Subversive Oil

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The IV th Republic, as the political regime prior to 1998 has been posthumously baptized, was torn apart by two subversive movements, one in the military and the other in the national oil industry. The story of military subversion is well known, but not the story of subversion in the national oil company, *Petróleos de Venezuela, Sociedad Anónima* (PDVSA). After nationalization of the oil industry in 1976, PDVSA became something of a 'state within a state.' Its Venezuelan executives shared the outlook of international oil companies, for whom they had worked for many years. Furthermore, successive governments of AD and Copei during and after the boom period of the 1970s failed to create a new efficient fiscal and regulatory system, at the same time that they implemented disastrous developmental policies characterized by poor planning and waste. This ultimately led, after 1989, to the 'oil opening policy' *(Apertur*a), which put Venezuelan oil policy on a path toward re-privatisation of the industry. It also put Venezuelan oil policy on a path toward minimization of fiscal oil revenues. President Hugo Chávez arrested the momentum, but the direction of oil policy remains very divisive not only in Venezuelan society but within the *Chavista* movement as well.

There are some remarkable parallels between the ways each of these two subversive movements arose. Chávez founded his movement around 1982; PDVSA executives embarked on their strategy of internationalisation in 1983. Internationalisation was devised by PDVSA to create a conveyor belt to relocate profits out of the reach of the government through transfer pricing (i.e., the price charged by one affiliate to another affiliate in the accounts of the mother company). Both PDVSA executives and Chávez and his followers believed that the current political regime was beyond repair. In the judgment of both groups of conspirators, the squandering of oil revenues played a crucial role in this steady decline. Both the military and PDVSA took a moralizing approach, blaming corruption for the crisis. The military dreamed about saving the country; PDVSA executives dreamt about saving the oil industry from the country.

The Aftermath of Nationalization

Nationalization in Venezuela in 1976 was the outcome of a long-term policy of maximizing fiscal revenues collected from oil exports. For the last two years prior to nationalization, for every dollar of oil exports, the government collected 80 cents in rents, royalties and taxes. By 1970 the government had asserted a right to levy export taxes at its sole discretion, effectively leaving the companies with nothing but a regulated profit.

The foreign companies were losing control of their businesses. They could no longer maximize their own profits because additional earnings were subject to appropriation by the government via the export levy. They hardly resisted when President Carlos Andrés Pérez nationalized the industry on January 1, 1976. However, only a few years after Pérez left office, his plans to create 'Great Venezuela' and develop the country through an overnight program of industrialization had failed disastrously. PDVSA then began to develop its own 'hidden agenda' to break away from state control.

Nationalization changed *ownership* of the oil industry but not, for the most part, *managemen*t. Prior to nationalization, there were three major foreign companies operating concessions in Venezuela: Exxon, Shell, and Mobil. Over the years, partly in response to political pressure, the companies selected Venezuelan nationals for executive positions. These executives accepted nationalization in 1976 only because they had no choice. Once they were in charge of PDVSA, their prime objective was to displace the Ministry of Energy and Mines (MEM), the traditional steward of the 'landlord' state. The company certainly did not have in mind the maximization of fiscal revenues (royalties, income taxes, and export levies). On the contrary, once the 'Great Venezuela' of Pérez had crashed, PDVSA sought to limit its own fiscal obligations. The failures of development policy only reinforced the company's determination. Why generate fiscal revenues that would be squandered anyway? Why maximize profits when the state would inevitably siphon them into the Treasury? Instead, the company concentrated on its own agenda: the development of the oil sector in real terms, maximizing volume, turnover and sales (not profits) in all the segments of the industry, both at a national and an international level, at the same time that fiscal revenues were disregarded. PDVSA thus undermined nationalization and paved the way for the return of private investors. By 1989, when Pérez was back in office and implementing his 'Great Turnabout,' which included the *Apertura* to foreign capital, an alliance emerged between the national oil company, on the one hand, and the international oi1 companies and the consuming countries, on the other. Contrary to what is widely believed, outright privatisation was not the top priority of this alliance. The international companies and the consuming countries were primarily worried about dismantling the political and institutional framework that had led to nationalization in the first place. That is, they wanted to reduce the power of the state to maximize its share of oil revenues and to control prices and supply. Their strategy was to put in place a new governance structure designed to prevent the government (in the form of the MEM) from ever again pursuing a strategy of maximizing fiscal revenues. Only then would full-scale privatisation move to the top of the agenda (Mommer 2002a). In the meantime, foreign capital in association with PDVSA became again a major producer in Venezuela. At present about 25 percent of Venezuelan oil is produced in this form. According to the contracts signed under the terms of the post-1989 period of *Apertur*a, this percentage will increase to over 40 percent by the year 2010 (Mommer 1998).

