

# INTER-AMERICAN DIALOGUE'S

## LATIN AMERICA ADVISOR ► ENERGY

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### FEATURED Q&A

#### Will Major Oil Companies Invest Significantly in Venezuela?

**Q** According to press reports earlier this month, major oil companies—including Chevron, Shell, and Petrobras—spent \$2 million apiece for technical data on deposits in Venezuela's Orinoco Belt following the country's invitation to bid on minority stakes in projects with state-owned PDVSA, which faces diminishing returns due to the downturn in oil prices. Will these companies invest significantly in a Venezuela ruled by Hugo Chavez? How will the risks and benefits of such an investment be measured?

**A** **Board Comment: Garrett Soden:** "Yes, these companies will invest in Venezuela, but they will require a higher potential return to do so. The Carabobo bid entails huge integrated projects with three upgraders to be built at a total estimated cost of over \$20 billion. Nineteen companies purchased the data pack, and PDVSA has since received over 1,000 questions from interested parties. The first reason for the strong interest is the area's low-risk geology. Some companies prefer to take perceived political risk rather than exploration risk. These reserves carry very little geological and operational risk (compared to Brazil's deepwater reserves, for example). A second reason is size: the Carabobo bid is the largest of its kind in the world. PDVSA will continue to hold a majority 60 percent equity interest and operational

control, but private companies will gain access to a significant amount of reserves—an estimated 15 billion barrels of oil in each of the seven blocks being offered. Third, major oil companies have limited alternatives. The few countries with comparable reserves are not open to private investment (Saudi Arabia, Mexico) or come with similar political or worse security risks than Venezuela (Iraq, Nigeria). Fourth, major oil companies

*Q&A continued on page 3*



#### Morales Nationalizes Nation's Fourth-Largest Gas Producer

Bolivian President Evo Morales on Friday announced the nationalization of Chaco, a subsidiary of BP-owned Pan American Energy and the country's fourth-largest producer of natural gas. See story on page 2.

*Photo: ABI.*

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## ENERGY SECTOR BRIEFS

**Cuba Revokes Shared Contract With Pebercan and Sherritt**

Cuban national oil company **Cupet** on Friday revoked a production-sharing contract on an oil block with a subsidiary of Montreal-based **Pebercan**, reported Reuters. Cupet will pay the company \$140 million for its share in the project, approximately \$60 million of which will go to Pebercan's partner in Block 7, Canadian oil company **Sherritt**. In a press release on Monday, Sherritt said Block 7 accounts for 26 percent of the company's Cuba production but that the termination would not affect its other wholly owned projects. Sherritt on Tuesday announced Chief Executive Officer Jowdat Waheed was stepping down for a family health matter and would be replaced by Chairman of the Board of Directors Ian W. Delaney.

**Mexico's Calderon Scheduled to Meet With IOCs at Davos Forum**

Mexican President Felipe Calderon said Wednesday that he would meet with leaders of international oil companies at the World Economic Forum in Davos, Switzerland, reported Bloomberg News. Mexico is preparing to offer exploration contracts to foreign companies for the first time in 70 years under the auspices of last October's energy reform. Calderon did not specify which oil companies he would meet with.

**Chavez Says OPEC Could Further Cut Oil Production**

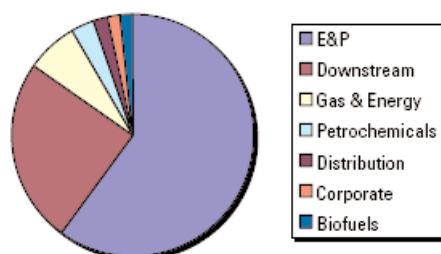
Venezuelan President Hugo Chavez said Monday he would support OPEC if it decides to further cut oil production in order to lift sagging oil prices. Chavez said OPEC could reduce production by up to 4 million bpd in addition to the 4.2 million bpd it cut since September.

