held company (Electricidad de Caracas) has only 8,000 shareholders. As a result, not one company ever converted to SAICA status under the old law.

The 1975 version of the Capital Markets Law maintains the fifty percent stock distribution requirement. However, it omits a minimum number of shareholders and the maximum size of holding companies which, by publicly distributing at least fifty percent of their shares, may become eligible for a twenty-five percent credit on corporate income tax. This tax credit ranges as high as fifty percent for distributions in excess of seventy-five percent of capital. The Capital Markets Law also provides that shareholders and bondholders of SAICAs are exempt from taxes on interest or dividends. In addition, capital gains are exempt from tax if they are reinvested in securities issued by SAICAs. Following the promulgation of this law, several Venezuelan banks,⁸⁸ financiers, textile companies, and breweries opted for SAICA status. There was

87. The policy of Banco Industrial de Venezuela (BIV) is to give priority to ventures that save or earn foreign exchange or that use domestic raw materials, particularly in agro-industry, textiles, construction materials, automotive components, wood and paper, and chemicals.

88. The most successful experience as SAICA is undoubtedly that of Banco Provincial de Venezuela.

speculation that foreign-owned firms might follow suit, but this has not materialized. The tax incentives may encourage expansion of the capital market; however, many investors still find SAICAs unattractive because their shares are overpriced, they are overcontrolled, and their price/earnings ratio is below average.⁸⁹

4. Technology Transfer and Nonfinancial Service Companies

(a) Licensing and Decree 746

Pursuant to Decree 2442, all agreements involving the transfer of technology and licencing of valid patents and trademarks must be registered with and approved by SIEX within thirty days after execution in order to attain legal effect.⁹⁰ Since Venezuelan courts lack the authority to halt infringements and violations of industrial property rights, patents and trademarks should be registered immediately in Venezuela in order to prevent piracy. Venezuela operates on a first-to-register basis rather than the first-to-use system of the United States.

The legal definition of technology includes a multitude of fields ranging from the licensing of patents to the transferring of human knowledge and services (including training) from abroad. Under a liberal interpretation, a conference given by a foreign speaker could even qualify as a form of technology transfer. In practice, however, only the transfer of human knowledge and the performance of services (*e.g.*, engineering, design, or consulting) contracted by a company or an individual in Venezuela for private use fall under the scope of these rulings.⁹¹

Royalty payments and technical assistance fees are limited by this regime. Additional payment restrictions are imposed on majority foreign-owned subsidiaries.⁹² Royalty payments between a local subsidiary and its controlling parent company are strictly prohibited under Decree 2442, and they do not qualify for a de-

89. Interview with F.J. Amador, Jr., Second Vice-President, Latin American Marketing Unit, Chase Manhattan Bank (July 1981) [hereinafter cited as Amador, Jr.].

90. Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977, art. 63.

91. Address by F. Roland Matthies, of the Venezuelan law firm Matthies & Klahr Zighelboim, before the Council of the Americas, in New York City (June, 1980).

92. For a discussion of this restriction in a similar provision under Colombian law, see Radway, *Transfer of Technology to Colombia: A Proposal to Modify Decision 24*, 12 LAW AM. 321 (1980).

duction as an expense from gross income.⁹³ Such payments would generally be treated as dividends for tax purposes. Royalty payments to an unrelated foreign licensor may be made by mixed companies, national companies, and firms which have signed transformation contracts with Venezuela.

Decision 24⁹⁴ and Decree 2442⁹⁵ list restrictive clauses which may not be included in new contracts.⁹⁶ SIEEX does not authorize the registration of technology contracts which contain any of eighteen specific clauses that restrict the freedom of the licensee to make a wide range of decisions.⁹⁷ SIEEX may add other clauses

93. Decree 2442, GACETA OFICIAL EXTRA. NO. 2,100, Nov. 15, 1977, art. 68.

94. See Common Regime, *supra* note 38, arts. 20, 25.

95. Decree 746, Technology Contract Registration, GACETA OFICIAL NO. 30,635, Mar. 1, 1975, art. 1.

96. ANCOM Decision 24 lists two types of prohibited clauses, one pertaining to "Importation of Technology," Common Regime, *supra* note 38, arts. 19, 20, and the other to "Exploitation of Trademarks," *id.* art. 25. Decree 2442, GACETA OFICIAL EXTRA. NO. 2,100, Nov. 15, 1977, and Decree 746, GACETA OFICIAL NO. 30,635, Mar. 1, 1975, consider both categories as transfer of technology. Article 66 of Decree 2442 authorizes SIEEX to define the restrictive commercial provisions and other clauses which would be objectionable to the government.

97. The following provisions are from ANCOM Decision 24:

(1) Require the acquiring party to purchase certain raw materials equipment, materials, or personnel from a source designated by the technology supplier (exceptions for raw materials, intermediates or capital goods supplied at market prices);

(2) Provide that the supplier has the right to establish prices for the resale of the products manufactured from the technology or under the trademark;

(3) Restrict the volume and structure of production;

(4) Prohibit the use of competitive technology;

(5) Establish the supplier's right to purchase some or all of the output;

(6) Compel the purchaser to transfer to the supplier (grant back) the rights to improvements or inventions arising from use of the technology;

(7) Require the user to pay royalties on patents or trademarks which are not used;

(8) Prohibit or limit exports of the products made from the technology or under the trademark, except in exceptional cases, but in no case prohibit exports to other ANCOM countries;

(9) Provide for royalties for intangible contributions by a foreign company to its parent or other affiliated company (nor will such payments be deductible for tax purposes);

(10) Provide for dispute settlement outside of Venezuelan courts.