When foreign companies controlled oil production and set prices, the state was naturally vigilant over their operations. After nationalization, vigilance seemed unnecessary. Worse, in response to the explosive growth of oil prices and, hence, fiscal revenues in 1973/74, the newly elected Congress passed an Enabling Law that gave President Pérez complete liberty to spend the money at his discretion, in accordance with his vision of a 'Great Venezuela.' In other words, Congress shirked its most elementary and essential task: the control of public finances. Pérez launched a series of huge investment projects, nationalized the iron industry, and forced foreign capital out of many other key economic areas, such as banking and chains of retail commerce, while a system of state enterprises arose in the heart of the new economy. Simultaneously, private Venezuelan enterprise was marginalized. Fedecámaras, the peak organization of the business community, had grown on the eve of nationalization into a politically (even economically) relevant body. Once the foreign members of the organization left, among them the international oil companies, what remained was only a shadow of its former self.

During the post-nationalization years, the government – or more precisely, the President – appeared to hold all the trump cards. Fiscal income from oil increased from $1.4 billion in 1970 (about ten percent of GDP), to $9 billion in 1974 (a staggering 40 percent of GDP). Such an influx relative to the nation's productive structure was far beyond the absorptive capacity of the economy. Worse, in the rush to build his 'Great Venezuela', the Pérez government contracted international loans, in effect spending future oil revenues on top of huge current earnings. With foreign enterprises leaving, the capacity of the economy to absorb capital was actually falling.

The country did not need the money of foreign investors at the time, but it certainly needed their managerial skills in order to bring its ambitious investment plans to fruition.

Thus, at the end of the day, the government, isolated and helpless, was to drown in its financial wealth. Political clients, not citizens or business partners, surrounded the state, which was supposedly possessed of magical powers to develop the economy (Coronil 1997). This was a recipe for disaster. Congress never recovered control over public finances; nor would the private sector ever recover its proper role. Only foreign creditors were eventually able to force the government and state enterprises to change policies, and then with their own particular agenda. After 1983, there was only one strong and working institution left standing within the national economy: PDVSA. The lack of checks and balances was to become of consequence for this company as its virtually autonomous status allowed it to go ahead with its own particular agenda.

The Internationalisation Policy of PDVSA and Transfer Pricing

PDVSA's first response to the implementation of exchange controls in 1983 was its internationalisation policy (Boué 1997). In a last minute and unsuccessful effort to contain the developing foreign debt and currency crisis, the government fell back on the investment fund of the company, totalling about $5.5 billion, which it had been allowed to accumulate during the years of high prices. At the same time, however, oil price hikes led to sharply falling demand and to ever more restrictive OPEC quotas, which left the company no outlets for new investments in Venezuela. In order to prevent the government from appropriating its liquid assets again, PDVSA decided not to have any.

As investing in the country was not feasible, accumulated profits had to be spent abroad. But where could the money be spent at a time when production was to be cut? The answer was PDVSA's internationalisation policy. In 1983 PDVSA bought its first share of a foreign refinery (VEBA) in Germany. At the time, the company argued that this refinery would provide a market for Venezuela's heavy crude, which were difficult to market otherwise. To this very day, however, the German refinery has never processed heavy crude. Over the years, PDVSA has supplied VEBA lighter crude oil that could have been easily placed on the world market anyway. Furthermore, PDVSA has sold the oil to its European interests at substantially discounted 'transfer' prices, thereby shifting a portion of its profits beyond the reach of the Venezuelan government (Guevara 1983).