**Oil & Gas News****Petrobras Unveils Five-Year \$174 Billion Investment Plan**

Brazilian national oil company **Petrobras** on Monday said it will invest \$174.4 billion by 2013, some \$62 billion more than the amount projected in the company's previous plans. Most of the investments will be earmarked for exploration and production, at \$104.6 billion (see chart). A total of \$28.6 billion is expected to be invested in 2009, the company said. The plan aims to maintain 1 million jobs in Brazil, and is expected to contribute some 10 percent of Brazil's GDP. Petrobras intends to build 28 drilling rigs in Brazil, the first seven of which are expected to be delivered between 2013 and 2017. Speculation had surfaced in recent months that lower oil prices would hurt Petrobras' cash flow and ability to make long term investments. Company director Almir Barbassa said the company's cash

Petrobras:

\$174.4 Billion in Investments through 2013



Source: Petrobras.

generation in the next five years is expected to range from \$120 billion to \$150 billion. "The two first years will be the most challenging, but we are in a very comfortable scenario," he said. Barbassa added that Petrobras would cut up to \$4 billion in costs each year in order to hold the line on debt. Resources have already been secured for the 2009 investments, with \$11.8 billion in funds from state development bank BNDES. Barbassa said \$5 billion will come from international banks, which will involve operations in the capitals market with the issuing of debentures in the upcoming years, he added. Internationally, Petrobras will invest \$15.9 billion during the next five years. The US

will receive the biggest volume of investments, at 28 percent of the total, trailed by Argentina (16 percent), Peru (5 percent), and Chile (3 percent), with African countries Nigeria (12 percent) and Angola (5 percent) also garnering investment.

**Bolivia Nationalizes Pan American Energy Subsidiary Chaco**

The Bolivian government last Friday nationalized energy company **Empresa Petrolera Chaco**, which it seized from **Pan American Energy**, reported Reuters. President Evo Morales announced the move at a Chaco national gas field in Cochabamba. "With this decree today, we nationalize all the shares of oil company Chaco. [The shares belong] to Bolivians now," Morales said. Last year, Morales attempted to take control of Chaco by ordering Pan American Energy to transfer its stake in the company to Bolivia's state oil firm **YPFB**. However, discussions over Morales' order broke down, leading to Friday's seizure. In a statement, Pan American Energy, which is controlled by **BP**, said it would "continue its efforts to align its legitimate interests—that it will defend at all levels—with the objectives and interests of the Republic of Bolivia." Morales nationalized the country's energy industry in 2006. The move forced energy companies including Brazil's **Petrobras** and Spain's **Repsol YPF** to pay higher taxes. In reserve terms, Chaco is Bolivia's fourth-largest natural gas producer, controlling 4.9 percent of the country's natural gas deposits, according to a 2005 audit cited by Reuters.

**PDVSA Unit Seizes Control of Ensco Rig After Payment Dispute**

Dallas-based **Ensco International** announced Thursday that **Petrosucre**, a subsidiary of the Venezuelan national oil company **PDVSA**, has assumed control of its drilling operations in Venezuela in "an ongoing dispute over Petrosucre's non-payment of past due invoices" on a contract for the ENSCO 69 jackup drilling rig, the company said in a press release. "When Petrosucre failed to honor recent commitments to pay past due amounts, Ensco suspended drilling operations upon comple-

tion of the well in progress pending payment," the company said. For its part, Petrosucre views Enco's stoppage of



Rabun

File Photo: Enco.

operations as an "abandonment of their contractual responsibilities," PDVSA said in its own press release issued Wednesday. Although Enco has been told it is free to terminate the contract and remove the rig, senior representatives of Enco and Petrosucre are currently engaged in discussions, Enco said. Dan Rabun, Chairman, President and Chief Executive Officer of Enco, said he was "hopeful" that the situation "soon can be resolved to the mutual satisfaction of Petrosucre and Enco." Enco says its total receivable balance with Petrosucre is approximately \$35.5 million and that the rig is insured for \$65 million. Lower oil prices, which have fallen by more than half since peaks last summer, have put pressure on some producers. PDVSA accounts payable climbed 39 percent, or \$2.21 billion, to \$7.86 billion at the end of September from the end of December, according to Bloomberg News.

