

**Testimony of the Honorable Phillip H. Muller,
Minister of Foreign Affairs,
Republic of the Marshall Islands.
Presented to the Subcommittee on Fisheries, Wildlife, Oceans and Insular
Affairs of the House Committee on Natural Resources**

Chairman Fleming, Ranking Member Sablan, Members of the Subcommittee, Ladies and Gentlemen:

INTRODUCTION

On behalf of His Excellency President Christopher J. Loeak, I wish to thank you for convening this hearing on GAO's Report entitled *Compact of Free Association: Micronesia and Marshall Islands Continue to Face Challenges Measuring Progress and Ensuring Accountability*.

The relationship between our peoples goes back more than a century and a half to the days when American whalers visiting our waters came ashore at numerous islands seeking to trade for fresh fruit and other local delicacies. If the nature of our relationship had been based only on those encounters, perhaps we would not be here as friends today. But within less than a decade, American missionaries arrived in their sailing ships to bring Christianity to our people. Marshall Islanders have always been forgiving and the teachings of the Bible reinforced that trait in our ancestors of that era.

More than two-thirds of a century ago, many of our people came in contact with U.S. soldiers and other military personnel as they passed through these islands seeking to bring an end to hostilities that had plagued the whole world. For many years, the different dates that American troops arrived at various atolls in the Marshalls have been marked on the calendar every year and observed as days of great significance across both the Ratak and the Ralik chains.

Immediately following World War II, the U.S. used the Marshall Islands to begin learning more about the effects of the atomic weapons which it had ultimately used to end that tragic era. As the race to develop the ultimate bomb accelerated, the U.S. again used the Marshall Islands to detonate the world's first hydrogen bomb, establishing a new level of power far beyond atomic, namely that of the thermonuclear weapon. Over the following six years, these islands were the sites of seventeen more multi-megaton level nuclear explosions. The largest atom bomb tested in Nevada, code-named Sedan, had an explosive yield of just one-tenth of one megaton.

Just over one-third of a century ago, our Republic was established when the people of the Marshall Islands approved a formal Constitution and began to take responsibility for governing our nation. And just over one-quarter of a century ago, our relationship with the U.S. was formalized under the Compact of Free Association.

In a video to Micronesians to commemorate our acceptance of that relationship, President Ronald Reagan said that he welcomed our "new status in the world as a sovereign nation" and added "But you will always be family to us."

RMI ACCOMPLISHMENTS: 2011--2013

In discussing the GAO Report on measuring progress and ensuring accountability under the Compact, it is imperative that this be done against the backdrop of some of the accomplishments of the Loeak Administration, which took over the reins of the RMI Government only two years ago.

The Government continues to work on our National Strategic Plan (NSP), which will provide a framework for the planning and coordination of the RMI's priorities and objectives. The NSP will be used as the roadmap for development and progress in the medium term (2014-2016) and will be continually updated for use in meeting longer term objectives as the RMI moves towards 2023 and beyond. It will be the first time the RMI will have such a framework.

Education and health continue to be top priorities for the RMI. Prior to the iteration of this fact in the amended Compact, our Constitution guarantees education and health for the Marshallese people in the Bill of Rights. Significant steps to improve and expand these Education priorities have been taken by the RMI with the aim to enhance the knowledge and skills of our students and provide more training opportunities. One such step is the passage by the *Nitijela* of the Education Bill to establish an autonomous public school system. Another step is accelerating the training and certification process of Marshallese teachers, including plans to retain them through augmented salaries and an improved working environment. Moreover, the primacy of education programs is reflected in RMI's fiscal priorities with the Ministry of Education being the primary recipient of Compact funding. All of these measures demonstrate the Government's ongoing efforts to ensure our children obtain the education they need so as to do their part in advancing the RMI.