Some politicians belonging to *Acción Democrática* (AD) – Rafael Guevara and Celestino Armas – became aware of the maneuver and raised the alarm in Congress, but to no avail. On the contrary, the issue of transfer pricing was settled entirely in favor of PDVSA when the government of President Jaime Lusinchi (1984-1989), himself a member of AD, decreed that the company would henceforth set its own prices. This decree gave the internationalization policy a new boost. Subsequently, PDVSA shifted its attention to the U.S. market, where it operates under the name of Citgo. Once again PDVSA bought systematically into refineries, signing long-term supply contracts and granting substantial discounts to its new affiliates for the purpose of transferring significant portions of its profits abroad. In order to ensure that this money was definitively beyond of the reach of the government, the contracts were used as collateral to secure foreign loans. Thus, before Chávez or any other future government can change the terms of the contracts between PDVSA and its own subsidiaries, it will have to cancel all of PDVSA's debts, which now total nearly $10 billion.

This goal of shifting profits abroad is the real motive for internationalization and explains the unchecked growth of PDVSA's international refinery network, presently capable of handling about two million barrels per day (b/d), and its retail business, consisting of over 14,000

gasoline stations in the U.S. By the second half of the 1990s, PDVSA was remitting through transfer pricing an average of about half a billion dollars annually from its domestic accounts to its foreign affiliates (Mendoza Potellá 1995; Boué 2002). For eighteen years after the beginning of internationalization, the foreign affiliates of PDVSA never paid dividends to the holding company in Caracas. But earning profits for the country was never the objective of the policy in the first place. In December 2001 the Chávez government obliged them to pay dividends for the first time.

OPEC Quotas and PDVSA

In the early 1980s, after world-wide demand began to flag, OPEC created a quota system in an attempt to maintain high prices. Both PDVSA and the financially troubled Venezuelan government started to look for ways to minimize the impact of, or to bypass, these quotas. Thus, in 1983, Venezuela began to measure production subject to quotas at refinery gates and ports of exports rather than in the storage tanks of the producing fields (as usual everywhere in the world for the purpose of royalty payments). At the time, PDVSA promised MEM that it would install modern meters in the fields. This never happened, despite the repeated and formal protests of the Ministry over the next fifteen years. As a result, MEM effectively lost its ability to monitor and control levels of production of crude oil and natural gas, giving PDVSA significant leeway to minimize its royalty payments.

PDVSA looked for other ways to manipulate the definition of crude oil subject to OPEC quotas: increasing production of the extra-heavy (i.e. heavier than water) crude of the Orinoco Belt, by far the largest reserves of its kind in the world. The company argued that Orinoco deposits – which are processed into a product called "Orimulsión" – did not fall under the definition of crude oil. (This assertion is technically correct, as they do not constitute a liquid at normal temperatures.) Therefore, PDVSA argued, the Orinoco Belt should be classified as 'bitumen' and, hence, not be subjected to OPEC quotas. In 2000, PDVSA produced approximately 100,000 b/d of Orimulsión derived from about 70,000 b/d of extra-heavy oil – and it planned to triple this figure in the near future.

After 1989, with the initiation of *Apertur*a, PDVSA entered into joint ventures with foreign companies in four integrated projects for the production of synthetic crude ('syncrude') from the same extra-heavy grades of oil. PDVSA planned to increase production of syncrude to 1.2 million barrels per day (requiring about 1.5 million b/d of extra-heavy crude) by the year 2010. Like Orimulsión, syncrude is subject to lower levels of taxation (one percent royalty and 34 percent income tax). If this oil were included in Venezuela's OPEC quota, it would displace more highly taxed conventional crude from PDVSA's exports. Calculated on prices in the first half of 2001, the loss in revenue for the government would be as high as ten dollars per barrel.

The rush into the Orinoco Belt was justified during the years of *Apertura* with the argument that it was not subject to OPEC quota. A more far-reaching purpose, however, was to force Venezuela into conflict with OPEC, possibly forcing it out of the organization, by committing the country once and for all to an oil policy predicated on high volumes and low prices. This strategy is consistent with goals of the International Energy Agency (IEA), which was founded by the consumer countries in the early 1970s in order to confront OPEC. Indeed, Andrés Sosa Pietri, PDVSA president in the early 1990s, has consistently advocated Venezuela's withdrawal from OPEC and its membership in the IEA.

