

## **Increasing Trade Security: United States-Venezuelan Trade Incentives**

Nathaniel T. Edwards

University of Georgia

ntedwar@uga.edu

Dr. Christopher Allen, faculty advisor

### **Abstract:**

Trade with Venezuela has risen to the top 15 nations with which the United States conducts trade; it has also become the fourth largest provider of American crude oil and petroleum products, topping over a million barrels every day. While trade with Venezuela has steadily increased, diplomatic relations have steadily declined due to open antagonism and criticism by both sides. In juxtaposition, there is a significant national security threat as Venezuela becomes a prime locale by which to load a weapon on a boat intended for American ports and Venezuela offers little domestic protection of exports to America. This risk is becoming even greater as Chavez continues to increase relations with American adversaries and openly critiques American capitalism. As trade relations increase, each state can demand a greater level of security be met and maintained in order for trade to continue. Therefore, this paper proposes the creation of a system of economic incentives in exchange for meeting and maintaining security standards at ports. Because there is a risk of Venezuelan hesitance to participate, the policy aims to appeal exclusively to the economic sector of Venezuela and avoid political confrontation. Furthermore, it aims to avoid Chavez' criticism of capitalism by establishing a controlled economic system between the United States and Venezuela. This policy will be rationalized by comparing similar case studies as well as noting inherent benefits of trade systems.

Improving national security in the United States requires increasing our efforts in some of the country's most inherently vulnerable areas—its ports. The primary port

activities, loading and unloading, are subject to minimal governmental regulation, and much of the security burden subsequently falls to corporations and industry. Where government regulations exist, they are often undermined by business interests seeking to prevent delays by avoiding shipment screening. Furthermore, the sheer number of physical components involved in trade make regulation complex. It is estimated that over 46,000 ships and almost 4000 ports are engaged in some form of international trade.<sup>i</sup> In effect, the government's ability to monitor what enters and exits the country is limited, drastically reducing its ability to protect the country. To address this gap in national security and the private sector-dominated paradigm, the United States must engage and utilize the private sector to secure American ports from small arms trading, drug cartels, and potential terrorist threats, especially nuclear ones.

The International Maritime Organization (IMO) passed the new International Shipping and Port Security (ISPS) code in 2004 to address the issue of port security and vulnerability. Previously, the IMO had passed the International Convention for the Safety of Life at Sea (SOLAS) in 1965. SOLAS was designed to address safety of ships and ship-port interaction. The agreement regulated building and shipping standards to ensure safe sailing from unintentional hazards<sup>ii</sup>. Because SOLAS failed to address intentional activity, the IMO created the ISPS code. The IMO, which actively oversees the conversion of ports to meet the new regulatory standards of the ISPS code, reported in 2004 that “fewer than 20 percent of the world's ships and 10 percent of global ports had certified that they have made the changes called for by the new rules” within a week of their July 1 deadline.<sup>iii</sup> Official U.S. policy requires turning away ships that do not meet the regulations, a mandate that is unlikely to be fulfilled by port administrators because of

its negative affect on trade, further compounding the issue of port security. Schoen, a senior producer at MSN, reports that the largest obstacle is a lack of financial resources. For example, the United States spends only a nickel on maritime security for every dollar spent on aviation security, with only \$500 million having been utilized to counter maritime terrorism since September 11, 2001, compared to \$11.7 billion for aviation terrorism.<sup>iv</sup> For less developed nations, an even smaller amount of money is available to enforce port regulations. A 2003 Organization for Economic Cooperation and Development report estimates the initial cost to ship operators of complying with the ISPS code at \$730 million to \$1.3 billion.<sup>v</sup> Many less developed nations lack the financial means to comply with the ISPS code, preventing even well-intendin governments from meeting IMO security standards. It is therefore imperative that countries are given the means and the incentive for meeting the security standards set by the IMO. Moreover, American private port facilities are burdened with renovations, which have not been made a high priority, and necessary safety renovations have gone unchecked in favor of more affordable and more lucrative renovations, such as scales or aesthetics. It is imperative that businesses, like states, be rewarded to meet security goals.<sup>vi</sup> In the absence of incentives, many states and businesses will be unable to comply with the ISPS code. Therefore, without some form of incentives, ports worldwide will be without necessary security measures—radiation detection technology, adequate manpower, secure fencing, and so on—to comply with ISPS regulations. States that, with or without incentives, fail to meet the ISPS code will otherwise be negatively coerced to comply.

