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FEATURED Q&A

How Will New Tariffs Affect Venezuela's Oil Industry?

Q On April 21, Venezuelan President Hugo Chávez announced drastic changes to windfall oil tax rates, hiking the tax from 60 percent to 95 percent when oil prices surpass \$100 per barrel. The new legislation also raises the taxes to 80 percent when oil prices are between \$70-90 per barrel and 90 percent when prices are between \$90-100 per barrel. The government has since sought to reassure investors, saying that companies will only pay the higher rates after they recoup their original investment. How are the new taxes likely to affect investment in the country's oil sector in the short- and medium-term? How will the taxes affect the development of Venezuela's Orinoco belt? Are Chávez's social spending projects, funded with oil revenues, achieving lasting results?

A Gustavo Coronel, former member of the board of directors of PDVSA: "The new Venezuelan oil tax was to affect all companies producing oil in Venezuela but was rapidly modified to include only Petroleos de Venezuela and its partners in joint ventures, excluding those foreign companies initiating projects in the Orinoco region, any incremental production generated during 2010 and the oil exports to China that are in payment of the Chinese loans. The new tax, therefore, will be applied to about one million barrels per day of oil

production. The big losers are, of course, the state-owned petroleum company and its foreign partners in the joint ventures. The major impact of this new tax will be political, designed to show the government as obtaining maximum benefits for the nation. Hugo Chávez is already campaigning for re-election in December 2012. A second effect will be the loss of autonomy of Petroleos de Venezuela. The new tax intensifies the direct transfer of oil income to the central government, leaving the company with little money for invest-

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Argentina's YPF Makes Second Large-Scale Shale Discovery

Argentina's YPF, a subsidiary of Spain-based Repsol, has discovered the equivalent of 150 million barrels of shale oil in southern Patagonia, YPF Chief Executive Officer Sebastián Eskenazi announced Tuesday. See story on page 2.

File Photo: YPF.

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ENERGY SECTOR BRIEFS

Total Confirms Lower Estimate on Bolivian Gas Find

France's **Total** announced Thursday that the recent natural gas find in Bolivia would initially produce over 500,000 cubic meters per day, a significantly lower figure than the government's estimate of 6.5 million cubic meters per day, Reuters reported. Total had declined to comment on the government's figures, which would have boosted reserves by 30 percent. Bolivian state oil company **YPFB**, Total and Argentina's **Tecpetrol** plan to invest \$1.1 billion over the next nine years in the new Aquio field.

Colombia Will Resend Bill to Sell Ecopetrol Stake

Colombia will withdraw and then resend a bill to Congress which seeks to sell shares of as much as 10 percent in state-run energy company **Ecopetrol**, Bloomberg News reported Monday, citing Finance Minister Juan Carlos Echeverry. The new version will seek to correct procedural problems. Proceeds from the sale will be used to fund reconstruction efforts after last year's devastating rains. Last week, **Ecopetrol** reported soaring profits on rising production, higher prices and surging exports, rising 59 percent in the first quarter from the year prior.

BP Wins Final Approval to Buy Brazil Blocks from Devon Energy

Regulators granted final approval on Tuesday for **BP** to purchase 10 exploration and production blocks in Brazil from **Devon Energy**, the *Financial Times* reported. The deal was announced March 2010 and gives BP assets in the Campos basin, as well as two onshore licenses. BP also acquired majority control in **Brazil's Companhia Nacional de Açúcar e Alcool** last month.

Oil & Gas News**Argentina's YPF Makes Second Large-Scale Shale Discovery**

Argentina's **YPF**, a subsidiary of Spain-based **Repsol**, has discovered the equivalent of 150 million barrels of shale oil in southern Patagonia, YPF Chief Executive Officer Sebastián Eskenazi announced Tuesday. It is the largest find in two decades and the second major discovery in Argentina's Neuquén province. In December, YPF announced a find of 4.5 trillion cubic feet of shale gas nearby. The company plans to drill 17 new wells in the Loma La Lata area and will invest \$270 million this year to develop the shale oil project. Unconventional gas is more com-

The discovery of 150 million barrels of shale oil will bolster YPF's crude reserves by 27 percent and Argentina's reserves by 6 percent.