Common Regime, *supra* note 38, arts. 20, 25.

to this list. Decree 746⁹⁸ provides that SIEX has ninety days to rule on the legality of clauses in new contracts, and if the contract is part of a previously authorized project, authorization must be granted in fifteen days.⁹⁹

Technology transfer contracts are typically limited to five years, and they must provide that the foreign firm will train local personnel in the necessary procedures within that term. Subsequent to the enactment of Decree 746, which required existing agreements to conform as of December 31, 1975, SIEX stated that technology transfer contracts are subject to the same maximum duration. According to Decree 2442, however, SIEX may authorize technology agreements for up to fifteen years with approval of the relevant Ministry.

(b) SIEX and Its New Philosophy

In 1979, the new administration faced severe problems in deter-

The following provisions are from Decree 746:

- (11) Prohibit the manufacture or sale of products using the technology after the agreement expires;
- (12) Prohibit the use of technical knowledge acquired through the technology after the agreement expires;
- (13) Prohibit the use of similar or like commercial trademarks after the contract period;
- (14) Impose the use of a predetermined quality control system on the user;
- (15) Require the user to sell part or all of the production to the supplier;
- (16) Establish royalty payments for technical assistance not supplied;
- (17) Require royalty payments when the user has purchased the technology outright;
- (18) Establish the obligation by the user to pay the taxes of the supplier;
- (19) Oblige the user to grant an irrevocable right to sell the manufactured products to the supplier;
- (20) Require the user to grant the supplier rights to use any inventions or improvements arising out of the processes or products which are the object of the contract;
- (21) Other clauses with equivalent effects.

Technology Contract Registration, GACETA OFICIAL No. 30,635, Mar. 1, 1975, art. 1. For a more detailed discussion, see Radway, *supra* note 15 at 302-08.

98. See Decree 746, Technology Contract Registration, GACETA OFICIAL No. 30,635, Mar. 1, 1975.

99. *Id.* art. 7.

mining the country's official debt. Foreign investment appeared to be a low priority. The attitude of the previous government was that oil rich Venezuela did not need foreign capital. That attitude continues to persist at very high executive and legislative levels and in the private sector. Initially the local private sector did not publicly oppose that position, and complaints by foreign groups were ignored.

SIEX was neglected by this new administration. An official from the Customs Agency was assigned an acting superintendent with no experience in foreign investment or technology transfer. He was replaced several months later by the Deputy Minister of Finance, also an interim appointee, who clearly had too many other significant responsibilities. More than a year after the inauguration of the Herrera Government, another acting superintendent was appointed.¹⁰⁰ An economist, this official had some background in international trade and economics, and had participated in economic studies of Venezuelan investment and growth options. The new superintendent soon realized that credibility was part of the problem, and he proceeded to cultivate the foreign investment community by filling several important vacancies on the staff and reducing the processing time for applications. He announced on several occasions that he viewed SIEX more as an investment promotion agency than as a controller of foreign investment. This vital message was heard around the Western world.

(c) Technical Assistance, Technological Services, and Engineering Services

Confusion has existed over the scope and meaning of "technology transfer" within Decision 24 and Decree 63 (later 2442). The laws were apparently drafted to regulate specific types of companies, yet they have been applied generally. Tax consequences normally follow determination of the legal effect. While the tax consequences of ordinary license agreements for patents or trademarks (and the royalty and technical assistance payments therefor) were understood, several decrees and regulations complicated the problem for companies providing engineering, design, consulting, or similar services. The 1978 Income Tax Law (discussed *infra*) further complicated this situation as did a decree

100. This was Dr. Alfredo Gonzalez Amare.

later in 1978 granting a tax exemption for foreign services companies working for Venezuelan entities on important projects (Decree 2932), and one in March 1979 to clarify these technology transfer definitions and the tax consequences (Decree 3106).

Decree 2932 provided an exemption from Venezuelan income tax for profits arising from payments received for technical assistance or technological services rendered from abroad to Government enterprises. The exemption was limited to those enterprises performing industrial activities other than mining, hydrocarbons, or related activities, and to those companies in which the ownership of public entities is greater than eighty percent.¹⁰¹

Decree 3106 was passed to clarify the technology transfer definitions. "Technical assistance" was defined to include the supply of instructions, written documents, recordings, films, and other similar material of a technical nature intended for the purposes of the elaboration of a work project or product intended to be sold. Technical assistance may include the furnishing of technical knowledge or engineering services, including the supply of technical data, specifications, diagrams, plans, instructions, and the provision of basic and detail engineering and related services, such as engineering services, project research and development, and advisory and consultant services.¹⁰² The decree also defined the latter three terms. "Engineering services" are defined as the execution and supervision of the assembly, installation, and starting up of the machinery, equipment, and production plants; the gauging, inspection, repair, and maintenance of machines and equipment, and the making of tests and assays, including those required for the purposes of quality control. The term "projects' research and development" is defined as the elaboration and execution of pilot programs, laboratory investigation, and experiments; the exploitation services; and the technical planning and programming of production units. "Advisory and consultant services" are defined as the carrying out of external purchases; the representation, advice, and instructions furnished by technicians; and the rendering of technical services for the administration and management of enterprises in any of the lines of activities or operations of the