While the number of Non-Communicable Diseases (NCDs) is on the rise, there are various reasons for this, including better screening through numerous community health outreach efforts. I want to stress that the Government continues to develop its ability to address these challenges. The Ministry of Health (MOH) has recently completed a strategic plan, the implementation of which is imminent. MOH is also currently working with some of our Non-Governmental Organizations in addressing NCDs. Other partners that have assisted MOH in providing health care assistance were the 2013 Pacific Partnership Mission, the Flying Doctors of America and Canvasback. The World Health Organization, Pacific Islands Health Officers Association and Centers for Disease Control and Prevention also provide tremendous financial and technical assistance. As with education, the RMI also allocates a large portion of its Compact funding towards the health sector. For example, the Government used Compact assistance to purchase a boat, *Ejmour II*, which has allowed for more frequent health mobile team visits to secluded outer-islands.

The Government has also made great strides with respect to improving transportation. Under a grant from Japan, the RMI recently received two ships, *MV Majuro* and *MV Kwajalein*, to expand domestic transportation for people and goods throughout the RMI. Another ship, *MV Tobolar*, is also in operation to improve services towards the copra industry. *Air Marshall Islands'* Dash-8 received a major overhaul in Australia earlier this year, and as a result, air service to the outer islands has significantly improved. *Our Airlines* has assisted with

international transportation, namely Majuro, Fiji and Brisbane, and will provide more opportunities for travel.

Throughout the history of the nuclear legacy, the United Nations was not involved in the nuclear issue despite it having entrusted administration of the RMI to the U.S. under a Trusteeship; despite the cumulative impact of the 67 nuclear detonations in the RMI from 1946 to 1958 being equivalent to 1.6 Hiroshima bombs dropped every day for 12 years; and despite passing UN Resolutions 1082 and 1493 in 1954 and 1956, respectively, essentially rejecting two petitions submitted by the Marshallese people to stop the nuclear testing. A *United Nations Special Rapporteur* provided his report last year to the Human Rights Council (HRC), which considered for the first time environmental and human rights impacts resulting from the nuclear testing. Recommendations were provided in the report, which were supported by the RMI and, through New Zealand, by Forum countries. I spoke on behalf of President Loeak at the HRC, and I would like to reiterate that we must move beyond the accusations and the international silence towards real actions to fully resolve these issues surrounding the nuclear legacy.

In early September, the RMI hosted the 44th Pacific Islands Forum Leaders' meeting where leaders from countries in the Pacific Region, including Australia and New Zealand, discussed issues of mutual interest and opportunities to advance the region. With the theme "Marshalling the Pacific Response to Climate Change", the Majuro Declaration for Climate Leadership was the meeting's signature outcome. I want to stress that during the preparations for this important meeting, the RMI experienced two climate-induced disasters: an extreme drought in the northern part of the country, and wave inundations in southern RMI. Our determination to continue with plans to host the meeting along with our responses to the disasters were assisted by the international community, and it is my pleasure to say that the U.S. was one of those countries.

RMI-U.S. RELATIONSHIP

Although this relationship has come a long way, there is no doubt that our countries must continue to look for more opportunities to further strengthen our close and unique ties. I want to raise and put forth for the record some of these opportunities.

Beyond the Compact

The RMI-US relationship goes beyond the spirit of cooperation outlined in the Compact. In the twenty eight (28) years since the original Compact, the RMI and U.S. have confronted many regional and international issues together. Our mutual cooperation has led to a more secure Northern Pacific region, and our common principles for democracy and freedom assures the U.S. an ally in the global war on terrorism. Our voting record at the United Nations speaks volume to our commitment to this relationship. We consistently support the U.S. in casting very tough votes even if it is not the most popular thing to do. In the end, we believe we are contributing to the greater good and security of the world.

My Government is very pleased to know that the U.S. Government is keen on being a major player in the Climate Change discussion. The RMI is situated about a meter above sea-level - thin coral atolls so narrow you can stand in the lagoon and see across the land to ocean waves on

the other side. We stand on the close edge of global progress - or failure - to address climate change. We are only the very first soldiers of a much greater, and common, global struggle; not just to preserve the environment but to address our collective international security.

Earlier last year the RMI addressed members of the UN Security Council – just as we emerged out of UN Trusteeship, our very statehood and future is again in the hands of the international community. Urgent action must be taken, but it appears that we are only into finger-pointing. During the Development Partners’ Dialogue at the Forum Leaders’ meeting, I am pleased that the U.S. and the EU, amongst others, signed up to the Majuro Declaration on Climate Leadership. More support is needed, and I urge the U.S. to assist in bringing more countries into the fold.