## Featured Q&A

*Continued from page 1*

have a long-term perspective. While oil prices have decreased dramatically since last summer's peak, these projects will take many years to develop and will be based on oil price expectations over the next 25 years. The global supply-demand situation favors higher oil prices in the long-term. Finally, the recent decline in oil prices increases the bargaining power of the Western oil companies in the bid process. Of course, terms may eventually change as oil price volatility increases, but this is a risk companies face in every country. Furthermore, Venezuela's favored NOC partners do not have the required technology or financing capabilities of the IOCs like Chevron and Shell. The bids will ultimately depend on investor sentiment regarding contract sanctity, international arbitration rights and how the economics work with projected recovery factors, oil prices and the royalty/fiscal regime. The recent forced migration of the private oil and gas investments in Venezuela to PDVSA joint ventures and the subsequent nationalizations of other sectors in Venezuela may give investors pause. In addition, the

tightening global capital markets will make it difficult to finance these projects. Nevertheless, companies are interested."

**A Board Comment: Ramon Espinasa:** "The interest shown by a good number of the major oil companies, albeit with conspicuous absentees, just goes to show how attractive resource-rich Venezuela is in a reserve-thirsty oil scenario. A number of hurdles lay ahead for these joint ventures to be completed. The bidding is for the production and upgrading of the Orinoco heavy crudes, which are both very capital-intensive and technologically complex projects. Furthermore, all the investment is to be made up front and the capital recovery period is long term. All of this will make for a very complex contracting process. The main difficulty will stem from the fact that by constitutional rule, PDVSA will have to retain a majority stake and control of the projects. This raises a number of questions. Will PDVSA be able to finance its share of the projects? Will the company be able to assemble the manpower to carry these

*Continued on page 6*

## Power Sector News

### Chilean Electricity Companies' Profits Surge in 2008

Profits of Chile's leading electricity companies surged last year, reported Reuters on Wednesday. Generator **Endesa Chile's** profits doubled in 2008 to more than 442 billion pesos (\$US 704 million) while profits of its parent company, Chile-based **Enersis**, the Latin American unit of Spain's **Endesa**, nearly tripled to almost 571 billion pesos (\$907 million). Power generators and distributors saw profits soar elsewhere in the region, including in Brazil, Colombia and Peru, due to more electricity sales and higher prices. **Chilectra**, a unit of Enersis and Chile's number one electricity distributor, reported its net profits rose 93.5 percent in 2008. The company said costs also

increased because of the higher prices it paid to electricity generators. **Colbun**, Chile's second-largest distributor, earned a net profit of 28.83 billion pesos (\$US 37.9 million) in 2008 after posting a loss of 50.92 billion pesos the previous year. Bernardo Larrain, Colbun's chief executive, told reporters last week he believes the energy sector is the only one that, despite the crisis, will maintain "a relevant level of investments" in Chile. Colbun is moving ahead with a planned \$1 billion investment in two new hydroelectric plants, according to Reuters.

### Argentina: No Lights Out for Clients Who Can't Afford Rate Hikes

An Argentine judge on Tuesday ruled that local electricity distributors cannot cut off service to customers who are unable to afford a new rate increase, reported local daily *Clarín*. The ruling by judge Cecilia

De Negre prohibits distributors **Edenor**, **Edesur** and **Edelap** from "implementing electricity cuts due to the failure to pay bills" on accounts affected by the rate increase, which applies to customers who consume in excess of 1,000 kilowatts every two months. The electricity distributors say the judge's ruling only protects those who don't pay the amount of the increase, and that customers still need to pay a portion of their power bill to avoid losing electricity. Argentina's ombudsman's office, which is challenging the rate increases in court, said Wednesday it believes De Negre's judgment applies to the entire bill and not just the increase, but that it's best for customers to go ahead and pay based on the old tariff structure. "We're telling customers to pay the bill, but without the increase, because the judge has not yet resolved our petition to roll back increases," Ombudsman Eduardo Mondino said, reported local

daily *La Nacion*. Mondino has called the increase "illegal" and "unreasonable" because it could raise bills by up to 300 percent. The current ruling will hold until a final decision is made regarding Mondino's challenge to the law's legality, De Negre said. Last year, the Argentine government announced it would cut subsidies for electricity and allow a rate increase for the first time in seven years due to the rising cost of generating energy.