101. Decree 2932, Nov. 7, 1978, GACETA OFICIAL No. 31,611, Nov. 10, 1978, art. 1.

102. Decree 3106, Feb. 27, 1979, GACETA OFICIAL No. 31,686, Feb. 28, 1979, art. 2.

same.¹⁰³ Finally, for income tax purposes, "technological services" are defined as the licensing, for use and exploitation, of patents or similar industrial property rights.¹⁰⁴ Decree 476, effective January 1, 1980,¹⁰⁵ superceded Decrees 2932 and 3106. That law includes approximately the same definitions and tax consequences as Decree 3106; however, its cancellation of Decree 2932 removes the tax protection given to companies supplying foreign technical assistance or technological services to Venezuelan Government enterprises.

5. 1978 Income Tax Law

(a) General Structure

Venezuelan taxes are among the lowest of the major Latin American countries. Superceding the 1966 Tax Law, the new Income Tax Law took effect on July 1, 1978,¹⁰⁶ and it attempts to reduce tax evasion, increase the impact of incentives, stimulate the stock market, and reduce fiscal dependence on petroleum reserves. Venezuelan taxes include personal and corporate income taxes, an income tax imposed on mining and hydrocarbon activities, import duties, and various stamp registration and recording taxes. The majority of individuals and corporations are taxed at graduated rates. Taxpayers engaged in the hydrocarbon or mining industry and related activities, however, are subject to flat rate taxation. Each category of tax has individual rates, credits, and rules for determining taxable income, taxable basis, and deductions. There are three schedules (*tarifas*) of income taxes under the Income Tax Law. Schedule 1 applies tax rates to the income of individuals, schedule 2 applies to corporations other than those engaged in hydrocarbon or mining activities, and schedule 3 applies a much higher rate to companies engaged in hydrocarbon or mining activities.

(b) Corporate Taxation

The income of corporations which are not engaged in hydrocar-

103. *Id.*

104. *Id.* art. 3.

105. Decree 476 to Regulate Articles 56 and 88 of the Income Tax Law, GACETA OFICIAL SPECIAL No. 2,531, Sept. 31, 1979, art. 13.

106. Venezuelan Income Tax Law of 1978, GACETA OFICIAL SPECIAL No. 2,227, June 23, 1978.

bons and mining is subject to a progressive tax ranging from eighteen percent on taxable income of up to Bs. 300,000 (70,000 dollars) to fifty percent on income in excess of Bs. twenty million (4.7 million dollars).¹⁰⁷ Under the former law, the rate extended from fifteen percent on the first Bs. 100,000 to fifty percent on more than Bs. twenty-eight million. Tax rates on the income of such corporations are provided by schedule 2 in article 62 of the law.¹⁰⁸

Corporations engaged in the mining and hydrocarbon industries and related activities are subject to flat sixty percent and 67.7 percent rates, respectively.¹⁰⁹ Mining companies whose gross income is less than Bs. ten million are subject to the corporate tax rates of schedule 2. As of July 1, 1978, income from agriculture, livestock, fishing, and forestry activities may be tax exempt for a ten-year period.

The taxation of branches of foreign corporations is similar to that of local corporations under schedule 2. However, an additional twenty percent participation tax is levied on net income remaining after payment of income tax, regardless of whether the branch remits the full amount to the home office. This tax is in lieu of the twenty percent tax imposed on dividends paid to non-resident shareholders of domiciled corporations. Subsequent profit remittances are not taxed further, but foreign investors are subject to the twenty percent ceiling under Decree 2442.¹¹⁰

(c) Dividend and Reinvestment Limitations and Resolution
324 on "Limbo Money"

Funds earned on excess of the profit or dividend remittance

107. *Id.* art. 8.

108.

Schedule (Tarifa) 2

<u>Income (Bs.)</u>	<u>Rate (%)</u>
0 - 300,000	18
300,000 - 2.5 million	30
2.5 million - 5 million	35
5 million - 20 million	45
20 million and up	50

Id. art. 62.

109. *Id.* arts. 9, 10.

110. Decree 2442, Nov. 15, 1977, GACETA OFICIAL EXTRA. No. 2,100, ch. V, arts. 32, 33.

ceiling of twenty percent and the reinvestment ceiling of seven percent are called "limbo funds." SIEX had permitted capitalization of limbo funds through the use of an account called "Reserve for Reinvestment," but the 1978 Income Tax Law provides that such transactions (which require board declaration of a stock dividend) now require a dividend withholding tax of twenty percent. The result is that only eighty percent of the blocked profits could be added to the capital base to which future dividends would be subject. Following an earlier Colombian policy,¹¹¹ the Venezuelan Ministry of Finance issued Resolution 324 in September 1980 which allows foreign-owned companies in Venezuela to reinvest amounts in excess of seven percent without declaring a stock dividend by using the "Reserve for Reinvestment" account. The companies must obtain SIEX authorization and establish that the funds will be used to finance endeavors labeled as industrial expansion projects and defined as development priorities in the VI NDP.¹¹²