Compact Implementation: 5-Year Review

Regional and international cooperation aside, we come back full circle to the amended Compact and its implementation. As with anything that has many moving parts, there needs to be constant review of its performance to ensure that program delivery is optimized in the most efficient and effective manner. Under the amended Compact, the mechanism is the 5-Year Review.

Pursuant to Section 104(h)(2) of Public Law (108-88), the amended Compact provides for the U.S. Government to “review the terms of the respective Compacts and consider the overall nature and development of the U.S.-FSM and U.S.-RMI relationships”. The section further states that the RMI will have a chance to review and comment on the review with further follow-up by the U.S. President including “any recommendations for actions to respond to such findings.” Furthermore, this includes Section (E) of paragraph (1) which allows for “recommendations on ways to increase the effectiveness of United States Assistance and to meet overall economic performance objective, including, if appropriate, recommendations to Congress to adjust the inflation rate or to adjust the contributions to the Trust Funds based on non-U.S. contributions.”

The first 5-Year Review has been done, and as we are in the 10th year of the Compact, the second review is overdue. To date, the RMI has identified key areas that need to be addressed to fully optimize the potential of Compact assistance. Although the RMI has already provided the following in our comments to the first 5-Year Review, we take this opportunity to reiterate them herein.

Full Inflation Adjustment

Limiting the inflation adjustment to just two-thirds (2/3) of the Gross Domestic Product (GDP) Implicit Price Deflator has had a negative impact for the RMI. This, coupled with the annual decrement of \$500,000 from the financial assistance from the U.S., is currently taking a toll on the RMI’s fiscal stability. The declining real and nominal values of the grant assistance is hindering our ability to fully maximize the potential economic growth for the Marshall Islands.

For example, from fiscal year 2005, the first year both the decrement and the partial inflation were applied to the base grant, today, the RMI lost approximately \$5.5 million (not including full inflation) in real value. This places significant pressure on the RMI to provide mandated

services without cutting essential elements in providing these services. If this situation does not improve, many of the essential services currently being provided by the Government will have to decrease or ultimately be cut.

Global economic conditions further exacerbate the effects of the partial inflation adjustment and the decrement to our fiscal situation. One example is the cost of petroleum. This single commodity has managed to ravage our energy sector, increase the cost of delivering vital services to our people, and has increased the operation cost of the Government, as a whole. Paying for fuel to ensure that lights are kept on and that ships are running on schedule has become more of a burden to our financial situation.

Full inflation adjustment is needed to assist the RMI in offsetting some of the impact caused by the decrement. Granting RMI the full inflation adjustment will limit the effect of the decrement on our financial situation in the short-term, and will give us ample time to transition to a fiscally stable state. We anticipate that when the decrement finally catches up to us, the shift will not be too extreme. Not doing so will force the RMI to make radical decisions that could potentially hinder our economic growth.

Trust Fund Sufficiency and Amendments to the Trust Fund Agreement

The amended Compact provides a provision for the establishment of the Trust Fund. The main purpose of this Trust Fund is to replace the revenue source currently provided under Section 211 of this agreement post-2023.

The last GAO report on the RMI Trust Fund calls into question the adequacy of the fund, much like reports by the International Monetary Fund, Asian Development Bank, U.S. Graduate School and Goldman Sachs. The RMI agrees with these assessments and urge the U.S. to work with the RMI to find a solution that will guarantee the sustainability of the trust fund. Our immediate concern is to facilitate a reasonable approach to maximize the potential and viability of the Trust Fund. Below are some possible solutions to this dilemma.

Extension of Grant Assistance

The initial delay in the establishment and investment of the Trust Fund puts the RMI at a disadvantage from the beginning. The Trust Fund Agreement requires an investment for a period of twenty (20) years, but because of the delay, the Trust Fund will have been earning income for only seventeen years. There were legal and administrative hurdles to overcome before the fund was invested.

