RESEARCH MEMO

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Sanctioning and Rebuilding Venezuela

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Introduction

Elliott Abrams, the State Department's special representative for Venezuela, called on Nicolas Maduro "to let the country move forward, to step aside and let the country return to democracy and begin to rebuild its economy." One of the pivotal challenges facing the Trump administration is how to escalate sanctions pressure on Maduro without compromising the potential for an economic recovery following his departure. This research memo provides specific recommendations for addressing both facets of that challenge.

To facilitate a swift and meaningful transition, the United States and its partners should increasingly target the personnel and assets keeping Maduro in power. The first section of this research memo lays out specific measures that can hasten the fall of the current regime.

The recommendations that follow include measures to address the economic challenges likely to arise during transition, designed to ensure that Venezuela is able to rebuild as quickly as possible. To encourage foreign investment, the U.S. should lay out a clear road map for the removal of sanctions as part of a democratic transition – thereby helping investors avoid becoming entangled in legal and regulatory hurdles.

Venezuela's full recovery will take many years. Two decades of pervasive corruption and mismanagement will undoubtedly hinder progress long after Maduro is gone. Sanctions relief must therefore be designed in such a way that empowers the Venezuelan economy to recover as quickly as possible yet prevents former regime cronies, cartels, or other malign actors operating in the country from unduly benefitting from the removal of sanctions.

Sanctions and Economic Measures

Expose the international assets of PdVSA to pressure the company more effectively. While state-owned oil company Petróleos de Venezuela, S.A. (PdVSA) is a sanctioned entity under U.S. law, its holdings and assets are spread around the world, and its true ownership interests are often hidden through layered legal structures. These assets are blocked property. Until they are exposed, however, the Maduro regime may transact through them with unsuspecting parties, earning much-needed revenue abroad, where there is little knowledge of PdVSA's expansive international network. By reviewing public records filed in a number of countries across the world, the U.S. government and its partners can identify where PdVSA has significant holdings, companies, or other property. Firms such as Sayari have compiled much of this data and pieced together these networks already. The State Department, working with the Treasury Department, could conduct outreach to the countries where these assets are held, to create a publicly releasable list of PdVSA assets and warn local companies of the risks of doing business with PdVSA.

The administration should also implement sanctions in a manner that does not cause lasting damage to potential long-term production by PdVSA. For example, it would be a mistake to prohibit the export to Venezuela of diluents necessary to operate oil wells, or to prevent necessary maintenance of upstream facilities and infrastructure. Such restrictions would likely inflict damage that impacted the value proposition for future work in Venezuela.

Comprehensive targeting of the "Palace Economy." The administration should systematically target Maduro's "Palace Economy" – especially the regime leadership's assets parked offshore, which are derived mainly from the oil and narcotics trade. The administration should pursue these assets by means of a track, trace, and forfeiture campaign. It could also target regime *testaferros*, or strawmen, who have thus far escaped sanctions but play an important role in helping the regime and its cronies raise and move money. Targets could include Wilmer Ruperti and Danilo Diazgranados, among others.

In addition, the administration should consider listing the Maduro government as a state sponsor of terrorism for its willingness to let the terrorist group Hezbollah operate freely within its borders. Doing so would allow authorities from the Justice Department to seize additional assets tied to individuals, entities, and regimes engaged in sponsoring terrorism or narco-terrorism.

Venezuela is also one of the largest transit points for cocaine and heroin flowing into the United States. The administration should expand its efforts to indict, extradite, and prosecute individuals in the Maduro regime for narco-trafficking and violations of the RICO anti-racketeering law. DOJ has already indicted top Venezuelan leaders, including Minister of Industries and National Production and former Vice President Tareck El-Aissami and former Minister of Intelligence Hugo Carvajal. DOJ may have other indictments under seal. The continued rollout of indictments and their successful prosecution would dramatically aid in pursuing regime assets worldwide and provide the basis to charge accessories to RICO predicate crimes. DOJ could also establish a rewards-for-justice program, paying cash for information leading to the capture of senior-level Venezuelan officials indicted by DOJ.

Impose additional sanctions restrictions on Rosneft. Rosneft – the Russian energy giant subject to U.S. sectoral sanctions following Russia's annexation of Crimea and destabilizing activities in eastern Ukraine – continues to operate in the Venezuelan oil sector, with PdVSA reportedly asking at least two of its clients to make payments for Venezuelan oil via Rosneft. Rosneft has reportedly invested around $9 billion in Venezuelan projects since 2010. The secretary of the treasury, in consultation with the secretary of state, determined on January 28, 2019, that persons operating in the oil sector of Venezuela may be subject to sanctions. While the U.S. should not go as far as to designate Rosneft as a Specially Designated National, or SDN, the administration should impose additional restrictions on U.S. persons doing certain business with Rosneft, in order to penalize and unwind the company's activity in Venezuela. Likewise, as it has done with Cuban entities, the U.S. should continue targeting Maduro regime supporters in Turkey, China, and Russia.

Appoint a central authority to coordinate sanctions implementation, relief, licenses, and public-sector engagement. The administration should consider the temporary appointment of a senior official responsible for coordinating sanctions and subsequent sanctions relief with the private sector, the interagency, the Guaido government, and other governments and international organizations. Rather than assigning this responsibility to the special representative for Venezuela or relying on existing interagency processes, the administration should consider appointing a singular, authoritative point of contact. This person could work within the Office of the Special Representative but could be a Treasury Department detailee with extensive knowledge of U.S. sanctions laws and regulations. In effect, he or she would be a deputy special representative for sanctions and economic pressure and should have commensurate staff support. While the State Department Basic Authorities Act and the Foreign Assistance Act largely provide the authorities needed to implement this recommendation, the special representative may also consider specialized contracting (5 USC 3161) or temporary excepted service positions (Schedule A).