(d) Taxation of Engineering, Construction, and Other Service Companies

Although Venezuela generally taxes income only when it arises from economic activities carried on within the country or from Venezuelan assets, income derived from technical assistance or technical services performed abroad but utilized in Venezuela is also taxed. Rather than allowing specific deductions from such income, the Tax Law provides that a certain percentage of gross income is presumed to be (net) taxable income. The 1978 Tax Law¹¹³ raised to ninety percent from eighty percent the percentage of gross income from royalties, technical assistance, and engineering services presumed to be taxable as net income. Decree 476¹¹⁴ published definitions designed to clarify this situation. This Decree defined the two major categories of technical assistance and technological services, and included the following: guidelines

111. See Radway, *supra* note 92, at 330 & n.30.

112. Ministry of Finance Resolution 324, GACETA OFICIAL No. 32,067, Sept. 12, 1980. See also VENEZUELAN-AMERICAN CHAMBER OF COMMERCE & INDUSTRY, FLASH REPORT, 6 (Sept. 1980).

113. Venezuelan Income Tax Law of 1978, GACETA OFICIAL SPECIAL No. 2,227, June 23, 1978, arts. 56, 57.

114. Decree 476 to Regulate Articles 56 and 88 of the Income Tax Law, GACETA OFICIAL SPECIAL No. 2,531, Sept. 31, 1979, art. 13.

for characterization of the net taxable income from these two activities (thirty percent of gross income for the former and fifty percent for the latter); guidelines for allocation of each of these two categories when the particular percentages are not specified in the agreement (twenty-five percent to the former and seventy-five percent to the latter); guidelines for allocation of the income to services performed inside and outside Venezuela when not specified in the agreement (forty percent deemed Venezuelan source and sixty percent foreign source); the characterization of income from licenses of trademarks and similar property rights, their deductions, and allowable costs; and those cases where the Decree is not applicable.¹¹⁵

(e) Withholding Taxes on Loan Interest and Technical Services Payments

Interest paid to foreign banks and other financial lending institutions without Venezuelan branches is subject to a fifteen percent withholding tax.¹¹⁶ Interest and premium income on loans held by local Venezuelan entities, however, is not subject to withholding tax and is taxed as ordinary income. Interest paid to foreign banks for loans of more than one year duration for industry, agriculture, construction, fishing, forestry, and other priority development areas is now exempt from the fifteen percent withholding tax.¹¹⁷ Interest paid to foreign nonfinancial entities is subject to corporate tax rates and is withheld at the source. Under a companion law, however, even this interest is exempt if the loan is for financing the acquisition of capital assets for the production of income in the same priority areas; if it is for not less than a five-year term; and if it is at a concessionary rate (8.5 percent including commissions and related services).¹¹⁸

Taxes on fees or royalties for technical assistance or technological services must be withheld at the source, on an accrual basis, by the beneficiary of the services, and deposited or credited with appropriate treasury accounts within a very short period thereafter.¹¹⁹ When such services are rendered by other Andean Pact

115. *Id.* arts. 1-7.

116. DELOITTE, HASKINS & SELLS, INTERNATIONAL TAX & BUSINESS SERVICE, TAXATION IN VENEZUELA 25 (1980).

117. Decree 2736, GACETA OFICIAL No. 31,526, July 11, 1978.

118. Decree 2837, GACETA OFICIAL No. 31,565, Sept. 5, 1978.

119. Decree 476 to Regulate Articles 56 and 88 of the Income Tax Law,

member countries, Decision 40 of the Cartagena Agreement, concerning avoidance of double taxation among members, shall apply.¹²⁰ Withholding agents for oil or mining companies and their affiliates must file an additional withholding statement quarterly with the tax authorities.¹²¹ Tax exemptions are available for interest on foreign loans providing the financing, refinancing and working capital of companies dedicated to bauxite extraction, production of alumina or aluminum through integrated processes involving alumina reduction, and hot and cold aluminum lamination.¹²²

6. Labor Law Structure

(a) Unions in Government and Society

Approximately one-half of Venezuela's working population is unionized. Most of the legally recognized unions are affiliated with the Venezuelan Workers Confederation (CTV). Labor syndicates such as the CTV are composed of unions from related sectors, and they are permitted to negotiate collective labor contracts. An employer is obliged to enter a collective contract with the union if seventy-five percent of an employer's workers request it. Collective contracts run from one to three years and may include everything from wages and fringe benefits to work rules and grievance procedures.¹²³ Since wages are relatively high today, the major concern of the unions is to increase the workers' fringe benefit packages. Collective contracts have been negotiated and implemented in the petroleum, steel, paper, and tobacco industries.

(b) General Considerations and Protective Orientation

Venezuela's labor legislation stipulates that at least seventy-five percent of all workers in an enterprise must be citizens of Venezuela. This percentage must be calculated separately for salaried employees and wage earners. Managers and other key executives are often excluded from the seventy-five percent requirement. A company which is unable to meet the seventy-five percent re-

GACETA OFICIAL SPECIAL No. 2,531, Sept. 31, 1979, arts. 8, 9.

120. *Id.* art. 12.

121. *Id.* art. 10.