To remedy this delay, the RMI would seek an additional three years of annual grant assistance to meet the conditions set forth in the agreement of a twenty-year investment and build up timeframe. Discussion on a base amount would have to happen to determine the appropriate level of grant assistance for the three-year extension. This amount would become, in effect, the benchmark for the annual proceeds from the trust fund.

Additional Contributors

The Republic of China (Taiwan) is the only subsequent contributor to the Trust Fund. Taiwan will provide \$50 million to the trust fund over the life of the build-up time period, making payments on a scheduled plan prescribed by our bi-lateral arrangement with the Taiwanese government. This is a major step as we try to give all the possible opportunities for the trust fund to become viable post 2023. The RMI is actively seeking other subsequent contributors to the Trust Fund, and I urge the U.S. to do the same.

Full Inflation adjustment for Trust Fund Contributions

Under the current trust fund agreement, contributions to the fund are not adjusted for full inflation. These contributions lose their real value each year it is not inflated to reflect its true value. We believe a full inflation adjustment to the Trust Fund contributions will help stabilize this fund, and provide adequate resources to the RMI post-2023.

Tax and Trade Compensatory Adjustment

The RMI is seeking remedy to the tax and trade report it submitted to the U.S. Government in September 2009. Pursuant to Section 111(d) of Public Law 99-239, the RMI could petition the U.S. Congress to allow for compensatory adjustments if the RMI could show adverse impact from U.S. Congressional changes to the tax and trade provisions in the original Compact. The 2009 report stipulated that the RMI had indeed lost potential revenue as a result of the enactment of the original Compact.

The report clearly shows that the RMI lost out on approximately \$245 million as a result of these changes. The U.S. Administration conducted its own study based on the RMI's submission, and concurred with our findings and recommended to the U.S. Congress to act on these findings. The Compact has authorized up to \$60 million to compensate the RMI and the FSM for these changes, and the RMI is awaiting the U.S. Congress to fully address this issue. I urge the Congress to act accordingly as these funds will be injected into the Trust Fund to ensure its viability as per Section 216 (b) of the amended Compact.

Supplemental Education Grant (SEG)

The idea behind having the Supplemental Education Grant (SEG) was to enable the RMI considerable freedom in designing and implementing our own educational programs to best fit our needs. This led to the RMI "cashing-out" of these federal programs to establish a similar system without the strict criteria in which many of these Federal Programs adhered to. The Compact, as Amended, authorizes \$6.1 million annually to fund these supplemental educational programs.

Our national Kindergarten Program is a primary beneficiary from this arrangement. This grant allows the RMI to formulate a universal pre-school program that caters to the learning norms in the Marshall Islands.

Though progress has been made with respect to the implementation of the SEG, there are still barriers to which we still need to overcome to fully appreciate the intent and purpose of the SEG. Moreover, while there have been some improvements in regards to the disbursement of the SEG, it is important to note that it remains a year behind.

To compound these problems, the SEG is not adjusted for the 2/3rd inflation provided in the Compact. The RMI has seen the reduction in the SEG since the second year it was made available to the RMI, and fears that this trend will subsequently lead to the RMI not being appropriated the SEG in future years.

The RMI requests this committee and the Administration to make provision that the SEG be made available to the RMI as a permanent appropriation and adjusted for inflation. This is an issue that could be corrected in the Compact mandated 5-Year Review. Doing so would greatly improve our ability to provide educational services to all Marshallese.

Joint Economic Management and Financial Accountability Committee (JEMFAC)

The Joint Economic Management and Financial Accountability Committee (JEMFAC) was established under the Compact, as Amended, to assist the RMI in monitoring and reporting on the use of Compact Sector Grants. Furthermore, the JEMFAC process is the mechanism used to allocate Compact funds. However, in recent years, it has, in our view, gone over and beyond its intended function to the point where it is straining our bi-lateral relationship.