Many ports may be forced or choose to turn away entering ships that do not comply with the ISPS code. According to Stephen Flynn of the Council on Foreign

Relations, if all ships are barred from entering ports when they fail to meet regulations, some states might experience upwards of 50 percent unemployment throughout the entire economy. Unemployed populations are prone to migrate or become involved in crime or terrorism, especially in Caribbean states.<sup>vii</sup> Such effects are sure to spread from the Caribbean to Latin America, where many prominent U.S. trading partners are located, namely Venezuela.

A decline in employment that leads to increased crime or terrorism has widespread implications. Terrorism not only directly affects nations through its human and physical costs (buildings, boats, etc), it also effects also economic systems. Terrorism that affects private businesses will disrupt their market participation. Private actors are inclined to trade through the most secure channels—businesses or states perceived as being exempt from terrorist threats—especially if a business feels its own ships or personnel are threatened. Potentially, terrorism could cripple developing economies beginning to globalize. A study conducted by the World Bank suggests that economic deterrence is heightened even more if an attack is performed by an organization from within a trading partner’s state.<sup>viii</sup> A trading partner viewed as a security concern is quickly relegated to a position of lesser importance. The larger the trading partner, the greater the potential for trade displacement following a terrorist attack.

Trade data indicates that Venezuela ranks within the top fifteen nations in dollars of U.S. imports. Additionally, it is the fourth largest provider of crude oil to the United States, supplying 1.221 million barrels every day. Venezuela also supplies the United States with 1.4 million barrels of petroleum daily.<sup>ix</sup> Lapper notes that although America is dependent on Venezuelan oil, Venezuela is more acutely dependent on American oil

consumption.<sup>x</sup> However, as China invests heavily in Venezuelan oil, this dependency safeguard will erode. A news report indicates that Chinese investment in oil and gas fields in Venezuela will reach five billion dollars<sup>xi</sup>. That same news report quotes Venezuelan Energy Minister Ramirez explaining the growth of exported oil to China, rising from zero in 2004 to 200,000 barrels a day in 2006, with a projection of 500,000 barrels in 2009 or 2010. Venezuelan dependence on U.S. oil consumption is expected to continue in the immediate future as long as the United States has the ability to refine large quantities of Venezuelan crude oil and China does not. Additionally, transportation costs and technological symmetries make U.S.-Venezuelan trade, rather than China-Venezuelan trade, the most beneficial for Venezuela.<sup>xii</sup> Trade disruptions with Venezuela would have significant economic and political implications for the United States.

Despite their important trade relationship, the diplomatic relationship between Venezuela and the United States has grown tenuous since the 1998 election of President Hugo Chavez and his accompanying socialist agenda. Consequently, American policy must be equipped to provide greater security between itself and its trading partners, especially when those partners are aggressive. Again, Venezuela is of particular concern because of its high level of exports to America and the deteriorating relationship between the two nations.

President Chavez's foreign policy aims to make connections and develop relationships with nations who share similar values, especially anti-imperialist sentiment, or who are viable trading partners and major oil consumers. For the most part, oil has been the strongest connection between Venezuela and other states with which it has forged positive relationships.<sup>xiii</sup> Venezuela's attempts to expand its trading partners,