122. Decree 3050, GACETA OFICIAL No. 31,669, Feb. 5, 1979.

123. See SUPERINTENDENCIA DE INVERSIONES EXTRANJERAS, *supra* note 82, at 52-55.

quirement, due to the unavailability of workers with particular technical skills, must apply for a waiver from the national Labor Office. Labor shortages in recent years and the selective immigration policy of the present Government have facilitated the availability of these waivers.¹²⁴

Venezuelan unemployment in 1980 was estimated at eight percent. The recent increase in unemployment can be attributed to worker dismissals, the slump in important economic sectors such as construction, the abandonment and slowdown of major projects, and the influx of lower priced labor from other Latin American countries. Underemployment is a serious problem today, particularly in the urban areas.

(c) Employee Fringe Benefits

In addition to providing a minimum wage,¹²⁵ minimum working conditions, and health and safety requirements, Venezuelan labor legislation provides a minimum benefit package for employees. The Government requires employers to make the following contributions: (1) a two percent tax on annual gross payroll and other remunerations, including housing and other fringe benefits, which must be paid to the Instituto Nacional de Cooperacion Educativa (INCE) to finance the technical training of workers; (2) a tax at the rate of either seven, eight, or nine percent on salaries up to Bs. 3,000 per month, according to the degree of risk assigned to the industry by the Social Security Administration (IVSS)¹²⁶ (In addition to the employer's contribution to Social Security, a four percent tax must be withheld from employees' salaries); (3) full wage payments for nine legal holidays and all Sundays, and a minimum vacation of fifteen paid working days per year; and (4) a maximum distribution among the employees of ten percent of each year's net profits, equal to at least fifteen days' pay, but no more than two months' base salary.¹²⁷

124. *Id.*

125. The Venezuelan minimum wage has been approximately seven dollars per day since 1980.

126. Engineering and related services are likely to be taxed at 7%, but the construction industry is typically taxed at 9%.

127. This ensures employees a bonus in the event the employer has little or no profit.

(d) Difficulties in Termination

An employer is liable for a long-term service indemnity (*indemnización por antigüedad*) and a severance indemnity (*auxilio de cesantía*) when it dismisses an employee, regardless of the cause of dismissal.¹²⁸

After imposing wage hikes and price controls in March 1974, the Government passed an Unjustified Dismissals Law applying to workers employed by a firm for at least three months.¹²⁹ That Law stipulates that in cases other than voluntary retirement or resignation in which an employer would have to pay service and severance indemnities, the employer must pay twice the standard indemnities if an employee is unjustifiably dismissed. In order to contest a dismissal, the employee must file an appeal with a special commission consisting of representatives from the Labor Ministry, management, and the unions. If the commission decides in favor of the employer, the employee receives his standard indemnity. If a decision is rendered in favor of the employee, the employer must reinstate the worker, appeal the case, or pay the employee double indemnification.

C. *New Establishments in Venezuela*

1. Forms of Business Association

The foreign investor may enter the Venezuelan market in three practical ways: (1) by establishing a branch of the company in Venezuela; (2) by forming a Venezuelan company, including a joint venture; or (3) by appointing a delegate for the company.

(a) Branch of Foreign Company

A foreign company can establish a branch only in two limited situations: the "technological branch" for one-time engineering or construction activities for Government entities or high priority projects, or the strict sales-service representative office. The former will be explored *infra*, and the latter is approved only when

128. Each generally amounts to one-half of the last month's salary for each year of service. Thus, based on the employee's most recent salary, the employee receives one month's salary for each year of service at the time of termination.

129. Unjustified Dismissals Law of March 1974, GACETA OFICIAL No. 30,468, Aug. 8, 1974. The law requires that all companies file a quarterly list of employees with the Labor Bureau in their district and to inform the Bureau of all dismissals. *Id.*

SIEX considers the office not to be doing business in Venezuela.¹³⁰

(b) The Venezuelan Company and Joint Ventures

The second and most common way for a foreign investor to enter the Venezuelan market is the formation of a Venezuelan company, either in the familiar forms of *compañía anónima* (C.A.) or *sociedad anónima* (S.A.)—the equivalent of a United States corporation. Also available are SRLs and CRLs (resembling close corporations or personal companies limited to entities of smaller capital), partnerships, and SAICAs, as discussed earlier. The S.A. and C.A. are the forms most commonly selected by foreign investors. Since 1974, the new company must generally be a joint venture (*i.e.*, mixed company) which limits the foreign shareholder to a maximum of forty-nine percent ownership. At that level, however, the foreign shareholder may receive royalties of up to four percent from a licensing agreement to the joint venture company (JVC). The foreign shareholder may also receive profits from sales to the JVC of materials, parts, chemicals, and other items not produced in Venezuela. Minimal protection is available under Venezuelan Commercial and Civil Codes and Corporation Law for the minority shareholder, similar to that provided by Mexico and Brazil. Their rights include the use of an outside inspector (*Comisario*), the right to have certain important items discussed at extraordinary shareholder meetings requiring a high percentage for a quorum, and veto rights for authorization of significant transactions affecting the character, purpose, or financial liabilities and exposure of the JVC.

(c) Delegates

An additional option available to foreign investors is the appointment of a delegate or representative of the foreign firm. This representative is actually a self-employed or independent contractor who pursues the firm's business interests by soliciting customers or partners for transactions, and he maintains necessary relations with governmental authorities. Unlike the other two options, the appointment of a delegate requires no official approval, translation, or publication of corporate and related documents, and this option can be made operational almost immedi-

130. See *Financial Times*, June 8, 1981, § III (Special Supp.), at 22.

ately. He needs only a work permit, which is usually granted for one year and is renewable. One interesting feature of this option is that the delegate may thereafter qualify as a Venezuelan for purposes of the Foreign Investment Law,¹³¹ without losing his home country citizenship. He may then subscribe shares without prior approval, like any other Venezuelan citizen.