This is exemplified by JEMFAC Resolution 2013-2, which required the RMI to re-do its Medium Term Budget and Investment Framework (MTBIF) and *Fiscal Management Model* so as to adhere to the 50/50 cost-sharing measures in the areas of utilities and housing for the education sector and the areas of utilities, housing and food for health sector. Given the make-up of the JEMFAC membership, the Resolution was adopted despite RMI's effort in decreasing the percentage to a more reasonable level, i.e. from 10/90 up to 25/75. 50% equated to \$2 million, which the RMI Budget Coordinating Committee had to take from other sources. It should be highlighted that the Resolution was adopted with the RMI JEMFAC members voting against it, the first time a JEMFAC resolution was not adopted unanimously since 2004. While increasing the budget for education and health, this Resolution decreased the budgets of other critical sectors such as transportation, amongst others, that directly complement our education and health services. As abovementioned, the RMI has 3 new ships to use for the 29 atolls and 5 islands widely dispersed throughout the country. Schedules will now have to be decreased to accommodate this Resolution.

The basis for this Resolution is the decrement plan. While acknowledging the efficacy of such a plan as a planning tool, the RMI is concerned about certain elements included in the JEMFAC Resolution 2010-1: *Long-Term Fiscal Planning*, that are no longer accurate. Firstly, as indicated in successive single audit reports, there is no long-term "unsustainable growth in government wage bills," and revenues are increasing significantly in many areas. Secondly, tax reform initiatives are on schedule and have broad-based political support. Moreover, commenting on subjective interpretations such as "apparent political obstacles" in any fiscal plan does not move the discussion further along with respect to more efficient tax administration, increasing

revenues or management of U.S. grants. Finally, economic activity is neither stagnant nor declining as evidenced in a recent report contracted by OIA. Noting these changed scope items from the decrement resolution, RMI believes the usefulness of a decrement plan is a policy guide and planning tool, not as a basis for imposing line-item expenditure ceilings, which seldom reflect broader policy goals.

During one of our virtual meetings to discuss the 50/50 cost-sharing measures, U.S. JEMFAC members provided a World Health Organization (WHO) Report showing that the RMI has the largest number of NCDs so as to further justify their position. Has the U.S. Government analyzed this Report to determine the cancer-related percentage of these NCD cases? Should we ignore the 500 excess cancers related to the U.S. Nuclear Testing Program originally reported by Nuclear Cancer Institute? If this is an annual report by WHO, with these excess cancers, I do not see how the number of NCDs for the RMI will decrease. Moreover, this is an opportune time to revisit the Changed Circumstances Petition (CCP) submitted in 2000 wherein the RMI argued that NCDs, given that they result from lifestyle choices, were indirectly caused by the U.S. Nuclear Testing Program through the 4 Atolls' Food Program under the Compact where USDA foods, mainly white rice and other processed foods such as luncheon meat, were provided to the people of the 4 Atolls. Rather than continuing with their traditional food and lifestyle, processed foods became a norm, resulting in an exacerbation of NCDs, such as obesity and diabetes.

Nuclear Claims Tribunal Trust Fund and the RMI Economy

A factor contributing to the under-performing economy in the RMI is the failure of the Nuclear Claims Trust Fund to attain the promised minimum rate of return of \$18 million per year, in perpetuity. The GAO correctly noted in 1992 that "the trust fund is not achieving the 12.5-percent investment returns expected when it was agreed on and may be nearly depleted when the 15-year term of required disbursements is completed". That report also correctly predicted that the trust fund would be depleted with the result that medical, personal injury, and property claim awards "remain partially unpaid." [Results in Brief section, GAO/NSIAD-92-229]

Had the Nuclear Claims Trust Fund been able to pay \$18 million or more per year on those awards, the contribution to the RMI economy would have created vastly increased potential for local private sector activity. That activity would have expanded the tax base and provided increased revenue for public services, including health and education. Instead, more than \$2.3 billion in compensation awards remains unpaid to thousands of Marshallese whose health and land were damaged by the nuclear weapons testing program. More than \$530 million of the unpaid awards total is for cleanup of radioactive contamination and restoration of land in the atolls of Bikini, Enewetak, Rongelap, and Utrik. That amount is above and beyond what the U.S. has already done in the way of cleanup or provided in the form of resettlement trust funds for those atolls. At the same time, there is a recurring need for the RMI to depend on Compact funding for such basic human services.

