

STANDING COMMITTEE REPORT NO. 16-114

RE: C.B. NO. 16-124/R&D

SUBJECT: LUEN THAI FISHERIES PROJECT

SEPTEMBER 5, 2010

The Honorable Isaac V. Figir  
Speaker, Sixteenth Congress  
Federated States of Micronesia  
Third Regular Session, 2010

Dear Mr. Speaker:

Your Committee on Resources and Development (R&D), to which was jointly assigned and referred C.B. No. 16-124, entitled:

"A BILL FOR AN ACT TO AUTHORIZE THE PRESIDENT TO EXECUTE ON BEHALF OF THE NATIONAL GOVERNMENT OF THE FEDERATED STATES OF MICRONESIA A CONCESSIONAL LOAN AGREEMENT WITH THE GOVERNMENT OF THE PEOPLE'S REPUBLIC OF CHINA AND TO SET THE TERMS AND CONDITIONS THEREOF, AND FOR OTHER PURPOSES.",

begs leave to report as follows:

The intent and purpose of the bill are expressed in its title.

Your Committee held a series of public hearings in the states.

**Chuuk State hearings**

The first hearing was held in Chuuk on June 28, 2010. In attendance were Governor Wesly Simina and his cabinet. Governor Simina appreciated the effort of the Committee and stated that the State of Chuuk is in full support of the proposed bill and project because of the potential socio-economic benefit for Chuuk State.

This sentiment was echoed by leadership of the Chuuk State Legislature during the second hearing that was held on June 29, 2010 at the Chuuk State Legislature chamber. Attending the

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hearing were President Mark Mailo and most of the Chuuk State legislators. Also, attending the hearing were members of the general public. One of the concerns raised is the potential social and environmental impact of the fisheries project. At the end, the Legislative branch and the members of the public expressed their support on the fisheries project. However, the recommendation that was brought up during the hearing is for the implementation of the fisheries project to coincide with the other infrastructure development projects of the Chuuk State, especially the power upgrade to achieve coordinated support of these two projects.

#### **Kosrae State hearing**

Your Committee held two separate hearings in Kosrae. The first hearing was held on July 1, 2010 at the Governor's conference room. In attendance were Governor Robert Weilbacher, Lt. Governor William Tosie, Directors Steven George, Weston Luckymis, Tiser Reynold, Attorney General J.D. Lee, staff from the Department of Resources and Economic Affairs and the Governor Chief of Staff, Josiaha Waguk.

Governor Weilbacher understands that the original bill (C.B. No. 16-124) did not include the infrastructure requested by the Kosrae State. He indicated that, once the project is implemented, a power upgrade in Kosrae is very important so Kosrae State will need an additional generator. After the hearing, the Governor indicated that Kosrae State is in full support of the rehabilitation project.

A second hearing was held at the Kosrae Legislature chamber on July 2, 2010. Attending the hearing were Senators Ilahi Abraham, Bob Skilling, John Martin, Gibson Siba, Albert Welly and Semeon Phillip.

At the hearing the intent of the bill was explained. The Senators were informed that Kosrae State will lease the facility to a commercial fishing operation (Luen Thai), and the proceeds of the lease agreement will be used to pay for Kosrae's obligation on the loan package, as is the case for the other states. Also, the facility remains the property of Kosrae State. At the end of the hearing, Vice Speaker Albert Welly on behalf of the 9<sup>th</sup> Kosrae State Legislature indicated its full support on C.B. No. 16-124. Kosrae State's strong support of the project was communicated to Speaker Isaac V. Figir on September 29, 2010 in State Communication No. 16-64.

#### **Yap State hearing**

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Your Committee held a joint hearing with the Yap leadership on July 6, 2010. Witnesses at the hearing include: Speaker Charles Chieng, Senators Jesse R. Subolmar, Clement Mulalap, Sabino S. Sauchomal, Henry Falan, Governor Sebastian Anefal and most of his cabinet members.