The Chávez government had to confront this situation. The practical compromise has been to include syncrude in the OPEC-quota, but not Orimulsión. Nevertheles**s,** the recent cuts in production (2001) are causing very substantial and disproportionate losses in fiscal revenues.

Lower prices, however, would even be worse. Leaving OPEC is not an option the Chávez government is about to consider.

Apertura in the Context of Neoliberal Policy after 1989

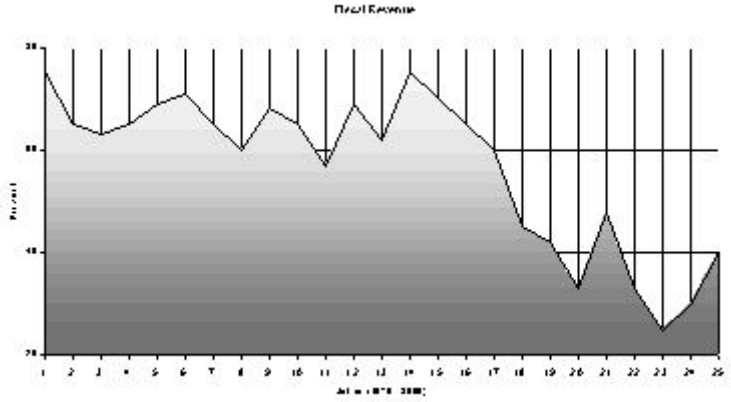
In 1988, Pérez was elected President for a second term, but he faced a totally different situation than fifteen years earlier. Notwithstanding the oil price collapse in 1986, the preceding administration of Jaime Lusinchi had carried on spending as usual. Thus, at the time Pérez took office in February 1989, the Central Bank was left without foreign reserves. Pérez immediately accepted agreements with the International Monetary Fund and the World Bank that included an increase in domestic gasoline prices. Pérez now promised a 'Great Turnabout,' which came as a surprise to the Venezuelan people who had never been told that there was anything fundamentally wrong with the economy in the first place. Indeed, an increase in gasoline prices, reflected in higher transport fares, sparked the *Caracazo* of the week of February 27, 1989.

Pérez also began to allow private investors back into the Venezuelan oil industry. As part of the *opening* of the Venezuelan economy to the outside world, PDVSA was put in charge of the *Apertura Petroler*a. The role of MEM, which prior to nationalization had overseen contractual and fiscal relations with oil companies, was reduced to rubber-stamp status. PDVSA preached the gospel of competitiveness to the government, arguing that royalties and taxes would have to be lowered to attract foreign investors. The government followed its advice. In addition to the aforementioned joint ventures for extra-heavy oil, PDVSA opened 'marginal' fields producing conventional grades to private investments (arrangements known as 'operating services agreements'), which by 2001 accounted for about 500 thousand b/d. The greater part of this oil is not subject to OPEC quotas, and is low-taxed. In the process, the higher-taxed production of PDVSA was cut. Moreover, in these agreements PDVSA acts as an 'umbrella' shielding private capital from the state, guaranteeing that the state company will pay an indemnity to its 'partners' if there is any 'detrimental' legislative change. These contracts were made subject to international arbitration, an arrangement Venezuela had never accepted until then. Last but not least, in case of disputes PDVSA exports are subject to sequestration. Nevertheless, Congress approved all of them.

Having acted on behalf of private foreign investors, PDVSA also insisted on lower taxation for itself as well. Its best opportunity came in the chaotic year of 1993. President Pérez was removed from office, mainly as a consequence of the two coup attempts in 1992. A very weak provisional government took over and accepted a new Income Tax Law with generous allowances for inflation. In addition, the government's power of discretion over the export levy, which had been created in 1970 to allow capture of extraordinary profits in periods of high prices, was phased out, and finally abolished in 1996. These measures contributed to a significant drop in fiscal revenue from oil.