establish international relationships, and develop a stronger, better-equipped military are part of a greater movement to modernize the country. President Chavez has increased trade with North Korea, Iran and Cuba, forging controversial arms deals with these U.S. adversaries.<sup>xiv</sup> In July of 2007, President Chavez launched the construction of a joint petrochemical plant with Iran's Mahmoud Ahmadinejad; the two also signed a series of trade deals designed for economic expansion in an "axis of unity."<sup>xv</sup> Both nations are hostile towards the United States but are also prominent members of the Organization of Petroleum Exporting Countries (OPEC). President Chavez told reporters "the two countries will united defeat the imperialism of North America." A week before the conference the President forced two major U.S. oil companies out of Venezuela—Exxon Mobil and ConocoPhillips.<sup>xvi</sup> He has also initiated an anti-American socialist agenda, which allegedly heightens the chance of harming trade relations with United States, mostly indirectly by shipping small arms and drugs into the United States or by allowing other states to use Venezuelan shipping to carry in weapons of mass destruction (WMDs). A World Bank study found that most states from which incidents of terrorism or sabotage originate are developing states specializing in natural resources and manufacturing those resources, such as oil and oil related products.<sup>xvii</sup> Such products are the major exports of Venezuela, and the major American imports from Venezuela.

### Policy Proposal

It is widely believed that increased security at a country's borders facilitates an increase in international trade. However, current research indicates that increased trade also increases security for the participating nations. As each nation increases its

engagement in international trade, the level and types of security measures that can be demanded and met increase. Furthermore, contributing to a state's development contributes to its general prosperity, including economic and political reform. A study conducted by the University of Kentucky Center for Business and Economic Research argues that even in bilateral trading systems, where there is a high likelihood of conflict, increasing trade does not increase its vulnerability or the likelihood of armed conflict.<sup>xviii</sup> Establishing a security cooperative<sup>1</sup> with Venezuela would provide the vehicle by which to increase trade security between the two nations with a low risk of conflict escalation. A "cooperative" would be preferable between the United States and Venezuela in that it does not demand formal agreements or obligations between each state but still contains some structure and provides benefits for maintaining the relationship, similar to informal multilateral arrangements such as the Wassenaar Arrangement.

To increase security within a secure bilateral framework, the United States should offer to increase trade as an incentive with Venezuela if they comply with the standards of the ISPS code set by IMO. Specifically, the United States should require Venezuela to meet security benchmarks such as installing advanced generation radiological material detectors in order to increase American trade with Venezuela. Implementing a system of security for trade between trading partners is an effective way to increase security in an openly hostile nation. The agreement should apply equally to both parties, so that for every benchmark an American shipping company meets, more Venezuelan business is offered. The system would require a government-private relationship structured through contracts that obligate businesses to conduct trade in Venezuela or with Venezuelan

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<sup>1</sup> Security cooperative: a bilateral informal arrangement using economic incentives to produce political and governmental effects

businesses. Optimally, each state can strategically establish contracts in order to open particular industries in each other's state.

For example, State A assembles a group of private businesses expressing interest in trade with State B. State B assembles a group of private businesses expressing interest in trading with State A. The government and the business groups work together as a state cooperative. As Cooperative B meets a level of security standards, Cooperative B is offered a particular level of trade from the businesses in Cooperative A. The security standards met may be achieved through actions by government mandate or private sector initiative. If the state funds the security upgrades, then trade offered may be granted to the businesses at the states' discretion. If a private company complies with the security upgrades, then only that company is offered increased trade from businesses within the other cooperative. As the level of security increases, the cost of compliance also increases, and higher costs tend to inhibit trade. The dollar amount increase in trade offered as an incentive must be more than the cost of providing a certain level of security, but it must also be less than the cost of providing the next level of security. In this way, access to trade can serve as an incentive for countries to continue upgrading their security measures until they reach the highest possible level based on IMO standards.

The ISPS code requires the security or risk assessment of each ship and port to be performed by the contracting government—in this case the United States and Venezuela. The levels of security that each nation can obtain correspond with the three levels of risk detailed in the ISPS code. The goal is to upgrade all ports so that they achieve level three security and are capable of responding effectively to a high-risk incident. The risk assessment has three main components. First, the contracting government must identify

and evaluate critical assets and infrastructure in the port facility that could suffer significant damage or casualties. Second, the contracting government must identify and enumerate the actual threats to those critical assets and infrastructures and prioritize them. Third, the contracting government must identify vulnerability by noting weaknesses in physical security, structural integrity, protection systems, procedural policies, communications systems, transportation infrastructure, utilities and other likely targets.<sup>xix</sup> Based on this assessment and cost estimates, the amount of trade per security improvement can be determined and converted into dollar amount estimates.