One of the Senators asked whether the \$22 million is inclusive of the additional needed infrastructure in each state relating to the implementation of the project. James Movick explained that with the due diligent work of the Forum Fisheries Agency and others, \$22 million is the figure that is considered to be viable for the project and does not include the other components the states want. Speaker Chieng inquired about the additional needs for the other states relating to the project. The additional components for each of the States are described later in this report. Another concern is why Luen Thai is selected as the operator of this project. James Movick explained that one of the lessons learned is that those fishing ventures that are successful are experienced in the commercial area. Still another is that Government owned fishing projects are not successful. Luen Thai is selected because it already has a track record in the FSM, as well as the region, is a good corporate citizen and also has the logistical arrangement in FSM.

#### **Pohnpei State hearing**

Your Committee held a joint hearing with the leadership of Pohnpei at the Governor's conference room on July 27, 2010. Present at the hearing were Senators Robert Nakasone, Aurelio Joab, Berney Martin, Dakkar Daniel, Naiten Phillip, Governor John Ehsa and Attorney General Scott Garvey.

One of the comments raised is whether the amount requested by Pohnpei State includes the relocation of the FSM Petroleum Corporation. James Movick explained that some of the funds requested are to that effect. One concern is whether, if one of the components is not included, for instance, say Pohnpei not included, what will be the status of the project. James Movick indicated that the project can proceed without one state, but the amount would have to be revisited.

#### **Palikir hearings**

In September 2010 your Committee held a series of hearings in Palikir with the Department of Resources and Development, Forum Fisheries Agency (FFA) representatives, and Luen Thai representatives.

The testimony began with an explanation of Congressional Bill No.

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16-124. The FFA representatives explained the state projects first. These were explained first to the Committee because the Committee had to make the threshold decision of whether to include authorization for the loans in the bill. The state components are needed because current state infrastructure is unable to handle the increased usage resulting from the overall Luen Thai project.

The proposed state improvements are:

- State of Yap - new generator; cost: \$1,000,000
- State of Chuuk - new ferryboat dock; cost: \$4,000,000
- State of Pohnpei - wastewater treatment and transformers; cost: \$3,800,000
- State of Kosrae - new generator; cost: \$886,000.

These improvements will enable each state to handle the increased demands that operation of the project will make.

Further testimony revealed that Luen Thai is willing to enter into user agreements with and make payments to Yap, Pohnpei, and Kosrae for use of the new facilities. These payments will provide those states streams of income to be used for repayment.

The project for Chuuk is unique in that Luen Thai will not use the completed dock there. The dock for Chuuk will be an alternate dock for local ferryboats to land. This alternative dock will reduce usage of the main dock thus freeing it up for use by Luen Thai. Therefore, there is no stream of income generated by this project. However, the bill includes language requiring the states to provide a general guarantee to repay their loan and to provide a plan and commitment to pay their loan.

Your Committee also reviewed Presidential Communication No. 16-284 in determining whether to include authorization of the loans for the state projects in the bill. In Presidential Communication No. 16-284, the President gave his support to authorizing state loans in C.B. No. 16-124, suggested his eligibility criteria for the states to receive the funds, and provided a revised bill containing the required new language.

After hearing the descriptions of the projects, and reviewing Presidential Communication No. 16-284 and the included revised bill, your Committee recommends authorizing the loan in the amount of up to \$33 million, which includes loan funding for the state projects.

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When questioned on the viability of this project in the light of past failed National Government projects, FFA representatives responded that they had critiqued this project against previous unsuccessful projects. They testified that past failures were mainly due to lack of competent management. It was further explained that this project is different because experienced Luen Thai managers will be managing operations.

The FFA representatives were also questioned as to why this loan was different than other unsuccessful loan projects in the past. The FFA representatives explained that the difference in this case was that the payments to FSM are not dependent upon the profitability of individual boats. Boats will pay fees for privileged access to our facilities; as long as there are enough boats, which Luen Thai guarantees, payments will be made sufficient to cover the loan payments.

The number of boats related to this project will be approximately 120. When questioned whether this number of boats was prudent the answer was yes. The FSM has historically licensed between 100 and 150 boats per year, therefore 120 is perfectly within that range. Luen Thai is contractually obligated to keep 120 boats in the FSM. NORMA will retain the authority to license further boats to fish in our EEZ.