Figure 7.1

Fiscal Revenue from Oil as a Percentage of Gross Income from Oil



Div. Source: Ministerio de Energía y Minas: *Petróleo y otros datos estadístico*s. (Caracas: 2001)

(graph on p. 211)

Statistics put in evidence the government's declining share of oil income. In 1981, gross income from hydrocarbon production, including refining, peaked at $19.7 billion. In 2000, a new peak was reached of $29.3 billion. Nevertheless, in 1981 PDVSA paid $13.9 billion in fiscal revenues, but only $11.3 billion in 2000. In other words, for every *dollar* of gross income, PDVSA paid 71 *cents* to the government in rents, royalties and taxes in 1981, but only 39 *cents* in 2000. Moreover, government revenue derived from syncrude production coming on stream in the near future will be substantially lower. Thus the trend of falling fiscal revenue is bound to continue.

The End of the IV Republic

In the general elections of 1998, the two subversive movements – one led by PDVSA executives and the other by elements in the military – confronted each other (Arrioja 1998; see also Hellinger's chapter in this volume). PDVSA had become powerful enough to play a high-profile political role, and its leadership was convinced that the time had come to implement fully its *liberal* agenda. Liberalism, in the context of international oil politics, is to be understood in its original revolutionary conception based on replacing the visible hand of the landlords with the invisible hand of the market. Like their forbearers, today's liberals would reduce the power of 'landlords' (i.e., sovereign nation-states) to restrict access of capital (i.e., international corporations). It is this restriction on access that is the basis for the landowner, private or public, to collect a rent. The goal for liberals is 'land to the tiller,' or, to be more precise, 'minerals to the miner'. They want natural resources considered a free gift of nature, freely available to the producing companies and consumers. 'Free' thus refers to elimination of the obligation to pay rent.

Is *Venezuelan* oil a free gift of nature to *international* producing companies and foreign consumers? PDVSA's liberal agenda answers this question with an unqualified 'Yes.' This view is antithetical to everything that Venezuelan oil nationalism has ever achieved, including the founding of OPEC and nationalization. It is imperialism in its most ancient of definitions: the conquest of foreign land and its mineral resources.

Not surprisingly, PDVSA enjoyed strong backing from the governments of the developed consuming countries as well as international oil companies. Their experts designed the changes in Venezuela's fiscal system following the example of the British North Sea, the most liberal oil-producing region in the world in terms of allowing capital free access to natural resources. PDVSA thus came to play an important role in bringing the country into a global world where the territorial state is supposed to have disappeared.

Venezuela joined the World Trade Organization (WTO) without reserving any special rights regarding its oil (in contrast to Mexico). According to the vision adopted by PDVSA, natural resources are an advantage in attracting investment, more than it is a leverage to promote national development. In contrast to earlier periods, the nation no longer should require foreign investors to transfer technology or to purchase needed components from national producers.

PDVSA argued that any insistence upon measures to maximize oil revenue would obstruct the free flow of much needed investment. If the paramount goal of the state as owner of natural resources is to attract foreign investment, then the more investment the better. Hence, the lower the levels of taxation and the more flexible the fiscal regimes, the better. Consequently, the fiscal revenue maximization policy of the past was replaced with a policy of *minimizatio*n. In February 1998, it seemed very likely that independent candidate Irene Sáez would easily win the elections and that PDVSA would play a central role in her government. Venezuela was on the brink of becoming Latin America's model pupil of natural resource-liberalism and globalization. A nation that had played a key role in founding OPEC, the epitome of an organization dedicated to strengthening national sovereignty over exhaustible natural resources, was now to become a leader in dismantling what had been achieved within the OPEC framework.

Then, to spoil it all, Chávez turned up as a popular candidate. The small political groups that had opposed PDVSA's liberal oil policy supported Chávez, although he had no specific agenda for oil beyond a more or less vaguely formulated commitment to follow a nationalistic approach. He and his followers were still unaware of subversive oil, but one thing was certain: his victory would at the very least slow down the implementation of the liberal agenda. And there was nothing the PDVSA leadership and the traditional political parties could do about it. Desperate, AD and COPEI joined in a last minute common electoral front, but to no avail. During the electoral campaign Chávez moved steeply and inexorably upward in the opinion polls as world petroleum prices moved downwards. PDVSA had been publicly boasting about never again cutting a single barrel of output. It was already no longer a question of extra-heavy oil not being subject to OPEC quotas, but to put an end to the quota system *per s*e. Even the formidable public relations machinery of PDVSA – which contended that lower prices would secure more markets for Venezuela with the overall balance being positive – could not convince the country that falling prices was good news, try as hard as it might.

