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STATE OF CHUUK, STATE OF KOSRAE, STATE OF POHNPEI AND STATE OF YAP, *APPELLANTS,* vs. SECRETARY OF DEPARTMENT OF FINANCE AND THE GOVERNMENT OF THE FEDERATED STATES OF MICRONESIA, *APPELLEES.*	APPEAL CASE NO. P4-1999 CIVIL ACTION NO. 1995-085 APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

I. INTRODUCTION

The Four States file this Reply Brief to respond to the Opening Brief filed by Appellees (Secretary of the Department of Finance and the National Government of the FSM) as well as to the *Amicus Curiae* Brief filed by the Congress of the Federated States of Micronesia.

This case raises fundamental questions of interpreting and applying the FSM Constitution and focuses on the intent of the Micronesian people in adopting the 1975 Constitution. If they had been asked at the time of the ratification vote whether they would agree to a constitutional provision stating that 100% of all the revenues from the living resources of the oceans would be controlled solely by the National Government, without any of it being shared with the States, they would have responded with a resounding "No." We can be confident of predicting this result, because every revenue source listed in the FSM Constitution is required to be shared with the States. *See* States' Opening Brief at pages 13-14. In addition, at the time of the ratification vote on the Constitution, all the revenues collected from fish were returned to the separate districts, and the sharing of goods and services received as a result of foreign fishing in the exclusive economic zone (EEZ) continued well after the Constitution was ratified. *See* States' Opening Brief at 10, 44-46 and Section II(B) of this Brief *infra*.

The National Government is nonetheless taking the position that the FSM Constitution authorizes the National Government to retain 100% of the revenues received from fishing licenses and control those revenues without any duty to share them with the State Governments. This position is contrary to the language and spirit of the Constitution, and of the intent of the people of Micronesia who voted to adopt the Constitution. It should also be emphasized at the

outset that a reversal of the trial court's decision will be beneficial for the country in the long run, because it will permit flexibility in economic development. The narrow interpretation of the word "tax" found in the trial court's opinion will tie the government's hands and make it difficult to structure flexible and appropriate taxing schemes related to the new economic activities that the country is trying to promote. This Honorable Court serves as the national arbiter, with the responsibility to resolve this dispute in a manner that is fair and consistent with the language and spirit of the FSM Constitution.

The States have argued that the inherent structure of the FSM Constitution, which creates a federation of geographically separated and culturally distinct island communities, requires the conclusion that the States are the underlying owners of all the marine resources.[1] This result is inevitable because the National Government is a limited government with only those enumerated powers that are explicitly delegated to it. Article IX, Section 2(m) delegates to the National Government the power to "regulate" the marine resources, but neither this provision nor any other part of the Constitution delegates ownership of marine resources to the National Government. The trial judge ruled the constitutional provisions were ambiguous regarding ownership of marine resources (App. 611, 614),[2] and the National Government's brief appears to agree with that conclusion, because it turns to nontextual sources to support its arguments.

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[1] This vision of the FSM's constitutional structure was recently confirmed in President Leo A. Falcam's inaugural address. President Falcam, who had been one of the leaders in the 1975 Constitutional Convention, said that he would undertake leadership in external affairs, which he described as "the one major area that is reserved by our Constitution to the National Government, but again, I must assure you that my Administration will view itself as *a trustee for State interests* in this area, not as an independent operator." (Emphasis added.)

[2] "App." refers to the Appendix filed with the Four States' Opening Brief.

Congress's *amicus* brief virtually ignores the textual provisions of the Constitution relevant to ownership, and focuses instead on the definitions of "tax" and "revenue" in Article IX, Section 5, as well as on policy arguments regarding the proper structure of the FSM government.

The States do not view the FSM Constitution as ambiguous on the underlying ownership of the marine resources, because the Constitution explicitly defines the borders of the Four States in Article I, Section 2 (utilizing "the principle of equidistance") as including the exclusive economic zone, and because it is a matter of common understanding that governmental entities exercise sovereign ownership over the public resources within their borders. But the States have also focused more directly on Article IX, Section 5 because this provision provides a simpler and more straight-forward way of resolving this dispute. In this Reply Brief, the States will again focus primarily on the issues related to Article IX, Section 5, while also reiterating their position regarding the underlying ownership and responding to issues raised by the briefs of the National Government and the Congress.

II THE MONEYS COLLECTED FROM FISHING LICENSEES ARE "REVENUES" WITHIN THE MEANING OF ARTICLE IX, SECTION 5.