The most important concern for many members was the lack of security provided to the National Government by the states to secure repayment. All loan funded infrastructure will be owned by the states while the National Government is the sole borrower. Therefore, the potential exists for the states to benefit directly from the facilities, while the National Government pays for them. For this reason, your Committee considers it prudent to retain oversight and approval authority over the subsidiary agreements, not only over the threshold authorization of the loan. To this end your Committee recommends limiting the authorization in C.B. No. 16-124 to negotiating the framework and subsidiary agreements. Authorization to execute the loan to come after the framework and subsidiary agreements have been reviewed and approved by Congress.

Your Committee also strongly recommends the Department of Resources and Development put itself into a position to lead the monitoring and reporting efforts on the implementation of the various components of the projects. Your Committee recommends the Department build its capacity toward this end in preparation for the project moving forward.

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Other member concerns and recommendations were the use of the loan money to leverage our Compact infrastructure grants to fund the projects, ensuring clarity of the procedures and extent of taxation of Luen Thai boats and project operations, and reworking the grace period to ensure lease payments from Luen Thai precede loan repayments from our side. The FFA, Luen Thai, and Department representatives appreciated and noted these concerns and recommendations.

Your Committee recommends the following amendments:

1. Page 1, title line 1, after "to" delete "execute" and insert "negotiate" in lieu thereof.
2. Page 1, line 1, delete "Inducements", and insert "Chinese Government Concessionary Loan availability." in lieu thereof.
3. Page 1, line 3, after "provide" insert "a concessionary ("."
4. Page 1, line 3, after "soft" insert ")".
5. Page 1, line 4, delete "assistance".
6. Page 1, line 5, after "fisheries" delete "trans-shipment" and insert "infrastructure," in lieu thereof.
7. Page 1, line 5, after "trans-shipment" delete "and".
8. Page 1, line 6, after "processing infrastructure" insert "and related infrastructure requirements".
9. Page 1, line 6, after "States" insert "pursuant to the Chinese Government Concessional Loan program generally that was offered to eligible Pacific Islands governments by the Government of People's Republic of China in April, 2004".
10. Page 1, line 7, after "indicated" delete "by the Government of the People's Republic of China that the soft loan assistance has a flexibility of being convertible into grant assistance if the fisheries project ultimately fails. The leadership of the National Government and the leadership of the four State Governments have indicated a desire to pursue a fisheries project in reliance of these inducements" and

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insert "that the standard terms of these loans provide that the Government of the Federated States of Micronesia, as the Borrower, and the Government of the People's Republic of China, as the Lender, shall from time to time inspect the utilization of the Loan and have consultations on issues arising from the execution of the Loan agreement, and that these consultations would generally be to consider additional flexibility requested by FSM Government as required to assist it to adjust to any unforeseen problems that may arise in the execution of the loan agreement that affect its ability to timely or fully repay the loan. The leadership of the National Government and the leadership of the four State Governments have indicated a desire to pursue a fisheries project in reliance on the concessionary nature of the loan and the historical practices of the PRC Government in working with borrowing governments to positively consider necessary adjustments due to unforeseen project difficulties or broader macro-economic distress" in lieu thereof.

11. Page 1, line 13, after "authority" delete "to appropriate funds".
12. Page 1, line 18, after "Micronesia," delete "and to execute".
13. Page 1, line 18, after "execute a" insert "concessional".
14. Page 1, line 18, after "loan" insert "framework".
15. Page 1, line 20, after "up to" delete "\$22" and insert "\$33" in lieu thereof.
16. Page 1, line 20, after "(USD)" insert "(in Renminbi Yuan equivalent)".
17. Page 2, line 1, after "China," insert "for the purposes and uses set out in section 3 of this act and".
18. Page 2, line 2, after "section" delete "3" and insert "4" in lieu thereof.
19. Page 2, line 3, after "act." delete "The proceeds of the loan shall be utilized for a fisheries rehabilitation project."