Single-Audit Reporting

As noted in the GAO report, RMI's unresolved prior year questioned costs totaled \$7.4 million at the end of fiscal year 2011. Before the commencement of the fiscal year 2012 audit, the RMI took several steps to better manage the audit fieldwork process and reduce prior year questioned costs. These measures included greater supervisory oversight and follow-through on missing procurement documentation and preliminary questioned cost citations. As a result, RMI was able to reduce its questioned costs in the fiscal year 2012 compliance report to a record low of \$35,000. Similarly, Ministry of Finance staff began a detailed examination of all prior year audit findings and worked closely with the DOI audit resolution official to obtain the necessary documentation to clear these questioned costs. DOI has now reinstated all questioned costs from Fiscal Year 2011, and the RMI is confident there will be timely resolution of all remaining prior year questioned costs.

Decrement Plan and Data Reliability

In 2011, and prior to the last JEMFAC meeting, the RMI provided 2 versions of the decrement plan, which did not meet the satisfaction of the U.S. JEMFAC members. Therefore, the RMI has invited the U.S. to hire a consultant who can develop such a document to satisfy their requirements. However, this is not sustainable, and with the Government's ongoing efforts to develop its NSP, ultimately counter-productive to the overall goals and objectives of the RMI.

In recognizing the issues surrounding data reliability, both the education and health sectors look forward to a joint evaluation of current indicators to improve and resolve any challenges that are apparent. It is the hope that once data reliability is improved, the ability to measure progress in health and education will no longer be a hindrance.

Energy Efforts

The Marshall Islands face great challenges in achieving reliable, affordable, and secure energy for power and transportation needs. Most of the islands are relatively small and geographically remote, wrestling for decades with their dependence on fossil fuels and the burden of high oil prices. Imported fuel is typically very expensive. The expense, volatility in price, and potential for disruption in supply of fuel has a significant effect on island economies. While the landscape of island energy planning and development has become more at the forefront of discussion, islands continue to struggle with various challenges. Most island communities have a relative abundance of renewable energy resources, but still remain highly dependent on imported fossil fuels to meet their energy needs. Although islands are faced with unique challenges, there are significant opportunities to build momentum and generate considerable sustainable results.

In the RMI, the goals in the National Energy Policy include 20% renewable energy generation by the year 2020 and improved efficiencies in generation, distribution, and end-user equipment. In addition to the government's goals, system reliability and the cost of energy are high-priority issues to RMI citizens and businesses, which are "bottom-up" drivers for energy sector changes. There are many energy efficiency and renewable energy opportunities for the RMI. However, there is no single opportunity or simple means to reach the policy's 20% renewable energy goal. Photovoltaic (PV) electricity generation is commercially available, economically competitive and well suited to the RMI urban centers as it is a distributed generation technology that is

currently being installed in small power clusters on existing rooftops. As of today, only three grid connected solar PV systems that are operational in the Marshall Islands. One grid connected PV system uses a 57 kilo-Watt-peak (kWp) array. The second one has a capacity of 209kWp and the capacity of the third off grid system is 12.54kWp. However, the total capacity only covers up to nearly 3% of the midday peak load of the Marshall Islands. If you include the future 1MW grid connect PV project in the mix, the capacity will go up to around 13% of the midday peak load.

The energy sector transformation will require significant investment in infrastructure, and local technicians and relevant key players will require the necessary institutional capacity to manage more complex systems in a sustained way. The lack of communication and coordination between the United States and the RMI government can be partially attributed to limited institutional mechanisms in place to support widespread dissemination of renewable and energy efficient technologies, and the dissemination of knowledge and skills required for the operation and maintenance of energy systems. Portions of grant money should be spent strengthening local capacity rather than simply providing systems that are poorly designed for reliable operation in the tropical marine environment and cannot be properly operated and maintained once the donors leave. This would in turn help increase the success of projects and increase public support for additional renewable energy and energy efficiency projects.

Thank you Mr. Chairman for hearing our testimony. I look forward to answering any questions that you or the committee might have.