Mondino

File Photo: Office of Nat'l Ombudsman.

In October, Argentine Planning Minister Julio de Vido said higher rates would affect only 750,000 residential customers, representing 8.5 percent of the total, in addition to 14 percent of businesses and 2 percent of industrial customers.

## Biofuels News

### Argentina's Ledesma to Invest \$19 Million in New Biofuels Plant

Argentine sugar producer **Ledesma** announced last Friday it will invest 65 million pesos (US\$19 million) for the installation of a new biofuels plant in the northern part of the country, Spanish news agency EFE reported. The company, which has 35,000 hectares of sugar cane plantations in Jujuy province, will increase its area of cane cultivation by about 4,000 hectares and install a plant to produce fuel alcohol, Ledesma said in a filing with the Buenos Aires stock exchange. The company indicated that it will also make investments in its current distillery, which aims to produce about 55 million liters of alcohol in 2010 to target the domestic market for hydrated alcohol and new ethanol markets, according to the report. Although Ledesma has traditionally focused on agricultural products, it has recently taken a 4 percent stake in exploration and production in the Aguarague natural gas deposit in Argentina's northern Salta province.

## The Dialogue Continues

### What is the Caribbean's Biofuels Potential?

**Q** The Jamaican government and Brazilian firm Infinity Bio-Energy failed to reach a deal for the company to take control of Jamaica's state-owned sugar plantations by the December 31 deadline, although the company said it hopes to raise the money to fund the takeover by the end of this month. What is the potential of biofuels production in Jamaica and other islands in the historically sugar-rich Caribbean, both for export and domestic electricity generation? Can the region become a viable destination for Brazilian and other foreign capital related to biofuels development?

**A** Guest Comment: **José Goldemberg:** "Most of the Caribbean countries have extensive sugarcane plantations used presently for sugar production. It would not be a big deal to divert some of this production to ethanol production and replace 10 percent of the gasoline used in these countries. An important driving force for bioethanol production in the Caribbean countries is the revision of the sugarcane regime by the European Union within the Common Agricultural Policy, which will reduce price support by 36 percent in

four years. Some countries, such as Barbados, Belize, Jamaica and Guyana, are considering converting the sugar they produce into ethanol as a way to respond to both the new sugarcane regime and the increase in their fossil fuels bill. Jamaica is the most developed country in this regard, since it intends to implement the 10 percent mandatory bioethanol blend. In addition to supplying their internal fuel markets, which in general are limited, Caribbean countries are also interested in the possibility of exporting bio-ethanol, especially to the United States. Under the Caribbean Basin Initiative established by the US Congress in 1983 these countries can export ethanol to the US free of taxation. Brazil has been using this channel to export several billion liters per year to the US via Caribbean countries."

**José Goldemberg** is Professor of Physics at the University of Sao Paulo and a former Secretary of the Environment of the State of Sao Paulo.

*Editor's note: the above is a continuation of a Q&A published in the January 19-23, 2009 issue of the Energy Advisor.*

## Political News

### In Referendum, Bolivians Approve New Constitution

Bolivians on Sunday approved President Evo Morales' new constitution, which includes measures aimed at empowering the country's indigenous majority, the Associated Press reported. The unofficial count registered 59 percent support for the new constitution and 41 percent against it. "Here begins the new Bolivia," Morales told a crowd in front of the presidential palace in La Paz after the results were announced. Currently, presidents

can serve two non-consecutive terms. However the new constitution will allow them to serve two consecutive terms, paving the way for Morales to stay in office until 2014 if he wins re-election. The new constitution will also give self-rule to indigenous groups in their traditional lands and will allocate seats in Bolivia's Congress for minority indigenous groups. In a departure from the current constitution, the Roman Catholic Church is not mentioned, but the document does refer to the Christian God and the Andean Pachamama. Freedom of religion is guaranteed as is freedom of the press. However, the press under the new constitution is required to "respect the

principles of truth and responsibility." Early returns from Sunday's voting also showed support for an additional item limiting land ownership in Bolivia to 5,000 hectares (12,400 acres). Current landowners are exempt from the restriction.

