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WASHINGTON, D.C. 20240

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14 November 1973

MEMORANDUM FOR THE RECORD

Subject: First Session of Drafting Committees, 14 November 1973

Mr. Wilson opened the first session at 1400, 14 November 1973 with an explanation of the framework for the U.S. proposal on finance.

He stated that there were significant conceptual differences between the JCFS draft proposal and ours. In the U.S. draft emphasis was being placed on the goal of economic self-sufficiency in line with the statements of members of the JCFS delegation. This was also in line with the objectives contained in the U.N. Trusteeship Agreement and the stated goal of the Congress of Micronesia.

In examining the question of proper orders of magnitude, we have given recognition to the Congress of Micronesia's own desires to reduce the expense and complexity of running the government by eliminating or decreasing the numbers of expatriates, simplifying government operations, and decentralizing operational responsibility to districts.

The proposal is therefore in line with the concept of economic self-sufficiency and a gradual decline in the amount of budget support. We would be willing, alternatively, to see the amount of budget support held at a constant figure over the years. But in that event the annual amount would be smaller than the starting amount in the proposal under consideration.

Another consideration in reviewing the financial assistance package is the nature and closeness of our relations - the closer the relationship, the more liberal the financial contribution.

Section 104(c) provides that the payments for lands leased to the U.S. will be included within the budget support figure. We believe that these amounts need not be very large-especially since part of the payment is for options rather than actual use.

Under Section 402 we recognize the need for continuation of an economic development program for economic and social infrastructure. We are prepared to provide funds on a grant basis for this purpose. We also agree with the desirability of setting up district economic development funds for loans to small entrepreneurs. We are prepared to provide financing for such funds through long term low interests loans to the districts.

The U.S. Government's Agency for International Development and the World Bank, among others, have demonstrated the usefulness of the loan arrangement as a means of spurring economic development. The loan procedure has the quality of being a more acceptable form of economic aid in the U.S. Congress and a form of aid that tends to elicit a higher degree of internal self-discipline in the aid receiving country in the use of the funds than if the funds were provided on a grant basis.

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In considering the amount of funds required for essential economic development, we should take into account other potential sources of financing -- both grant and loan. The Government of Micronesia (GOM) will have access to funds and technical assistance from the U.N., the Asian Development Bank, and World Bank, etc., in addition to assistance received from other countries. Additional income can be anticipated as well from foreign investments. The U.S. is studying a revision of present policy now, and after the trusteeship ends this will be entirely up to the Micronesians to control.

Section 404 provides for periodic regular reviews of the financial levels in light of changing conditions -- including such things as changes in the economic situation in Micronesia, as well as possible inflation and movement of the dollar -- up or down.

This, in broad outline, is the proposed concept and formula for extending U.S. financial assistance. In dealing with the question of levels, we started from the current level of government expenditures as a base point and have considered the pattern of both operational and economical development funding over the past several years.

Mr. Silver was then called upon to describe the methodology for determining a justifiable and proper aid level. He distributed a paper which represented the results of his research in this area (attached). He drew attention to Table II, which showed the FY 1973 budget expenditure figures for district government operations. This totalled some \$23 million.

He then proceeded to Table III, which reflected certain centralized expenditures (Congress of Micronesia, Judiciary, Community College, Nursing School, Auditing function, etc.) which had to be added to the district government figures to arrive at a total government expenditure requirement after the change in status.

Mr. Silver then drew attention to Table I, which was a recapitulation of the information in Tables II and III and went on to derive a budget deficit figure, taking into account (a) that the proposal covered five districts rather than six; (b) the Congress of Micronesia wanted a more streamlined government; (c) there would be some internal revenue from local taxes and fees. The net result was a \$22 to \$23 million deficit that would provide the starting point for a decision on levels of budget support.

With respect to CIP levels, Mr. Silver said that the current projections were running at about \$10 million a year on the average - some years a little higher, some years somewhat less. But we should take into account that the CIP levels could be expected to tail off after a while as the priority project list became exhausted.

After Messrs. Wilson and Silver had presented the U.S. proposals under Title IV (Finance), Mr. Warnke, on behalf of the JCFS, commented as follows:

The gap between the amount of assistance being requested by the JCFS and the amount offered by the U.S. (Warnke estimated the total U.S. package at \$35 million) is so wide as to suggest it may be unbridgeable. The "cardinal point" in the discussions on finance will center on whether the gap can in

fact be bridged. The JCFS, of course, will ultimately have to make recommendations to the Congress of Micronesia regarding whether there exists sufficient basis for an agreement on future status. A failure to reconcile this financial gap could conceivably cause the COM to abandon the negotiations.

The JCFS request is more consonant with Micronesian needs than is the U.S. offer.

Assuming that there were some agreement on a "ballpark" figure for total U.S. assistance, there would still be some details to reconcile in the two differing approaches to providing assistance to Micronesia. Some of these differences are significant, but most could probably be easily accommodated. Some of these other issues are:

1. The Joint Committee's charter specifies that it is to negotiate for all six districts of Micronesia. The JCFS has no latitude or choice in this regard. The people of the Marianas must have the same opportunity as the people of the other districts to decide whether the status agreement being negotiated here is acceptable to them. U.S. payments for military land use in the Mariana Islands must be considered as part of the package the U.S. and the JCFS are negotiating.