2. SIEX Policy on Branches

(a) Representative Office

SIEX continues to approve branches of foreign companies for limited purposes. The sales-service representative office has usually been a branch of a large international trading company, and it requires the activities of the responsible personnel to be limited to intermediation between the Venezuelan purchaser or user and the foreign company. This representative office is not considered to be actively engaged in its own business. In addition to the formal documentation requirements,¹³² a registration tax of 0.1 percent of the company's authorized capital causes many companies to have a second-tier subsidiary domiciled as a branch. Otherwise, branches are taxed as a corporation and pay a twenty percent participation tax on taxable income in lieu of the tax on dividends to nonresident shareholders.

(b) The Technological Branch

Venezuela recognizes that it does not possess the technology required to accomplish its formidable development plans. Many foreign companies are able to provide such technology without heavy capital investment, yet most are unwilling to enter into majority joint ventures to provide services while subjecting themselves to ANCOM profit remittance limitations. A solution put forth by SIEX is to allow companies undertaking a specific activ-

131. See Decree 2442, GACETA OFICIAL EXTRA. No. 2,100, Nov. 15, 1977, art. 2(b).

132. These requirements include copies of articles of incorporation, by-laws and registration documents of the parent, certificate of good standing, relevant sections of corporation law of state of incorporation, and power of attorney granting general representational powers to one or more attorneys-in-fact for customary purposes. Each of these documents must be duly consularized in the United States by the appropriate Venezuelan Consul General and then translated into Spanish for publication in Venezuela.

ity in Venezuela for either a Venezuelan Government entity¹³³ or a local private entity in an approved priority development project to qualify as a technology transfer arrangement, rather than as a foreign investment. Approvals of registration as a technology transfer agreement is generally limited to a single project and expires upon completion of that project.

3. Procedures for Energy-Related Activities

SIEX does not regulate activities within the scope of the Ministry of Energy and Mines.¹³⁴ The office of this Ministry which reviews applications has been referred to as "Mini-SIEX" by many observers. The policies actually applied by Mini-SIEX have mirrored those of SIEX, but they have been applied with greater speed and flexibility. This ministry has clear priorities, in contrast to the Finance Ministry and its treatment of problems with the foreign debt structure.

D. *Rules for Bidding and Performing Construction Contracts*

Past experiences with large infrastructure and industrial processing plant construction, and the extraordinary quantity of such projects anticipated throughout this century, caused the Government in 1977 to issue a decree containing "General Conditions of Contract for the Execution of Work Projects Entered into by (any Ministry or State-owned entity)."¹³⁵ These general conditions must be incorporated into all contracts for public agencies.¹³⁶ By specific agreement, some of the provisions contained therein may be inapplicable and other provisions ("special conditions") may be added. The usual qualifications documents must be submitted and approved. Furthermore, a certificate issued by the Contractor's Registry must accompany the contract docu-

133. Such Government projects include power plants, transmission facilities, petroleum refineries (or expansions or upgrades thereon), petrochemical plants, steelmaking or processing facilities or similar work related to the aluminum expansions, Caracas metro, hydroelectric projects, and port expansion.

134. Decree 1225, Oct. 21, 1975.

135. Decree 2189, GACETA OFICIAL EXTRA. No. 2089, Sept. 28, 1977.

136. *Id.* art. 1. In addition to the General Conditions, relevant provisions of the Civil Code and special statutes concerning labor, architects, engineers, arms, and explosives are also applicable.

ment¹³⁷ before final approval by the government entity and the Controller General. The decree requires the contractor to appoint a resident engineer (who shall be a member of the relevant professional society) and the Government to appoint an Inspection Engineer, who is the equivalent of an owner's architect, to coordinate with the resident engineer to assure sound execution of the job.¹³⁸ The decree contains provisions for payment (including advance payments, posting, and revision of bonds; formulas for approvals; and payments for overruns and extras), termination for convenience or default, obligations of both parties, guarantees and penalties, and inspection and acceptance. In view of the extensive litigation, construction contractors should be aware of the ten-year subsurface conditions guarantee required by the Civil Code.^{138.1}

IV. OUTLOOK FOR FOREIGN CAPITAL AND TECHNOLOGY

A. *National Development Plan (VI NDP)*

Since 1960, Venezuela has prepared national development plans under the direction of a special organization established for this purpose—the Central Office of Coordination and Planning (CORDIPLAN). The National Development Plan for the period from 1981 to 1985 is the sixth such plan. Its principal goals are to: (1) restructure and control public sector imports; (2) discourage import of luxury items by the private sector; (3) encourage non-traditional exports in order to increase productivity; (4) improve the structure of the national debt, using external financing only for projects of proven profitability that would not further aggravate the debt service burden; (5) totally or partially refinance the external debt; and (6) encourage domestic savings. The primary object of this plan is to improve the “quality and conditions of the lives of all Venezuelans, particularly those suffering from acute poverty.” The Plan also emphasizes development in the areas of agriculture, petroleum, petrochemicals, steel, social services, education, housing, electricity, water and sewage, transportation, and communications.

137. Also to be included are the General and Special Conditions, plans, specifications, project estimate or budget correlated to the schedule, and the necessary guarantees.