plex and costly than conventional production to extract. "The important thing about this ... is the fact that this is new energy, a new future with a new expectation," said Eskenazi, Reuters reported. The government said the recent find will boost YPF's crude reserves by 27 percent and Argentina's by 6 percent, a welcome lift to the country's oil sector. According a report recently released by former energy secretaries, oil production sank 18 percent and gas output fell 8 percent since 2003, the *Financial Times* reported. Meanwhile, Argentine oil refinery workers began a nationwide strike on Thursday, the latest in a series of labor protests that threaten the country's energy supply. According to private analysts, inflation is around 25 percent, stoking demands for higher wages. [Editor's note: see related Q&A in the Feb. 14-18 [issue](#) of the *Energy Advisor*]

Brazil to Force Petrobras to Lower Gas Prices, Raise Ethanol Production

The Brazilian government will force state-run oil company **Petrobras'** distribution arm, **BR Distribuidora**, to lower fuel prices by between 6 percent and 10 percent as it seeks to curb inflation, Mines and Energy Minister Edison Lobão said Wednesday, Reuters reported. Once BR cuts prices, the government expects that other fuel distributors will follow suit. The last time Petrobras changed the prices its refineries charge distributors was in mid-2009 when it lowered gasoline prices by 4.5 percent and diesel by 15 percent. Gasoline and ethanol prices have been rising in the past few weeks, further contributing to the booming economy's high inflation rate, which hit 6.51 percent in April. Rising consumer demand and a late sugar cane harvest led to a spike in sugar prices, causing producers to divert production to the sweetener. Brazil has also ordered Petrobras to triple its share of national ethanol production from 5 percent to 15 percent, Lobão said Sunday, the *Financial Times* reported. Brazilian demand for ethanol has led to a jump in imports from the United States—from 1 million liters in 2009 to 70 million liters last year. Ethanol prices have already begun falling as the sugar cane harvest picks up.



Lobão

File Photo: Brazilian Government.

Calderón Vows to Renew Pemex Output, Rejects Share Sale

Mexican President Felipe Calderón said Tuesday that he hopes to achieve a second reform of state-run oil company **Pemex** before the end of his term and added the government has no plans to sell shares in the company, but will focus on selling bonds. In an interview with Bloomberg TV, Calderón said "My plan is to try another legal reform in order to modernize Pemex in a way similar to what Petrobras did 10 years ago." In 2008, Mexico passed legislation to reform Pemex in an effort to boost flagging production

and promote investment. However, many analysts have suggested that the measures were inadequate. "The reforms enacted at



Calderón

File Photo: U.S. Government.

the end of 2008 probably did not go far enough and, alas, they are only just being implemented," David Shields told the *Energy Advisor* in April. Despite recent speculation that the administration planned to sell shares of Pemex, which would be a controversial move in Mexico, Calderón said that the government is focused on selling "citizen bonds." "What we are doing right now is preparing an issue of bonds, we call them citizen bonds, that do not imply shares, don't imply capital of the enterprise." He added that a share sale could be considered in the future. [Editor's note: related Q&A in the April 11-15 [issue](#) of the *Energy Advisor*.]

Power Sector News

Venezuela Rations Electricity After Massive Blackout

Nearly half of Venezuela's territory was affected by massive power outages on Monday and authorities rationed electricity throughout much of the country the following day, Dow Jones reported. The blackouts, which occurred in 11 of the country's 23 states, caused traffic jams and forced brief interruptions for businesses. The outages were mostly corrected within an hour, according to the report. Igor Gavidia, an official from the Energy Ministry, said that rationing took place on Tuesday in all states except for Amazonas, Bolívar, Vargas and the capital, shutting electricity off for three hours to stabilize the electric system. Last month, a fire damaged a power line in Venezuela and

caused the country's worst blackout since 2009. Government officials were adamant that Venezuela is now better equipped than in 2009 and 2010 when electricity shortages crimped the economy during a severe drought. However, industry analysts and business owners claim electricity shortages are hampering production this year, as well. [Editor's note: See related Q&A in the April 25-29 [issue](#) of the *Energy Advisor*.]

Brazilian Senate Approves Tripling Energy Payments to Paraguay

Brazil's Senate has given final approval to an agreement that triples payments to Paraguay for energy from the Itaipú hydroelectric dam, which lies on the border between the countries, BBC News reported Thursday. Under the deal, Brazil's annual payments to Paraguay will increase to \$360 million from their current level of \$120 million. Then-Brazilian President Luiz Inácio Lula da Silva and Paraguayan President Fernando Lugo originally agreed to the deal in 2009. The two countries inaugurated the dam in 1984 and each country has the right to 50 percent of the energy generated. However, Paraguay uses only about 5 percent of its portion and under the terms of the original agreement had to sell its unused share to Brazil at a fixed price. Lugo had argued that the price was too low as compared to

Brazil's annual payments to Paraguay will increase to \$360 million from their current level of \$120 million.

the amount Paraguay could get by selling the energy elsewhere. Brazilians had contended that they paid for the majority of the project and that Paraguay had to contribute its fair share. The deal has critics in Brazil, including Sen. Itamar Franco, who said the measure will force Brazilian consumers to pay more for energy. The vote comes ahead of a visit to Paraguay by Brazilian President Dilma Rousseff, who is due in the country on Sunday.