A. Introduction.

The National Government's Brief advocates a narrow, highly-technical definition of the words "taxes" and "revenues" in Article IX, Section 5 of the FSM Constitution. The States submit instead that a more common-sense and broad definition is appropriate, and that such a flexible definition will be important to permit the government to raise revenues from the variety

of economic activities that the country is trying promote.[3] The delegates to the 1975 Constitutional Convention were writing a document to serve the country for many generations, and they used words as lawmakers launching a new country on an uncertain voyage. It is appropriate, therefore, to interpret the constitutional language in light of the overriding scheme established by the 1975 Constitution, which was to create a federation of autonomous states in which all revenues would be shared between the National Government and the States.

B. The Refusal of the National Government to Share The Fishing Revenues with the Four States Is Not a Longstanding Practice that Deserves Any Respect.

Both the National Government's and the Congress's briefs assert that a ruling in favor of the Four States would reverse long-standing practices of the FSM that should be respected as valid indications of how the Constitution was meant to be interpreted. But in reality, the States *were* included in the distribution of revenues in the early years of fishing licenses, have continued to receive shares of the goods and services received from fishing agreements, and have objected with increasing vigor when they were denied their share of the revenues received, leading to the filing of this lawsuit in 1995. As explained in the States' Opening Brief at page 46, representatives of the States were part of the delegations that went to Japan in the early 1980s to discuss how the benefits received from fishing licenses should be distributed. The sharing of fees received in the form of goods and services has been formalized in Title 24, Section 115 of

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[3] An example of the confusion that can arise regarding interpretation of the taxing powers can be found by comparing the *Amicus* Brief of Congress with that of the National Government. Congress's *Amicus* Brief at page 5 refers to "the authority to tax...exports provided in the Constitution." But page 45 n.42 of the National Government's Brief says that the National Government's "taxing power is limited to taxes on imports and taxes on income," apparently acknowledging that the National Government cannot tax exports.

the FSM Code. Different formulae have been utilized over the years to divide these benefits, with the benefits rotating among the states in recent years. Compare SCR No. 5-158 (1987) to SCR No. 7-104 (1991). It is clear that the benefits being shared derive from fishing engaged in beyond the 12-nautical-mile territorial sea limit, because fishing agreements uniformly include the boiler-plate clause excluding fishing within the territorial sea. *See* examples of fishing agreements attached to Plaintiffs' Motion for Summary Judgment, Sept. 23, 1997, Exhibit C, para. 14, Exhibit D, para. 14, Exhibit E, para. 13(b), App. E. If, therefore, one were to give special credibility to the actions of the early FSM Congresses, as is suggested in the National Government Brief at page 6, it would support a recognition of the rights of the States to receive their share of the fishing revenues.[4]

C. The Linkage of the Fishing License Fees to a Regulatory Scheme Does Not Make These Fees Any Less "Revenues" That Must Be Shared Under Article IX, Section 5.

The sections of the National Government's Brief on the tax issue consist mostly of a restatement and recharacterization of the arguments presented in the States' Opening Brief, and

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[4] On page 30, the National Government's Brief argues that statutes and constitutional provisions should be interpreted to be compatible so that the statutes are found to be constitutional. But if they appear to be in conflict, it is improper to interpret the constitutional provision so that it is consistent with the statute. Instead, it is the statute that should give ground and be interpreted to be consistent with the constitutional provision, which is the more enduring and basic principle. The fact that unconstitutional behavior has been engaged in for some years should not validate the improper behavior, particularly since the States have been consistent in complaining about the failure to share the fishing revenues from the beginning. *See, e.g.,* Resolution No. 1-91-003 of the First State Legislatures Leadership Conference, Chuuk, April 22-26, 1991, attached as Exhibit W to Plaintiffs' Motion for Summary Judgment, Sept. 23, 1997, App. E.

this Reply Brief will not reexamine that well-trod ground once again.[5] The National Government appears to have abandoned as untenable the trial court's view that the fishing license revenues are "revenue from the sale of national assets," slip op. at 64, App. 653, and instead now argues (a) that moneys collected as part of a regulatory scheme cannot be "taxes" within the meaning of Article IX, Section 5, and (b) that the process of collecting fishing revenues fails to meet the test in *J.W. Hampton, Jr., & Co. v. United States,* 276 U.S. 394, 409 (1927), which requires the legislature to articulate an "intelligible principle" to guide the collection of taxes by an administering agency.[6]

The National Government's Brief at pages 32-36 is unpersuasive in trying to distinguish the FSM tax cases cited on pages 19-20 of the States' Opening Brief on the ground that the exactions collected under the Marine Resources Act are different because this Act, according to the National Government, "serves a primary and critical regulatory purpose." As the States' pointed out at page 21 and footnote 7 of their Opening Brief, the National Government has conceded that the primary purpose of the fishing-licensing program is to raise revenue, that the

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[5] The *Amicus* Brief filed by Congress argues simply that the fishing fees should not be viewed as taxes because "they are levied pursuant to regulatory authority," citing *San Juan Cellular Tel. Co. v. Public Service Commission*, 967 F.2d 683, 685 (1st Cir. 1992). The *San Juan Cellular* decision, however, emphasizes a number of factors, as the States' Opening Brief explains at pages 23-25, and the exactions determined not to be a tax in that case were dramatically different from the fishing revenues at issue in the present case, because they were designed solely to cover the costs of regulation and were deposited into a separate fund.