It is imperative that there is consistent interaction between the private and public sectors. Most threat information is known first, if not only, by the contracting government; the public sector must share this information and provide the means to make this information easily accessible.<sup>xx</sup> Relying on private volunteering to investigate threats and secure them ignores the security threat. And because costs are so high, financially or physically, many businesses are unlikely to voluntarily secure all but immediate threats. By establishing a program that is beneficial for the security and financial status of the private sector, businesses are more likely to become secure, even those who may be exempt from IMO's ISPS code.

### Challenges and Benefits

Implementing a security cooperative with Venezuela will bring auxiliary benefits to United States industry and security. However, a number of likely challenges must be overcome to ensure that such an arrangement can be implemented successfully. This

security cooperative can be reasonably established if the challenges and why they exist are fully addressed.

Economic globalization has both positive and negative effects on trade security. Globalization will erode funding sources for dissident and terrorist organizations by creating international pressure on countries in areas such as export controls and transactional transparency, bolstering national security.<sup>xxi</sup> Conversely, because terrorist organizations often depend on smuggling or money laundering and private donations as their main funding sources, globalization increases access to sources from which an organization might potentially acquire funds. Strengthening the economic ties between Venezuela and the United States causes Venezuela to become more invested in preventing terrorist attacks on either trading partner. Although terrorism may seem to thrive in a globalized economy, increased trade creates strong incentives for each state to prevent attacks—leading to the enactment of security measures that weaken rogue organizations.

The United States also benefits from strong, stable trade relations with Venezuela in the area of energy cooperation. Energy cooperation includes assistance in developing and modernizing the technology to efficiently extract and utilize energy resources. Previous efforts to support modernization and bilateral investment, especially throughout the 1990s, have failed as technology and information exchanges have become less frequent with the deterioration of the political relationship between the United States and Venezuela.<sup>xxii</sup> Stabilizing the Venezuelan economy and establishing a normalized trade relationship would help to reverse declining energy cooperation. Bilateral energy

cooperation translates into a stable energy infrastructure for Venezuela and the United States.

A historical example of a successful trade expansion occurred between America and the Soviet Union during the Cold War, illustrating the level of stability and security that trade can achieve. During the Cold War, when diplomatic tensions were at their highest levels, trade between the two states neither promoted arms production nor detracted from each state's national security.<sup>xxiii</sup> Rather, as each state perceived itself to be threatened by the other, trade policy increased non-threatening trade and decreased threatening trade of goods between them. The trade relationship between the United States and the Soviet Union provided an economic incentive to limit aggression and promote cooperation as the states become increasingly economically interdependent. In fact, Gift suggests that increased trade encouraged each state to comprehensively examine its trade deals and consequently, to increase its security by dictating what entered and exited each state.<sup>xxiv</sup> The U.S.-Soviet analogy provides an important illustration of the potential security benefits of tying the Venezuelan economy to that of the United States.

In 2006, the United States and Russia signed a bilateral trade agreement. The agreement details what measures the United States would require Russia to adopt before supporting its entry into the World Trade Organization (WTO) and serves as a model for a Russian draft of a Protocol of Accession. If Russia meets these requirements and joins the WTO, trade between the United States and Russia will be expanded greatly. Therefore, Russia's entry into the WTO would provide multiple economic and economic and security benefits for the United States: expanded access to non-agricultural goods

markets, new service markets (such as banking, securities, insurance, telecommunications, energy, and audio-visual services), transparent and predictable tariff treatments for agricultural products, reduced non-tariff barriers, and improved Russian enforcement of intellectual property rights.<sup>xxv</sup> Existing bilateral trade between the United States and Russia has grown by 15 percent annually, valued at around \$19 billion in 2005.<sup>xxvi</sup> Establishing far-reaching economic relationships yields significant benefits. Venezuela is already a member of the World Trade Organization and is thus primed for significant trade growth with the United States, as far as prerequisites for that trade. Trade with Venezuela may not return as large financial returns as trade with Russia, simply because of less capital and material trade available, but it would provide similar benefits to both the economy and national security.