Chile Approves \$7 Billion Project to Dam Patagonian Rivers

A Chilean government commission concluded a three-year environmental review and granted approval to build five dams on the Baker and Pascua rivers in southern Patagonia, the Associated Press reported. The \$7 billion HidroAysén project, which is a joint venture from **Endesa** and Chilean company **Colbun**, could generate 2.75 gigawatts within 12 years in a country that, according to some analysts, must triple its capacity to power the energy-

“The most important thing is that our country needs to grow, to progress, and for this we need energy.”

— *Rodrigo Hinzpeter*

intensive mining industry and improve living standards. "The most important thing is that our country needs to grow, to progress, and for this we need energy," said interior minister Rodrigo Hinzpeter. However, the project has drawn opposition from those who say the economic benefits don't outweigh the damage to the pristine region. In the most recent Ipsos opinion poll, 61 percent of Chileans expressed opposition to the project and protestors have taken to the streets in Santiago, Coyhaique and several other cities. Heavily dependent on hydropower and imported fuel to meet its energy needs, Chile's energy supply is contingent on variable weather patterns and world events. While environmentalists have advocated renewable energy sources, particularly solar and wind, President Sebastián Piñera has said that renewables can't affordably meet Chile's growing demand and the country needs reliable large power plants, the *Christian Science Monitor* reported Tuesday. The project was supposed to begin construction in 2008 but has been delayed several times. HidroAysén still needs approval of an environmental study for the transmission line before breaking ground.

Political News

Obama Calls for Immigration Reform in Speech at Border

In his first visit to the U.S.-Mexico border as president, Barack Obama called Tuesday for comprehensive immigration reform and mocked his political opponents for blocking immigration reform efforts solely over border security, saying Republicans will not be satisfied until there is a moat with alligators separating the United States and Mexico. During his speech in El Paso, Texas, Obama said the border is more secure than ever with over 20,000 Border Patrol agents, more than twice the level at the border in 2004. "We tripled the number of intelligence analysts working at the border. I've deployed unmanned aerial vehicles to patrol the skies from Texas to California. We have forged a partnership with Mexico to fight the transnational criminal organizations that have affected both of our countries. And for the first time—for the first time we're screening 100 percent of south-bound rail shipments to seize guns and money going south even as we go after drugs that are coming north," said Obama, adding that Republicans wanted a border fence, which "is now basically complete." Obama added that his administration has "gone above and beyond what was requested by the very Republicans who said they supported broader reform as long as we got serious about enforcement." Obama said Republicans continue to be unsatisfied with border security efforts. "Now they're going to say we need to quadruple the Border Patrol. Or they'll want a higher fence. Maybe they'll need a moat. Maybe they want alligators in the moat. They'll never be satisfied." Obama added that U.S. authorities are seizing record amounts of drugs, weapons and currency and that fewer people are trying to enter the United States illegally. Obama did not propose any new immigration policies during his speech, but he said bringing illegal immigrants out of the "shadows" would benefit the United States. He said reform would strengthen the middle class "so that there is no longer a massive underground economy that

exploits a cheap source of labor while depressing wages for everybody else." Obama said undocumented immigrants are vulnerable to businesses that pay less than the minimum wage, fail to properly pay taxes and comply with safety and health laws. In a statement Monday, Republican Senators John McCain and Jon Kyl of Arizona said they hope the visit

to the border allows him to "finally see first-hand the continued security challenges facing all of those who live along our southwest border." They urged Obama to support the Border Security Enforcement Act, which they said "will provide the much needed personnel, infrastructure, and technology to gain control of our southern border."

Featured Q&A

Continued from page 1

ments. This is tragic for a company that keeps getting into new debt. The third effect will be to increase the reluctance of foreign companies to invest in the country. All in all, the short-term financial benefit that can be obtained from this new taxation is clearly offset by its detrimental effects in the long term. Social projects that should have been generated by oil income are nowhere to be seen in a country where promises have replaced deeds."

