

**THE END OF THE COMPACTS:
WHAT ALL CHUUKESE SHOULD KNOW
For Public Hearings on Independence**

Chuuk Political Status Commission: 2014

An Excerpt from the Supplemental Committee Report

Independence Committee of the Chuuk Political Status Commission

Pandinos N. Suzuki, Chairman

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(2)

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Compact Dollars: Shrinking Allocations

(5). **Compact/Amended Compact:** These agreements represent our status quo. Through time, they have represented the declining assistance to Chuuk as the U.S. carries out its exit from Micronesia. There has been much debate about the relative allocations of Compact funding, and some confusion about the "formula" used by the FSM Government to disburse annual amounts.

(5a). **Old percentages/the EPIC resolution:** In October, 2005, the Economic Policy Implementation Council of the FSM agreed on the following percentages for allocating Amended Compact funds:

Chuuk	38%
Pohnpei	25.31%
Yap	15.79%
Kosrae	10.9%
FSM Govt	10%

EPIC was made up of the President of the FSM, the Governor of each state, the Speaker of the FSM Congress, and the presiding officers of each legislature.

(5b). **New percentages/FSM legislation:** The above breakdown of FSM Compact funds has been in effect until the recently passed FSM act, Public Law 18-12, which set these new percentages to be effective from FY 2014.

Chuuk	40%
Pohnpei	26.72%
Yap	16.67%
Kosrae	11.5%
FSM Govt	5%

(5c). **Dollars per head:** The Commission is familiar with the disparity between allocation percentage and population figures. The Independence Committee Chair illustrated this in an earlier meeting, showing the years 2004-2008, covering \$251 million for the FSM. Note per-capita dollars for each government.

FSM STATE	ALLOCATION	%	POPULATION	%	PER CAPITA
Kosrae	\$23m	10.2	8,000	7.3	\$3,250
FSM	27m	10.6	800	.007	33,750
Yap	43m	16.9	12,000	11	3,558
Pohnpei	71m	27.9	38,000	35	1,868
Chuuk	87m	34.2	50,000	46	1,740

Departments for all: The most striking number in the above chart is the per capita figure for the 800 FSM Government employees. At about \$34,000 per head, one would expect a modern office for each, adding up to one of the finest government operations seen in the Pacific!

(5d). **Chuukese wherever they are:** The revised allocation formula does move in the right direction, now allowing Chuuk a 40% share. Yet any such formula, based as it is on strict counts of resident citizens, does not approach levels of assistance which truly reflect our overall numbers.

Chuuk is in need of a funding arrangement which would recognize our entire Chuukese population, both here and abroad. Even taking into account overseas populations of other FSM states, Chuuk citizens may number up to 2/3 of the FSM total. [This is based on a projected FSM total of up to 120,000, which would include at least 80,000 from Chuuk].

As long as Chuuk is only a part of a sovereign nation, and not one itself, percentage allocations will remain insufficient. As it is, other entities compete for shares of foreign assistance and governments outside Chuuk control and regulate our civic and private enterprises. With independence, any and all funding from whatever international source arrives unrestricted and undelayed by outside government regulation.

(5e). **Declining dollar amounts:** These are very clear in terms of FSM grant assistance under the Amended Compact. Each year brings another Compact grant reduction of \$800,000 for the FSM. To use the new allocation figures in reverse, we can predict that Chuuk will lose 40% of the \$800,000, or \$320,000, each year until 2024, when some say Chuuk will lose everything.

That \$800,000 pulled from FSM grants (\$320,000 of it pulled from Chuuk) is moved to the Trust Fund, where we can hope it will safely be until the year 2024. We should note that investment losses out of this fund, totalling about \$1 million, recently occurred. The fund has recovered for now, but most analysts see the pay-off keeping Chuuk afloat for only a few years after 2023. In any case, we would be wise to keep reminding ourselves that the intent of the U.S. is to terminate assistance.

Compact Trust Fund: Investment History

(6). **The Trust Fund:** U.S. authorities have officially titled this catch-all bank account the "Trust Fund for the People of Micronesia." A more proper title might be: "The Final Way Out of Micronesia for U.S. Agencies." From all directions, we are advised that this savings account will evaporate within one or two years following the end of Amended Compact funding in 2023.

Our Commission exists as a result of the evidence pointing to this fiscal outcome. Faichuk leadership raised loud concerns about this over 10 years ago. The Chuuk Legislature has directed us to look for some other road to development. The FSM Government, through its SBOC (Compact Management) has advised that the Trust Fund will "significantly fall short" of the amount required to give us a "smooth transition from Compact sector grants in 2024." Even outside analysts from the International Monetary Fund warn:

Under existing arrangements, the trust fund may suffice only to replace expiring grants for a few years after the Compact expires. "Micronesia," in Pacific Island Economies, IMF, 2006.

(6a). **The cut of the \$92 million:** The initial FSM contribution to the Fund was \$30.3 million. Since 2004, ever-increasing FSM amounts to the Fund have reflected ever-decreasing Compact grant amounts. Each year, the same total of \$92.2 million for the FSM is divided with more for the Fund, less for the grants, never exceeding the sum of \$92.2 million. In 2004, it was \$76.2 million in grants, \$16m in the Fund. In 2023, it will be \$62.6 million in grants, \$29.6m in the Fund. By FY 2012, contributions to the Fund totaled \$204 million, representing a \$30.3 million initial deposit by the FSM and \$173 million contributed since then "by" the U.S., though obviously incrementally shifted (taken) from FSM Compact allocations.