### Colombia Says FARC Responsible for Deadly Explosion in Bogota

Colombian authorities blamed the Revolutionary Armed Forces of Colombia (FARC) for a bombing that killed two people Tuesday night in Bogota, Bloomberg News reported Wednesday. The blast, outside a **Blockbuster** video rental store in a wealthy section of the capital, also injured 20 people. "We condemn in all possible ways such an act of cowardice," Defense Minister Juan Manuel Santos said in a written statement. "Terrorism only causes damage to innocent people like the two victims who were killed." The government has offered a reward of as much as 100 million pesos (\$US 43,000) for information that leads to the arrest of the perpetrators. The bombing was most likely related to extortion, said Santos. Colombian authorities have pledged to increase security in Bogota and will create a new task force made up of police, military and intelligence officials to investigate extortion and terrorism in the city, said Santos. He added that Bogota Mayor Samuel Moreno will participate in a special meeting in order to review security in the capital. The explosion happened after a battery-operated device detonated up to 22 pounds of explosives that were placed in a backpack that had been planted in a cash machine adjacent to the video store.

## Economic News

### Argentine President Declares Agricultural Emergency

In response to the most severe drought in decades, Argentine President Cristina Fernandez on Monday declared an agricultural emergency, which will exempt farmers from paying some taxes for up to a year, the Associated Press reported. Farmers pressed for the relief in the wake

of a drought that analysts estimate could cause losses totaling \$5 billion this year. In a televised speech, Fernandez said the exemptions could cover thousands of farmers. The drought, the country's worst since at least 1971, has killed crops and livestock in the provinces of Buenos Aires, Entre Rios, Santa Fe, La Pampa, Cordoba, Chaco and Santiago del Estero. In order to be exempt from paying some taxes, agricultural producers must have lost at least half of their crops or livestock. In July, Argentina's farmers' organizations held protests for four months to urge the government to roll back a tax increase on exports. Eduardo Buzzi, the leader of the Argentine Agrarian Federation, lauded the emergency declaration but said more is needed. "What's at stake is much more than a harvest," he said, adding farmers are facing "desolation and uncertainty." [Editor's note: see related Q&A in the January 29, 2009 [issue](#) of the daily *Advisor*.]

### Crisis Could Cost 2.4 Million Latin Americans Their Jobs This Year

The global economic crisis could cost as many as 2.4 million Latin Americans their jobs this year, the International Labor Organization (ILO) said Tuesday, according to the Associated Press. Last year, urban unemployment fell to 7.4 percent from 8.1 percent, the group said. However, the crisis is expected to reverse that trend. This year, unemployment in Latin America is expected to rise to an average of between 7.9 percent and 8.3 percent. It would be the first increase in the unemployment rate since 2003. "We are talking about between 1.5 and 2.4 million jobs that could be lost this year," said the ILO statement. Latin American governments provided the data that formed the basis of the report. Last year's unemployment rate, the lowest since 1992, is equivalent to 15.7 million people. The Dominican Republic and Uruguay saw the largest drops in the unemployment rate, while Peru experienced the smallest decline. The report says the global financial crisis began affecting Latin America in the third quarter of last year, with lower demand for exports, lower raw materials prices, falling remittances and less-available credit.

## POLITICAL & ECONOMIC BRIEFS

### Bolivian Minister Sees Warming in Relations With US

Bolivian Foreign Minister David Choquehuanca said Wednesday his country hopes to exchange ambassadors soon with US, reported the Associated Press. Choquehuanca said the Obama Administration congratulated Bolivia on carrying out a successful referendum vote last Sunday, a move which he called a "good sign." Bolivia and Venezuela expelled US ambassadors in September, but Venezuela has said the US "will probably have wait some time" to re-establish its ambassador in Caracas."