A **Juan Pablo Fuentes, economist at Moody's Analytics:** "A recently announced increase in the windfall oil tax is another example of arbitrary policymaking by the Venezuelan government. Since the early 2000s, the government has used revisions of the legal framework for the oil industry to advance two clear goals:

global oil prices, international oil companies (including state-owned companies) have remained cautious about investing in Venezuela. The latest increase in the windfall tax will only make investors more reluctant. Some of the new Orinoco projects were already in doubt due to PDVSA's inability to finance its share. The windfall tax increase might effectively kill some of those projects, even though the government offered them temporary exemptions from the increase. In any event, the windfall tax hike will further delay development of the Orinoco Belt. The main victim of the tax increase is PDVSA, which will suffer a measurable drop in revenues, further eroding its finances. This will make it harder for PDVSA to invest in new projects as well as to maintain existing oilfields. PDVSA's ability to fund social programs

“The main victim of the tax increase is PDVSA, which will suffer a measurable drop in revenues, further eroding its finances.”

— Juan Pablo Fuentes

obtaining control over all oil-related operations and increasing the industry's tax burden. Unsurprisingly, the result has been disastrous for Venezuela's oil industry. Output has declined consistently in recent years despite record high oil prices. The government seems to be genuinely concerned about falling oil output and is aggressively pursuing new investments to develop the Orinoco Belt. Despite some concessions and high

will also decline. In essence, the government is transferring that responsibility, at least partially, to the development fund, Fonden. The increase in the windfall tax will provide President Hugo Chávez with about \$12 billion in additional revenues this year. These resources will fund higher levels of government spending on wages, imports and some infrastructure projects designed to boost Chávez's reelection chances in 2012."

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Accused International Drug Trafficker Arraigned in Venezuela

A Venezuelan accused of being a major drug trafficker was arraigned Wednesday after being extradited from Colombia, the Associated Press reported. A judge in Caracas ordered Walid Makled, who stands charged with crimes including drug trafficking, money laundering and hired killings, to remain imprisoned in the headquarters of the national intelligence agency during his trial, according to the government-run



Venezuelan News Agency. Makled was extradited from Colombia to

Makled
File Photo: *Venezolana de Televisión.*

Venezuela on Monday, approximately nine months after his arrest in Colombia. Both Venezuela and the United States had requested Makled's extradition, but Colombian President Juan Manuel Santos approved Venezuela's request, saying Makled was charged with more serious crimes in the neighboring country and it had made its request before Washington did. The move came amid Santos' efforts to repair frayed relations with his Venezuelan counterpart, President Hugo Chávez. Makled's arraignment came a day after a London-based think tank released a 240-page book alleging ties between the Revolutionary Armed Forces of Colombia (FARC) and the governments of Chávez and Ecuadorean President Rafael Correa. In a statement, the Venezuelan Embassy in London questioned the "authenticity and validity" of the information released by the International Institute for Strategic Studies. The analysis "looks like a dodgy Latin American dossier," said the embassy, which quoted Interpol as saying the files' handling by Colombian authorities did "not conform to internationally recognized principles for the ordinary handling of electronic evidence by law enforcement." The embassy added that Colombia's Supreme Court has "dismissed the 'evidence' coming from the computers as inadmissible in prosecution cases against Colombian politicians."

Economic News

Peruvian Congress Eyes Protection of Private Pension Funds

Peru's Congress this week is planning to debate a proposal to protect the country's private pension funds as it looks to the possibility of leftist Ollanta Humala being elected on June 5, Dow Jones reported Friday. Humala, a former army officer who is running against legislator Keiko Fujimori, previously announced plans for a new public-sector pension fund system, to which workers be required to contribute. Contributions to private pension funds would be optional. Currently, workers are required to contribute to either a private pension fund or the national public system. In the past week, private pension fund representatives have said Humala's plan would be devastating to the current private system, which uses a portion of workers' contributions to cover management costs and fees. The legislation to protect the private pension funds, which contain about \$30 billion, aims to make the funds "untouchable" by future governments. Current Finance Minister Ismael Benavides proposed the initiative. The measure would require the Peruvian bank regulator, known as SBS, to approve any changes to the mandatory pension

The legislation to protect the private pension funds, which contain about \$30 billion, aims to make the funds "untouchable" by future governments.

contribution amounts. Also, SBS would review the private contribution levels every five years. Among the companies involved in the private pension system are **ING Groep, Bank of Nova Scotia, Banco Bilbao Vizcaya Argentaria** and **Credicorp**. The private system has approximately 4.7 million Peruvians as clients.