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20. Page 2, line 5, after "act." return down to line 6 and insert "Section 3. Purposes and uses of the loan.
  - (1) The President shall utilize no more than USD \$22 million of this loan (in Renminbi Yuan equivalent) for the purposes of financing the rehabilitation and expansion of state transshipment and processing facilities that will be leased to the commercial operator who shall make and guarantee the associated loan repayments for the FSM Government to the Lender. The President shall undertake his best efforts to ensure that the various agreements and arrangements necessary to give effect to this authorized loan use shall be executed and ready to be implemented within 6 months of this bill becoming law.
  - (2) The President shall utilize no more than USD\$11 million (in Renminbi Yuan equivalent) to lend to the state governments or their authorized state entity, for the purposes of acquiring and constructing certain public infrastructure identified to be necessary to ensure the effective, timely and efficient establishment and operation of the fishery rehabilitation loan project in each state. In making these on-loans, the President shall require each state government to provide a security interest in favor of the FSM Government in the loan funded state facilities or in the stream or streams of income resulting from the use of lease of loan funded facilities, provide a general guarantee to repay the borrowed amount and provide a viable plan and commitment to pay loan repayments and associated direct administrative costs within the overall period of the framework agreement between PRC and FSM governments, and shall establish arrangements with the PRC Government that this portion of the loan may be available for draw-down for up to three years from the date that this bill becomes law."
21. Page 2, line 6, after "Section", delete "3" and insert "4" in lieu thereof.
22. Page 2, line 8, after "shall" delete "enter into" and insert "negotiate" in lieu thereof.
23. Page 2, line 15, after "Pursuant to" delete "the inducements on the soft loan facility, a written agreement must be executed indicating that the loan repayment is waived in the event the project fails or

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when the project operator is in default" and insert "reliance upon the historical nature of the concessionary loan program, provision is to be made in the loan framework agreement between the FSM Government and the PRC Government that in the event the project fails, or when the project operator is in default, or FSM Government faces a situation of significant overall macro-economic duress, the Government of the Federated States of Micronesia and the Government of the People's Republic of China shall have consultations on issues arising from the execution of the Loan agreement with a view to provide the FSM Government considerate adjustment or relief as appropriate and agreed" in lieu thereof.

24. Page 2, line 19, after "agreement" insert "shall resolve any differences regarding the Loan Framework Agreement with full recourse to all diplomatic avenues, practices and considerations between the two sovereign nations".
25. Page 2, line 19, after "and" insert "the parties to".
26. Page 2, line 19, after "all" delete "the" and insert "its" in lieu thereof.
27. Page 2, line 23, after "agreements." delete "A waiver of sovereign immunity and a full faith and credit guaranty executed by both sovereign governments shall satisfy this condition."
28. Page 2, line 25, after "condition." Return down to next line and insert "(4)The President shall seek from participating state governments sufficient legal assurances regarding the utilization of state facilities and that the lease payments receivable by the states for the use of the facilities, after rehabilitation by the FSM Government with the proceeds of this loan, shall be assigned to the FSM National Government of its designated agent to be used by the FSM Government for these loan repayments, and further that the FSM Government and its agents shall receive lease payment guarantees fro the facility operating sub-lessee that is sufficient to ensure that the FSM Government is able to meet its own loan repayment obligations with the PRC Government."

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29. Page 3, delete lines 1 through 15 in their entirety.
30. Page 3, line 16, after "Section" delete "4" and insert "5" in lieu thereof.
31. Page 3, line 17, after "prior to" delete "entering into" and insert "executing" in lieu thereof.
32. Page 4, line 1, after "Section" delete "5" and insert "6" in lieu thereof.

**CONCLUSION**

Your Committee on Resources and Development is in accord with the intent and purpose of C.B. No. 16-124, C.D.1 and, subject to the concurrence from the Committee on External Affairs, recommends its passage on First Reading, and that it be placed on the calendar for Second and Final reading in the form attached hereto as C.B. No. 16-124, C.D.1.

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Respectfully submitted,

/s/ Roger S. Mori  
Roger S. Mori, chairman

/s/ Tony H. Otto  
Tony H. Otto, vice chairman

/s/ Peter M. Christian  
Peter M. Christian, member

/s/ Dion G. Neth  
Dion G. Neth, member

/s/ Peter Sitan  
Peter Sitan, member

/s/ Joseph J. Urusemal  
Joseph J. Urusemal, member

Paliknoa K. Welly, member