138. Decree 2189, GACETA OFICIAL EXTRA. No. 2089, Sept. 28, 1977.

138.1 VENEZUELAN CIVIL CODE, art. 1637.

The principal tools to implement the Plan are monetary and fiscal policies. The flexible use of national planning and the improved management and control of the public sector's external debt are the major elements of this effort. In addition, the Plan emphasizes development of Venezuela's human resources through improved education and training programs, and the development of greater social infrastructure in the form of housing and public services, particularly for the urban and rural poor. Complete implementation will require Venezuela to surmount two major obstacles. First, the Plan's duration exceeds the present administration's term of office. If an AD candidate¹³⁹ were to win the 1983 election, there is a possibility that the COPEI¹⁴⁰ party's program could be substantially altered. Second, the Plan was based on a twelve percent annual increase in the price of oil, and it was expressly assumed that oil revenues account for seventy-six percent of Venezuela's total income during the life of the Plan. The 1981 oil price reductions and consequent revised projections would appear to jeopardize the financial strategy and the accomplishment of the Plan's objectives.

B. *Major Energy Projects in the 1980s and 1990s*

In order to reach the goals set forth in the Plan, the Government is prepared to initiate new extraordinary energy projects and complete large-scale industrial projects, begun during previous years, in the oil, aluminum, iron, steel, and hydroelectric industries.

1. Orinoco Oil Development

The development of Orinoco heavy crude located in eastern Venezuela is perhaps the Government's largest and most important project. Maximization of the recovery and the upgrading of these viscous crudes represents the main challenge in the development of the Belt. Field and laboratory experiments to determine the most suitable technologies for producing and upgrading these heavy crudes are underway.¹⁴¹ The Venezuelan Energy Min-

139. Accion Democratica is the party of the late Romulo Betancourt and Carlos Andres Perez, now out of office.

140. The COPEI party is the Social Christian Party of Luis Herrera Campins, now in office.

141. See Rodriguez Eraso, *supra* note 2.

ister has stated that "if Venezuela were to wait until 1988 to start the Orinoco project, Venezuela would no longer be a net oil exporter."¹⁴² Shortly after the release of this statement Venezuela awarded the first major contract in the Orinoco Belt to a United States contracting firm.¹⁴³ The first refining module to be built by this firm will upgrade the quality of the oil to twenty-eight degrees API using carbon reduction techniques, and it should be in production by 1988. Two or three more modules will probably be added by the end of the century.

Additional projects in the Orinoco region are currently being evaluated by PDVSA. Subsidiaries of PDVSA and numerous international firms have already established research offices and have brought skilled technicians to Venezuela in order to evaluate developments in this region. Meneven and Maraven are both actively pursuing projects in the Orinoco. Meneven is planning to spend Bs. nine billion by 1988 in order to produce 75,000 barrels per day from its wells in Anzoategui State. It will not upgrade this oil, but the oil will be mixed with a lower gravity crude to produce a blend acceptable to major world refineries. Maraven will begin drilling 200 wells in Anzoategui and Guarico States at a cost of Bs. 950 million. It is anticipated that these wells will contain the lightest crudes in the Orinoco heavy oil Belt (approximately twenty degrees API); however, since the oil is deeper in the ground, it will be more expensive to extract.

A three billion dollar program to modernize Venezuela's refining capacity is already well underway. The project will substantially change the existing plants in order to achieve greater flexibility in production yields and increase the output of lighter end-products while augmenting the ability to process a higher input of heavy crudes.¹⁴⁴ Once these refinery projects near completion, Venezuela will be able to process 350,000 barrels of additional heavy crudes each day.

2. Aluminum/Bauxite

Although Venezuela's major bauxite resources were only recently discovered, the Caroni power resource has transformed

142. LATIN AMERICAN WEEKLY REPORTS, Apr. 3, 1981.

143. The contract was awarded to the Lummus Company, a subsidiary of Combustion Engineering, Inc. See *U.S. Company in Big Venezuela Oil Accord*, N.Y. Times, Mar. 28, 1981, at 32, col. 1-4.

144. See Rodriguez Eraso, *supra* note 2.

Venezuela into a substantial aluminum producer. Caroni Aluminum (Aluminio del Caroni—ALCASA) was established in 1967 as a joint venture between Reynolds Metals Co. and CVG. The annual capacity of this plant is expected to expand from 90,000 tons to 124,000 tons. One-half of this quantity will be for export, since Venezuela has been self-sufficient in aluminum production since 1970. Since the recent bauxite discoveries, there has been greater emphasis placed on integration of the bauxite-alumina-aluminum complex. CVG also has an eighty percent interest in VENALUM, a joint venture project with a Japanese consortium. The VENALUM joint venture is expected to have an annual capacity of 280 billion tons by the end of the year. Before the close of this decade, VENALUM anticipates the completed construction of one of the world's largest aluminum smelters which would increase the national aluminum production capacity to 400,000 tons.