POLITICAL & ECONOMIC BRIEFS

Honduras' Zelaya to Return to Honduras Within a Month: Aide

Former Honduran President Manuel Zelaya, who was ousted in the country's June 2009 coup, will return to his country after nearly a year and a half in exile, an aide told the Associated Press Wednesday. "He has the will and desire to return to his homeland," Rasel Tome said of the former president, who has been living in the Dominican Republic. Honduras' Supreme Court last week dropped the last remaining charges against Zelaya, paving the way for his return and Honduras' possible readmission to the OAS. [Editor's note: See related Q&A in [Tuesday's](#) edition of the *Advisor*.]

Haiti Reverses Results of 15 Legislative Races

Haitian election officials on Wednesday reversed the results of 15 out of 19 legislative races that were contested by observers, the Associated Press reported. The international community expressed concern after the preliminary tallies from the March 20 runoff were wildly different than the final results released a few weeks later. Under the new changes, three of the seats will go to President René Préval's Unity party, which the U.S. Embassy in Port-au-Prince said still should have gone to other parties.

Chile, Peru Raise Interest Rates to Two-Year High

The Chilean central bank raised its benchmark interest rates from 4.5 percent to 5 percent and Peru implemented a quarter-point increase to 4.25 percent Thursday, hitting two-year records, Bloomberg News reported. Peru's economy is expected to expand by 7.5 percent this year, while Chile is projected to grow by 5.9 percent.

Featured Q&A*Continued from page 4*

A **Boris Segura, economist at Nomura Securities International Inc.:** "This changed oil taxation in Venezuela is likely to have a lasting impact on the private sector's willingness to invest. The new sudden profits tax represents yet another change in 'the rules of the game' in the oil sector, which is likely to have a chilling effect on private investment in the sector, especially at a time when the authorities are putting pressure on minority partners to increase investment and production. This new tax regime practically borders on confiscation once oil prices surpass \$70 per barrel. These tax changes are particularly relevant to the development of new heavy oil projects in the Carabobo/Junin areas. As there are very costly investments (basic infrastructure, upgraders, etc.) that run in the billions of dollars, the unpredictability of the basic investment conditions are likely to make it more difficult for minority partners to justify allocating resources to new investments in Venezuela. The jury is still out on the effectiveness of President Chávez's social programs. However, this latest tax change is explicitly devised to allow the authorities to do away with oversight on the use of public resources, displaying a worrisome lack of transparency. As such, the Fondo de Desarrollo Nacional (Fonden) provides plenty of discretion to the authorities in deciding how to spend the revenues it holds that otherwise would have to go into the official budget. More importantly, Fonden captures revenues from PDVSA before they make it into the budget, so as to avoid sharing them with the states and municipalities.."

A **Carlos Belloin, petroleum analyst at IHS in London:** "The new 'special contribution' (SC) as it is known, also set in \$70 per barrel as the ceiling for the calculation of royalty, extraction tax and import registry tax payments for companies

liable to pay the SC and established a 20 percent rate on the difference between the price of the value of the Venezuelan hydrocarbon basket as established in the Annual Budget Law (currently \$40) and \$70 per barrel. The first tier (\$40-70) is the regressive part of the SC which commences to be progressive after price breaks up the \$70 per barrel barrier. Although progressive in nature, the biggest chunk of the SC is payable when prices are between \$70-90 because the base is larger than the second tier (\$90-100) and mostly likely to be larger than the third one (greater than \$100), even though the rates are higher when prices are higher. The effect on investments is still to be assessed when the Ministry of Energy and Petroleum issues a resolution in order to help in the implementation of the SC, defining the parameters for 'recovery of investments' and 'incremental production,' which are essential issues to determine if a certain project is exempted from the payment of the SC or not. What can be said now is that this new levy will have a negative effect in the cost of the financing the new projects in the Orinoco Belt. This would be the most immediate effect. Existing projects in Venezuela (including the ones in the Orinoco belt) are liable to pay the SC although their 'incremental production' is exempted and new projects are exempted from this tax until they have recouped their total investments. Again, we will have to wait for the ministry's resolution to measure the full impact of the SC. It is not a secret that despite the massive amount of money received by the Chávez administration, it hasn't been able to implement any sustainable, lasting and viable social projects. I really hope that this trend changes during this new high oil price wave."

The Energy Advisor welcomes responses to this Q&A. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.

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