(6b). **Recent figures for Fund contributions:** Figures below to show trends; drawn from U.S. and FSM sources.

	<u>Annual Contribution</u>	<u>Total Trust Fund Contributions at FY end</u>
FY 2010	\$21.5 million	\$157 million
FY 2011	\$22.4 million	\$178 millin
FY 2012	\$23.6 million	\$204 million

(6c). **Total Trust Fund Net Assets:** Trust fund investments over the first 10 years of the Amended Compact have varied dramatically. In FY 2011 for example, investments on behalf of the Fund directly lost over 1/3 of a million dollars (\$339,312). Making the loss worse were indirect investment costs (listed as "investment expenses") of \$645,382. So FY 2011 Trust Fund investments lost \$984,694. In stark contrast, an FSM report for FY 2012 shows almost unbelievable investment gains of \$35.3 million! When added to the Fund contribution for FY 2012 (\$23.6 million), the total net assets of the Trust Fund jumped above one quarter of a billion dollars (\$257.3 million). These total net asset figures are naturally expected to be above actual contribution totals, but never have reached the hoped-for (or dreamed-of) levels widely propagated over 10 years ago.

Total Net Asset Value, Trust Fund

	<u>Dollar Amount</u>	<u>Percentage Increase (over prior FY)</u>
FY 2010	\$177.2 million	
FY 2011	\$198.5 million	12%
FY 2012	\$257.3 million	29.6%

(6d). **Growth rate(s) for Trust Fund:** Two recent growth rates have been presented which illustrate how sharp fluctuations occur when assets are even partially dependent on investment market conditions. The rate jump below reflects the \$35 million investment return proclaimed for FY 2012 by the FSM SBOC.

Average growth rate of Trust Fund per annum, FY 2004 to FY 2011:	2.2%
Average growth rate of Trust Fund per annum, FY 2004 to FY 2012:	3.8%

(6e). **Growth rate consequences** were casually projected by an accounting firm (Parente Beard) which examined FY 2010 and FY 2011 Trust Fund finances. Without going beyond the transition years of 2023 and 2024, they gave the following estimates for what might be available to the FSM for 2024 expenditures, depending on the percentage increase generated by the Fund.

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Uncertain Future of the Compact Trust Fund

<u>Rate of return for Trust Fund from FY 2012 to FY 2023</u>	<u>Estimated funding available for FY 2024 in relation to projected FY 2023 expenses</u>
5%	"Should provide" revenue at 85% of FY 2023 grant level
8%	"Probably" 100% of FY2023, without inflation adjustment
10%	"Probably" 100%, even with an adjustment for inflation

(6f). **Unanticipated contributions:** The same study mentions the old hope of dollars flowing into the Fund from an outside source, referring to Trust Fund Committee actions "to help attract other contributions." So far, the Fund has not appeared attractive to any donors. Without one or more major outside infusions to the Fund in the coming 9 years, "achieving such annual average growth (5%, 8%, or 10%) is not expected." Why such rates found their way into the report is a mystery.

(6g). **The Trust Fund Alphabet:** To confuse inquiring minds more, the Amended Compact presents four discrete accounts, A, B, C, and D. For purposes of the Commission, B and D are next to useless. Account "B", if ever established, would not be accessible until FY 2023. It will contain no funds until 2022. Account "D" may be established to allow contributions from "unanticipated" sources. (As far as we know, all sources outside the U.S. and the FSM are unanticipated). This leaves us the "A" account, which is the main body of the Fund, and the "C" account, which is intended for post-FY 2023 supplement. Trust Fund investment returns above 6% are directed to this account. Some recent figures for the "C" account are below.

	<u>C Account Contribution</u>	<u>C Account Total</u>
FY 2009		\$12.7 million
FY 2010	\$7.5 million	\$20.2 million
FY 2011	(zero)	\$20.2 million
FY 2012	\$20.9 million	\$41.1 million

(6h). **The Dream of Riches: Trust Fund growth projections** look fantastic on paper. For the remaining ten years of the Amended Compact, steadily increasing contributions will be made to the Fund, rising from \$21.6 million for FY 2013 to \$29.6 million in FY 2023. Each year, the new contribution is added to the new principal which includes average interest and investment gains from the preceding year. The following data assume a rather optimistic average Fund growth rate of 3%. (From FY 2004 to FY 2011, the actual average annual growth rate was 2.2%). Figures are in millions and are for discussion purposes only:

<u>Fiscal Year</u>	<u>Accumulated Fund</u>	<u>Contribution for year</u>	<u>New Fund Total</u>
2013	\$257.3	\$21.6	\$278.9
2014	287.3	22.4	309.7
2015	319	23.2	342.2
2016	352.5	24	376.5
2017	387.8	24.8	412.6
2018	424.9	25.6	450.5
2019	464	26.4	490.4
2020	505.2	27.2	532.4
2021	548.3	28	576.3
2022	593.6	28.8	622.4
2023	641.1	29.6	670.8
2024	690.8	(zero)	\$690.8

Total Compact and Non-Compact Assistance from the U.S. to the FSM has been running up to over \$100 million per year. The math here is easy. If the Fund grows at an average annual rate of 3% for the next 10 years, the FSM could see more than 5 years of existence at current levels. Note that total U.S. grant fund expenditures in the FSM were \$135 million in FY 2011.