### Latin Americans Who Lost Money With Madoff Sue Santander

Investors in Latin America who lost money in connection with **Banco Santander's** investments with Bernard Madoff have filed suit in Miami, claiming that the bank did not adequately carry out due diligence to guard against losses, Bloomberg News reported Tuesday. The lawsuit was filed in the Florida Southern District Court on behalf of Talcahuano, Chile's **Inversiones Mar Octava Limitada**, which suffered \$300,000 in losses in connection with the Madoff-related investments. The other plaintiff in the suit is Argentine resident Marcelo Guillermo Testa, whom the lawsuit says lost "all, or substantially all" of his investment.

### Obama, Uribe Discuss Bilateral Relations During Phone Call

US President Barack Obama and Colombian President Alvaro Uribe spoke for about 10 minutes by phone Tuesday to discuss bilateral relations, the Associated Press reported. An Uribe spokesman said the call was "constructive and cordial," but declined to share details.

**Featured Q&A***Continued from page 3*

projects forward from engineering to construction and operation? It is well known that PDVSA has been facing cash flow problems, which are only exacerbated by the collapse of crude oil prices. In addition, the disarray of global financial markets denies the possibility of resorting to the international financial community for the time being. Will the winning companies be prepared to finance the projects beyond their own share, increasing exposure and risk? And under what conditions? Will they be prepared to assemble the technical teams to be put under PDVSA management? In this case more than any previous contracting in Venezuela, the devil will be in the details."

**A Guest Comment: Gregory Wilpert:** "The big unknown in any prediction about foreign investment in Venezuela's oil sector is whether the price of oil will rise high enough again to make such investment viable. It is estimated that the price of oil must be in the \$30 to \$40 range for such investments to be profitable at the current Venezuelan tax and royalty rates. Nothing much has changed in the Chavez government's oil policies since 2001, when the new hydrocarbons law was passed via law-decree: all of the nationalizations and tax increases (except for the 'excess profit tax' of early 2008) that were implemented since then have their basis in this law, which does not anticipate any changes in the foreseeable future. The risks and unknowns involved in investing in the Orinoco Oil Belt are thus entirely rooted in the price of oil, not in anything that the Chavez government might do. Despite the current global economic crisis, oil prices are likely to pick up later this year or early next year. The reason for higher prices is because production will continue to drop due to current declines in global oil investment and due to increased economic activity as a result of economic stimulus packages that governments around the world are passing."

**A Guest Comment: Gustavo Coronel:** "Heavy oil resources of the Orinoco area of Venezuela amount to some one trillion barrels of oil in place. If only 20 percent of this oil is recovered we are looking at 200 billion barrels of oil reserves. The technology to upgrade this oil already exists, at the cost of some \$15-20 per barrel. In spite of Hugo Chavez's abuses of power and the recent weakening in oil prices, the companies still consider this project very attractive and will probably invest. Why? First of all, there is a strategic need to establish their presence in an area second in importance only to Saudi Arabia. Second is the long term nature of the project, which will take between six and eight years to develop. By then Chavez should be out of power and oil prices should be back up to \$100 a barrel (a scenario with 65 percent probability). Third, if Chavez remains in power he still would need the companies to do a job that his state-owned company or companies from Iran or China are not capable of doing, due to lack of technology and good management (a scenario with a 25 percent probability). If Hugo Chavez chose to 'nationalize' again, the companies can always resort to international arbitration (a scenario with a 10 percent probability). ExxonMobil and ConocoPhillips will return once Chavez is out."

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**Garrett Soden** is a member of the Energy Advisor board and CFO of PetroFalcon Corp.

**Ramon Espinasa** is a member of the Energy Advisor board and a former Chief Economist of PDVSA.

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**Latin America Energy Advisor**

is published weekly by the  
Inter-American Dialogue, Copyright © 2009

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**Latin America Energy Advisor** is published weekly, with the exception of some major US holidays, by the Inter-American Dialogue 1211 Connecticut Avenue, Suite 510 Washington, DC 20036 Phone: 202-822-9002 Fax: 202-822-9553

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