2. There are some basic problems in trying to break the U.S. assistance figure down into different categories as, for example, in the U.S. draft's Section 401(a), (b), and (c). In any case, (c) should be deleted, since it would create a special problem for the GOM. It would create a conflict of interest for the GOM by placing it in an adversary relationship vis-a-vis the landowners holding the land the U.S. wishes for military purposes. That is, the GOM would be expected to help negotiate for the land to fulfill the terms of the compact, but it would know that every dollar which the U.S. paid to the landowners would mean one dollar less for the GOM to manage its programs.

3. It is inappropriate to include all the language in 402(b) in the compact as now written, because the stipulations regarding loans would be in derogation of GOM authority. We should retain only the first part of this section. In any case, this suggested change is non-substantive, since it is understood that before the U.S. would loan the money in question there would have to be an agreement on loan terms between the GOM and the U.S.

It is puzzling to hear the U.S. Delegation say that the quantum of U.S. assistance should relate directly to the closeness of the Micronesia-U.S. relationship. There is nothing in what has been negotiated to date which would warrant the U.S. giving Micronesia any less financial assistance than Micronesia genuinely needs -- i.e., the amount for which it is asking. The Compact titles on defense and foreign affairs vest very substantial authority in the U.S. Government. What more does the U.S. mean to suggest that it wants -- authority over Micronesia's internal affairs? That, of course, is unacceptable. As it is, the U.S. is getting a lot for its money.

The U.S. will be able to preclude other countries using Micronesia's land and waters, and the U.S. will perhaps have land use options in Micronesia. The arrangements negotiated to date have the U.S. everything it wants from the standpoint of security. (Later, when Mr. Wilson noted that the U.S. Congress and the American people would not think that the U.S. should pay specifically

for the right to provide for Micronesia's defense, Mr. Warnke said that it was U.S. security interests in the Western Pacific that the U.S. is concerned about, not Micronesian defense needs. Warnke said the Micronesians do not think they need defending).

Warnke asked how we can ensure that the arrangements finally negotiated for U.S. financial assistance will be implemented beyond the first year of a compact. What if the U.S. Congress initially refuses to commit funds beyond one year and then subsequently refuses to commit further funds? Perhaps the Compact's termination clause will have to specify that if the financial terms of the compact are not kept, the agreement will lapse. Mr. Wilson acknowledged that there would be a real problem if the U.S. Congress failed to act, but our consultations gave no indication this would happen. If it should, however, it would clearly be a breach of the compact.

Warnke considered inappropriate the U.S. Delegation's approach to calculating Micronesia's financial needs. He argued that it is inadequate to use as one's starting point for such calculations the TTPI Government's budget projections over the next few years. The new GOM will want the Micronesian people to have a far better standard of living than they now have under the present administration's minimal, inadequate program of financial outlays. Actually, the \$100 million annually for which the JCFS is asking is a conservative figure. The islands' needs are in the neighborhood of \$125 million per year. The JCFS recognizes that it is important to develop an economic development plan as the framework for efforts to move Micronesia toward self-sufficiency. The JCFS is working on such a plan now, and will shortly present estimates of Micronesia's financial needs to the U.S. Delegation. Reaching self-sufficiency is the goal. The Micronesians are hopeful that this could be accomplished perhaps within ten years, i.e., by the time the two parties would, under the JCFS formulation, review the provisions of the compact.

Mr. Wilson began his response to Mr. Warnke's comments by citing comparative figures on the amounts of financial assistance currently being received by countries which are in a relationship with their political/economic sponsors somewhat resembling the free association relationship the U.S. and Micronesia are negotiating. He noted that Gibraltar receives about \$97 per capita per annum from Great Britain, the British West Indies about \$33 per capita from Great Britain, and the Cook Islands about \$96 per capita from New Zealand. He said that U.S. assistance to Micronesia of \$100 million annually would come to \$1000 per capita, almost certainly the world's highest assistance figure by a considerable margin.

In response to Mr. Warnke's questioning how there could be a U.S.-Micronesia relationship closer than the one envisaged under free association, Mr. Wilson said that when the two sides first began discussing future status, some consideration was given to a closer U.S.-Micronesian arrangement than the one now being negotiated. He also noted that a compact of free association with a termination clause implies the possibility of less permanency and therefore connotes less closeness than other possible relationships.

Commenting on Mr. Warnke's remark that the U.S. seeks to protect its own security interests in Micronesia rather than any defense interest of Micronesia, Mr. Wilson noted, inter alia, that the U.S. has security and peacekeeping responsibilities in the Western Pacific which it will continue to fulfill and

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said that, as a matter of policy, the U.S. does not pay to other governments compensation for denying to third countries access to their lands and waters for military purposes.

The U.S. delegation was not constrained to agree on the issue of conflict of interest that the scheme proposed would do anything of the sort. Other governments seemed to handle both chores without feeling such qualms.

The session adjourned at 1530 with agreement to meet again at 1000, 15 November 1973.