The V Republic

Hugo Chávez took over the Presidency in February 1999 in the middle of the worst price collapse in world petroleum markets in over fifty years. The situation, however, soon turned around radically and favorably, and there is no doubt that the Chávez government played a crucial role in the recovery. The last government of the *ancien régime* had come close to abandoning OPEC. PDVSA's publicly heralded policy to maximize volume in disregard of OPEC quotas and price objectives was a major cause of the 1998 oil price crisis. Even the Caldera government, which had shown little resistance to PDVSA initiatives, had to reverse its policy, and in its last months agreed to new OPEC quotas, but at home a weakened MEM was unable to impose them. Had it not been for the victory of Chávez, PDVSA would have been

transformed into little more than a licensing agency, and the privatization of its subsidiaries would have been the inevitable outcome.

President Chávez and his oil minister, Alí Rodríguez Araque, reversed the policy of spurning OPEC quotas, and began to defend prices. Together with Mexico and Saudi Arabia, Venezuela successfully promoted a new understanding on quotas between OPEC members and other exporting countries. Venezuela also promoted and hosted in September 2000 the second summit meting of OPEC heads-of-state. Prices recovered.

The gross proceeds from hydrocarbon exports peaked at $29.3 billion in 2000. However, price was only one aspect of oil problems confronting Chávez. His other task was to find a way to arrest the fall in fiscal revenues due to long-term structural and legal problems that may also be extremely difficult to redress.

Re-Gaining Control of the Nation's Natural Resources

As soon as Rodríguez Araque took over the Ministry in 1999, he began to implement a policy aimed at asserting control over natural resources and fiscal policy. Rodríguez Araque opposed the previous government's decision to leave the negotiation of upstream contracts to PDVSA. At the heart of the issue of formulation of fiscal policy is the question of royalty, which is the most secure form of revenue for the owners of natural resources (Mommer 1999). The virtue of royalties is the ease with which they can be collected, as there are only two variables involved: volumes and prices. Unlike in the case of income tax, they are immune against the manipulation of production costs. For that very reason PDVSA wanted the royalty scrapped; in its place it was willing to accept increased income tax rates on highly profitable fields (Espinasa 1998). The problem with this proposal is that effective collection of income taxes is more difficult to achieve, especially for a state whose bureaucratic capabilities were declining. The Venezuelan government, as we have seen, was struggling just to measure and control volumes and prices. Although only partially successful, MEM, under the direction of Rodríguez Araque began to monitor the volumes produced in some fields and rejected 'transfer prices' (prices charged by PDVSA to its foreign affiliates) as the basis for calculating royalty payments. PDVSA was thus obliged to pay royalties on the basis of international market prices. However, the Ministry of Finance continued to accept transfer prices in calculating what the company had to pay in income taxes.

Under Rodríguez Araque, MEM also redesigned the terms of contracts for natural gas, which had been in preparation when the new government took over. A new Natural Gas Law, enacted in 1999, established a minimum royalty rate of 20 percent, and in practice they reached as high as 32 percent. At the same time, this sector was completely opened up to private investors. A new Organic Law of Hydrocarbons, enacted in 2001 – drafted by Álvaro Silva Calderón, who succeeded Rodríguez Araque as Minister (Rodríguez Araque became Secretary General of OPEC) – establishes a minimum royalty rate of 30 percent for oil (with some downward-flexibility to 20 percent for conventional oil, and to one-sixth in the case of extra-heavy oil). At the same time, the law lowers income tax on conventional crudes from 59 per cent to 50 per cent; for extra-heavy oil the tax rate remained at 32 per cent. All in all, there is an increase in taxation based on the increase of royalty rates. The law also reserves for the state majority shareholding in any joint venture for exploration and production.