Work with the Lima Group and the OAS to place more international pressure on Maduro. The U.S. should call on the Lima Group and the Organization of American States (OAS) to help ramp up pressure on the Maduro regime. To date, these two organizations have chastised the Maduro regime and supported the restoration of democracy in Venezuela. They should be pressed to do more, including advocating for an International Criminal Court (ICC) indictment of Maduro and his senior leadership for their crimes against the people of Venezuela. Such an indictment could draw from the recent "Report of the United Nations High Commissioner for Human Rights on the situation of Human rights in the Bolivarian Republic of Venezuela." Such a move, initiated by regional actors, would emphasize the illegitimacy of the Maduro regime and the need to restore democracy to the country.

Post-Maduro Transitional Measures

Establish and announce delisting and licensing processes. On January 28, 2019, OFAC designated PdVSA as an SDN, noting that sanctions will remain until control of the company is transferred to the interim president or a new, democratically elected government. Since the energy sector will be the central component of any effort to stabilize Venezuela economically following a transition, the administration should lay out detailed criteria for delisting PdVSA. It should also establish a public, transparent process for the private sector with respect to permissible transactions in the event of a transition, to include clear instructions for companies dealing with U.S. banks. Concurrently, the administration should consider working with the Guaido government to revamp the boards of other key Venezuelan companies in industries such as gold and mining, thereby creating shadow corporate structures that could quickly and easily be put into place in the event of a government transition. The administration has already done so with PdVSA and its U.S. subsidiary, Citgo.

Developing public-private partnerships prior to transition. The widespread corruption and financial crime in Venezuela may create barriers for the re-entry of foreign firms into Venezuelan markets. To address this issue, the administration should consider establishing public-private partnerships (PPPs) between U.S. authorities, Guaido government officials, and financial institutions or businesses in the energy sector and associated sectors, with the purpose of identifying and disrupting corruption and financial crime.

Pre-transition engagement with the Commerce Department's Bureau of Industry and Security on Control List Items. Consistent with the public messaging recommended above on delisting and licensing, the Commerce Department should engage with the private sector to identify export-controlled goods on the Commerce Department's Commerce Control List (CCL) and to provide fast-track licensing for those goods. This effort will be particularly important in stabilizing the Venezuelan oil sector after transition.

Public engagement on terminating executive orders and exercising waivers. The administration should consider describing precisely which executive orders would be terminated following a transition in Venezuela, such as Executive Orders 13692, 13850, 13808, 13827, and 13835. Concurrently, the administration should draft waivers that suspend prohibitions on certain kinds of assistance as a means to jumpstart initiatives related to the energy and financial sectors. The relevant statutes include but are not limited to Trafficking in Persons Sanctions, codified in 22 U.S.C. 7107, international narcotics control legislation (whose current national interest waiver specifically for democracy promotion programs may need to be broadened to allow for the Overseas Private Investment Corporation [OPIC] and the United States Agency for International Development [USAID] to operate), and the Venezuela Defense of Human Rights and Civil Society Act.

Expand global donations to Venezuelan aid groups by establishing a formal cryptocurrency charity channel. In a post-Maduro Venezuela, the U.S. could encourage anti-money laundering/combating the financing of terrorism (AML/CFT)-compliant cryptocurrency exchanges to set up donation accounts for Venezuelan aid. During transition, former regime elements may try to siphon funds or goods from the country. Using AML/CFT-compliant cryptocurrency exchanges is one way to safely deliver funds to the country while limiting certain corruption risks. Cryptocurrency wallets could be earmarked for specific types of aid, with flows to local NGOs on a public blockchain to ensure transparency and accountability. Given cryptocurrencies' price volatility, the NGO wallets could hold so-called "stablecoins." Alternatively, the NGOs could transfer digital coins into local currency (or a more stable currency) as quickly as possible. Aid authorities should study cryptocurrency blockchain transaction data to compare its cost savings, efficiencies, and other benefits with those of conventional fund transfers.

Jumpstart commerce by helping local businesses use cryptocurrency wallets. Because the Venezuelan financial system will likely remain weak for some time even after the Maduro regime, the Venezuelan business sector should be encouraged to participate in a pilot program that leverages cryptocurrency payments to expand the provision of goods and services. The program should involve digital wallets for which users must undergo stringent AML and Know Your Customer (KYC) procedures and comply with FATF recommendations for virtual assets, including by capturing originator and beneficiary information for all transfers. Reputable cryptocurrency firms with demonstrated AML/CFT compliance systems should be encouraged to help build this pilot program and provide the necessary software and hardware to allow more Venezuelan enterprises – from large corporations to small food stands – to receive cryptocurrency transactions. The Financial Crimes Enforcement Network (FinCEN) should work closely with Venezuela's financial intelligence unit to help monitor this pilot program, which could help increase access to alternative payments while the conventional financial system is gradually re-established.

There are certainly other measures that the U.S. government can consider taking to ensure stability and growth in a post-Maduro Venezuela. But the key is to begin planning now. With the help of smart pressure, this planning will hopefully pay significant dividends for the people of Venezuela following Maduro's disastrous rule.