Nonetheless, increasing bilateral trade based on security improvements faces several obstacles. Foremost, it cannot be guaranteed that President Chavez and his socialist state will participate in a program based on a capitalist model and necessitates cooperation with the United States. However, a study conducted by Biglaiser and Brown, writing for the World Trade Organization, suggests that political institutions “do not pose significant constraints” on particular economic aspects.” Trade and capital are relatively unaffected for the most part by existing political policy structure.<sup>xxvii</sup> Therefore, if President Chavez were to act in accordance with the suggested policy, an agreement could be settled upon, despite the political structure of the state. Despite suggestions that the existing political system will not interfere with trade relations, President Chavez’s administration has additional reason to be hesitant to strengthen Venezuela’s relationship with the United States. In 2002, President Chavez believes that Washington helped fund

an unsuccessful coup to remove him from power. The United States also provides financial aid through USAID to the International Republican Institute (IRI), the National Democratic Institute for International Affairs (NSDIA), Freedom House, Development Alternatives, and Pan-American Development, all agencies viewed with skepticism by the Venezuelan government. USAID also recently increased direct funding to Venezuelan agencies that promote political and human rights, as well as business associations<sup>xxviii</sup>. These organizations work to promote democracy by undermining Chavez's administration, primarily through propaganda campaigns. After the 2002 coup attempt, the United States founded the Office of Transition Initiatives (OTI) in Caracas "with the all but explicit intention of aiding efforts to oust President Chavez."<sup>xxix</sup> United States support of non-governmental organizations (NGOs) and private sector participants that oppose President Chavez leads the Chavez government to question the sincerity of attempts by the United States to strengthen its relationship with Venezuela.

In light of Venezuela's difficulty joining the Common Market of the South (MERCOSUR), the state may decide to participate in an economically-oriented security cooperative in order to prove itself a reliable trading partner.<sup>xxx</sup> Establishing a secure trading network with the United States offers Venezuela a greater chance at eventually joining MECOSUR. The private sector could also thwart the success of the Cooperatives if the agreement is perceived as cost-inefficient or because it delays and limits the open trading markets that many shipping companies now enjoy. United States and Venezuelan business communities must be encouraged to participate with real political enthusiasm the offer of a stable trading partner, and increased security with as little inconvenience as possible. Participation in the security cooperative also helps businesses—shipping

companies and private ports—mitigate the costs of funding security improvements, such as customs checkpoints that delay delivery of products.

As security systems are upgraded and streamlined, in accordance with the ISPC code, all stakeholders stand to gain. This assertion is backed by a 2005 Organisation of Economic Co-operation and Development (OECD) policy brief, which found that governments benefit from increased efficiency in processing and detecting fraud, which increases revenue. Businesses benefit because they can deliver goods more quickly with less likelihood of delay or obstruction, and consumers benefit because increased trade and streamlined security mean that cheaper goods can be obtained faster. According to the OECD study, benefits are experienced by both developed and developing states; but especially in developing countries because replacing current systems that are inefficient and unstable can reap large benefits.<sup>xxxi</sup> An incentive program can provide the motivation and means to improve trade relations and meet security standards, while mitigating many of the negative effects by providing immediate economic gratification for making security upgrades.

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<sup>iv</sup> Ibid.

<sup>v</sup> Ibid. see i

<sup>vi</sup> Ibid. see iii

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<sup>viii</sup> Mizra, Daniel, Thierry Verdier, "International Trade, Security and Transnational Terrorism: Theory Empirics," World Bank Policy Research Working Paper 4093 (December 2006)

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- <sup>xvii</sup> Ibid. see viii
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