The new Hydrocarbon Law will apply only to new licenses, concessions, and contracts. Under existing arrangements, private companies will continue to pay less in royalties and taxes for access to Venezuela's highly profitable petroleum deposits than they pay for leases in marginal fields in the U.S. Indeed, since 1993, even PDVSA pays less in royalty and taxes than private oil companies in Alaska (Mommer 2001b).

Controlling PDVSA

The Ministry under Rodríguez Araque and Silva Calderón hoped to force PDVSA to spend less and to pay more taxes. This goal will not be easy to achieve. In late 2001, the Ministry remained in the hands of officials belonging to two small parties, *Patria Para Todos* (PPT) and *Movimiento Electoral del Pueblo* (MEP). Their weak status was further eroded when both parties lost their small representation in the National Assembly in the general election of 2000. Hence, the Ministry lacked political support in the legislature, whereas PDVSA continued lobbying Chávez's MVR. In November 2000, PDVSA convinced the Committee of Energy and Mines of the National Assembly to declare publicly its intention to promote legislation in favor of lower royalty rates. This was the very day an Enabling Law was approved, according to which the government was authorized to do exactly the contrary – to raise royalties. The latter position prevailed at the governmental level, but it is unclear whether it will be defended in the National Assembly. PDVSA's president General Guaicaipuro Lameda publicly criticized the new Organic Law of Hydrocarbons for increasing royalties. In February 2002, President Chávez dismissed Lameda and appointed in his place Gastón Parra, a University teacher with a strong nationalist background in line with the MEM.

At first glance, the new Constitution also appears to reinforce sovereign ownership of oil, but in reality the liberal agenda of PDVSA fared well in the Constituent Assembly. According to the new Bolivarian Constitution, PDVSA, which is in reality a *holding* company, cannot be privatized, but this restriction does not apply to its *affiliate*s. PDVSA, unlike its affiliates, does not produce a single barrel of oil. Most Venezuelans believe that the Bolivarian Constitution has actually strengthened nationalization, but ironically it may have paved the road for the transformation of PDVSA into a liberal licensing agency for a private industry.

In the year 2000, costs and expenditures of the company increased by a staggering 44.6 percent as reported officially by PDVSA. This is mainly explained by the *Apertur*a's operating services agreements with private companies, which were designed to be flexible enough to allow the company to produce very high-cost (and low-taxed) oil. PDVSA's costs now passed the ten-dollar-per-barrel mark. PDVSA also stuck to its old policy: whenever OPEC quotas limit the possibilities of investing its revenue in Venezuelan oil production, it is spent abroad. PDVSA continues to expand into the refining and retail business, but now all over Latin America and not just the U.S. and Europe.

The two businesses of oil – the business of the investor, on the one hand, and the business of the natural resource owner, on the other – were easy to distinguish as long as the first was in the hands of foreign investors and the latter was vested in the government of the nation. Institutionally, MEM represented the latter. With nationalization in 1976 the two businesses became completely confused. If anything, nationalization required stricter and more clear-cut fiscal control on the part of the state, but the opposite happened. Fiscal control became more and more relaxed over the years, and control of the company by its single shareholder – the state – really never worked. The Ministry wields no power of its own over the company because the President appoints all of its directors. They are peers of the Minister. The only real shareholder is the President, with virtually no institutional or structural support. PDVSA always advanced the same argument for relaxation of state control: the need to strengthen the national oil company, which was the pride of the nation, and to enhance its competitiveness. In fact, the company acted according to the maxim that it was always better to spend a dollar than to pay that dollar in taxes. Investment was a matter of principle, not a question of maximizing profits. Greater production at lower prices was always considered a better option than defending prices by limiting supply. Hence, PDVSA, contrary to its public claims, does not act as a commercial enterprise. It does not maximize profits (which might be converted into dividends for the

government), but rather volumes all the way down the line, from production to refining, transport and retail. Along the way it clears away profits from its Venezuelan accounts through the practice of 'transfer pricing' (Boué 2002).