3. Iron and Steel

The Zulia steel project is a joint venture which is fifty-one percent owned by Corporacion del Zulia (Corpozulia) and forty-nine percent foreign owned. It was projected that by 1990, five million tons of steel would be produced by this mill. This project has been delayed by the Herrera administration's deflation and readjustment program, and it is likely that the mill will be considerably smaller. Yet a smaller mill would be more realistic in light of Venezuelan market factors. The Government intends to increase significantly both public and foreign investment in the mining sector during the next five years in an effort to increase iron ore production to a level sufficient to meet the anticipated growth in the country's steel-making capacity. It is likely, however, that the Zulia steel project will be slowed down and, instead, the large coal resources will be developed in a program called the Chemical Coal-Zulia Development.¹⁴⁵

4. Hydroelectric Power

The percentage of electricity generated by hydroelectric power will increase significantly as the Guri Dam facilities in the Guyana region on the lower Caroni River are expanded. The Guri Dam project has entered its second phase, which calls for the

145. See Hoet-Linares, *supra* note 62.

completion of ten additional power units by the end of 1987. The Government also expects to begin constructing two additional Caroni River dams in 1983.

C. *Projected Capital Needs*

A consensus now exists among Venezuela's public and private sectors on the need for foreign capital. This is in sharp contrast to the division between the two sectors over this issue when Venezuela entered ANCOM in 1971. This is due in part to the large projected capital needs of the nation as it seeks to finance its major industrial projects. Furthermore, Venezuelans are aware that foreign capital will be needed to refinance its foreign debt structure.

Over the next ten years Venezuela will need to finance at least thirty billion dollars worth of oil industry projects in 1980 dollars,¹⁴⁶ and it will probably require an additional twenty billion dollars for adjacent infrastructure. Financing will also be required for the completion of the Caracas metro, housing, universities, water and electricity projects, and steel and aluminum expansions. Although the Government will be able to finance approximately seventy-six percent of its petroleum and energy-related projects, the principal financing for the other infrastructure projects will probably come from abroad.

1. Existing Foreign Debt Structure: Fixed and Floating

It is estimated that Venezuela's registered foreign debt, both direct and indirect, reached fourteen billion dollars at the end of 1980.¹⁴⁷ Several Government agencies, however, took advantage of legislation which avoided congressional approval for loans under two years of maturity, thereby incurring an estimated seven billion dollars of additional unregistered public obligations. These were not registered as National Public Debt,¹⁴⁸ and this outstanding obligation is referred to in Venezuela as *deuda flotante* (floating debt), in order to differentiate it from longer term credits registered with the Ministry of Finance. The major portion of this

146. See Financial Times, *supra* note 72.

147. See Amador, Jr., *supra* note 89.

148. The Public Credit Law of 1976, GACETA OFICIAL EXTRA. No. 1,894, Aug. 5, 1976, authorizes the National Executive to raise new capital to finance major projects and to refinance existing debt.

floating debt arose because several agencies entered into investment programs without sufficient cash flow.¹⁴⁹

2. Refinancing and Rationalization

On March 15, 1980, the Government was finally able to determine the approximate size of this floating debt. A study undertaken jointly by a Special Commission appointed by the President and the Directorate of Public Credit of the Ministry of Finance determined that the floating debt¹⁵⁰ of twelve major Government entities was approximately six billion dollars; 4.5 billion dollars of this represented short-term external debt of less than one year. In 1981 legislation was proposed to refinance this short-term debt by permitting a massive refinancing to stretch out 4.3 million dollars in short-term debt and to permit new borrowings to underwrite development projects. This legislation is still pending at the time of this writing.

V. SOME OBSERVATIONS ON DOING BUSINESS IN VENEZUELA

A. *Mixed Attitudes Toward Foreign Investment*

Notwithstanding the apparently favorable attitudes toward foreign investment held by the SIEX acting superintendent¹⁵¹ and the Finance Minister, observers continue to note strong voices against foreign investment. Presidents of the Venezuelan Investment Fund and the Venezuelan Foreign Trade Institute have voiced their opposition toward such foreign presence.¹⁵² Companies considering virgin investment in Venezuela should examine these facts as well as the more favorable aspects of no exchange controls and a favorable currency reserve policy.

B. *Lower Risk Forms of "Investment"*

As an alternative some firms may wish to consider providing only technology at the outset, as do the more traditional "services" companies. This option may involve a management con-

149. See Asheshov, *supra* note 23.

150. This floating debt is comprised of notes for the financing of working capital needs, bridge financing, and notes financing budgetary insufficiencies.

151. See BUS. WEEK, *supra* note 72.

152. VENEZUELA-AMERICAN CHAMBER OF COMMERCE AND INDUSTRY, ECONOMIC REPORT 80-12 (Dec. 1980). See also *Firms in Venezuela Remain Confused by Muddled Policies*, BUS. LATIN AMERICA, Aug. 27, 1980, at 274-75.

tract, a technology license, and a technical assistance agreement. That may include an option to take up to forty-nine percent equity, instead of royalties, thus leaving the firm eventually in a joint venture after having gained some prior experience.

C. *Fading Out and Fading In*

Another important consideration will be whether local firms are able to raise capital to fade in and acquire the interests which foreign companies are required to divest under ANCOM rules. The viability of ANCOM is questionable at this time, but Venezuelan officials continue to suggest that the rules will remain the same, even if the game changes. Current debates over methods to revitalize the economy, while keeping inflation down from record-high 1980 levels, suggest that growth rates may not reach projected levels and the VI NDP will consequently have to be scaled back substantially. Although Venezuela remains an attractive market for foreign investors in the long term, short-term strategies may require fine tuning to avoid overcapacity and early losses.