To control PDVSA effectively again, the new Hydrocarbon Law requires the company to present accounts properly, separated according to its different activities. It should thus become evident where profits are made, and where they are not, a *sine qua non* for any rational oil policy. PDVSA's opaque accounting methods are designed to hide discounts in their transfer prices as well as their deliberately inflated cost. For example, PDVSA transfers an important part of the costs of its internationalization program, including the service of its ten billion-dollar debt, to its Caracas headquarters. In many ways PDVSA has even lost control over itself, most notably regarding its internationalization policy. The company has structured itself in the course of many years to prevent its shareholder (the state) from interfering. In doing so, it has made itself increasingly difficult to steer.

Concluding Remarks

PDVSA turned its back to nationalization as early as 1983 with its policy of 'internationalization'. By 1989, it actually no longer claimed to be a national but a global company. Indeed, the gist of its message is that globalization requires elimination of national barriers to investments in the area of natural resources. As odd as it may seem, there is strong public support for this approach – whereby PDVSA aligns itself with the international oil companies and consumer countries – among Venezuelan professionals and the middle class in general. Until nationalization, it was clear to *all* Venezuelans that higher fiscal revenues in oil generated material well-being for the entire population. After nationalization, however, the validity of this thinking was questioned due to the appalling performance of the political and economic system. Hence, to bring PDVSA again under fiscal control may be much more difficult a task than one might imagine.

A large part of Venezuela's professional classes support PDVSA's reasoning that higher volumes are more important than defense of prices. Completely in the dark about oil policy (Baptista and Mommer 1987), and under the influence of PDVSA's public relations department, they are not likely to challenge the neoliberal logic. They seek a decent professional working environment in a modern (private) company and, of course, a decent salary, all of which the IV th Republic was no longer able to offer. They do not believe that the V th Republic can offer it to them either. They thus believe that privatizing PDVSA would better their prospects. At a popular level, however, the outlook is quite different. The underprivileged sectors of the population fear that they will be excluded and left behind if the nation were to privatize the oil industry. Hence, oil policy has been caught up in the general process of polarization that characterized the country in early 2002.

The whole country has been spellbound since nationalization. One government after another has concentrated all of its attention on PDVSA and forgotten about the MEM. One President after another has spent many hours in PDVSA; not one has set foot in the Ministry of Energy and Mines. The latter was progressively dismantled, and most of its best-qualified personnel lured away to PDVSA. MEM has fallen prey to physical decay, its workers impoverished together with other public employees. PDVSA moved to fill the gap in the heyday of *Apertura Petrolera* by paying a monthly bonus to employees of the Ministry working in the hydrocarbon section (a continuing practice), effectively doubling their paltry salaries. Today the budget of PDVSA represents no less than 40 percent of public spending. PDVSA's financial leverage extends deep into the world of politics, journalism and public opinion making in general, where people are easily convinced to work for PDVSA as part-time public relations consultants -- not to speak of

the international consultant companies which have established themselves in Caracas after the initiation of *Apertura Petrolera* in 1989.

In short, PDVSA was transformed into a 'state within the state' a long time ago, becoming more powerful the more the country became impoverished. Under the Chávez government this trend has been reverse**d;** as a result, the country has made significant progress in recovering control over its most important natural resource. In achieving this goal, however, the government failed to win over PDVSA's top personnel. Today, company executives are no more willing to co-operate with the Vth Republic, as they were with the IVth Republic.

These conclusions were fully confirmed by the April 2002 events in Venezuela. The failed coup left behind a highly fluid situation, and it left unsettled the ultimate fate of oil policy. Alí Rodríguez Araque, who at the time was serving as Secretary General of OPEC, agreed to take over the presidency of PDVSA as a candidate of a political consensus -- at least as far as a political consensus was possible in Venezuela at that time.

Rodríguez faced the task of carrying out a systematic reform of the oil sector for the first time since nationalization. The Chávez administration will have to demarcate the three roles of the state, politically and institutionally: as the sovereign generally, as the owner of the natural resource, and as the sole shareholder of the company. At the same time, it will have to define a new role for the private sector, national and foreign. Given the instability of Venezuelan politics, success remained very much in doubt.