[6] At page 36, the National Government's Brief criticizes the States' Opening Brief for relying heavily on U.S. decisions in the tax area. These decisions were discussed in some detail because the trial court utilized, almost exclusively, U.S. decisions for its analysis of this issue. It might also be pointed out that the 1990 opinion written by the FSM Attorney General's Office on the Pohnpei Airport Tax explained on page 21 n.8 of the States' Opening Brief utilizes U.S. decisions almost exclusively. *See* App. 245.

revenues raised substantially exceed the costs of operating the program,[7] and that the revenues collected are used for general governmental purposes. Like most other taxing programs, this one does have an incidental regulatory impact accompanying its revenue-raising purpose and effect, but the National Government cites no authority that would thereby remove such an exaction from the category of "revenue" that must be shared with the States under Article IX, section 5. In fact, the language from 24 FSMC sec. 101, which the National Government's Brief quotes at page 34 to establish the Act's regulatory purposes, acknowledges the primary revenue-raising goals of this program by confirming that the marine resources "provide[] the primary means for the development of economic viability" and that the enactment is designed to "generate the maximum benefit for the Nation from foreign fishing." In fact, any fair reading of the "regulatory" provisions of Title 24 would conclude that most are included primarily to raise revenue.[8] Thus, just as in the case of *Stinnett v. Weno*, 7 FSM Intrm. 560, 561 (Chk. 1996), we have a program "with the stated purpose of creating and collecting revenue," and under the decision in *Stinnett* and its progeny, this program must be characterized as a "tax" even though it may also have incidental regulatory effects.[9]

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[7] The National Government's Brief acknowledges this once again at page 34.

[8] If further evidence is needed that the fishing-licensing program is designed primarily to raise revenue, *see* Standing Committee Report No. 6-10 (1989), which contains the following language in connection with an agreement involving Taiwan fishing boats: "[T]he funds generated by this agreement are urgently needed, especially in this time of federal program phase out and compact step down, to assure a minimum level of governmental services and to pursue the ambitious development objectives, including domestic fisheries development projects, targeted by the President and State leaders."

[9] The National Government's argument is also undercut by the fact that the Micronesian

All taxes have a regulatory component, and any attempt to distinguish between revenues collected as part of a regulatory scheme and those collected "purely" to raise money would quickly prove futile. The United States Supreme Court attempted to draw such a distinction in cases like *Bailey v. Drexel Furniture Co. (Child Labor Tax Case)*, 259 U.S. 20 (1922); *Hill v. Wallace*, 259 U.S. 44 (1922); and *United States v. Constantine*, 296 U.S. 287 (1935), where it struck down various taxing schemes on the ground that they were designed to penalize, alter, or prohibit behavior rather than simply to raise revenue. But by 1937, the Court realized that the distinction between regulatory and revenue-raising enactments was untenable, because "*Every tax is in some measure regulatory*....But [it] is not any less a tax because it has a regulatory effect." *Sonzinsky v. United States,* 300 U.S. 506, 513 (1937)(emphasis added); *see also United States v. Kahriger*, 345 U.S. 22, 31 (1953)(upholding a tax on wagering even though it "has a regulatory effect"); Erwin Chemerinsky, *Constitutional Law: Principles and Policies* 201 (1997)("deciding whether a tax should be characterized as regulatory or revenue generating is inherently arbitrary").

The "intelligible principle" issue is discussed in some detail in the States' Opening Brief at pages 26-28, and that discussion will not be repeated here. The extensive list of decisions cited in footnote 12 of the Opening Brief, on pages 27-28, illustrates the flexibility allowed by

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Maritime Authority exacts two separate charges from companies operating in the exclusive economic zone – one is a per vessel charge that ranges from $250 to $600 per vessel, and the other is based on 5% of the estimated value of the expected landed catch. *See* States' Opening Brief at page 12 and App. 102, 107, 112A, 125. The National Government's position on the regulatory nature of the exaction might possibly be supported regarding the per-vessel charge, which might roughly cover the administrative expenses of the MMA, but it is certainly incorrect regarding the second element of the charge, based on the expected value of the catch, which, the National Government acknowledges, greatly exceeds any costs of regulation.

courts reviewing administrative agency actions. In the present case, the record establishes that the Micronesian Maritime Agency starts with the standard rate of 5% of the estimated value of the expected landed catch and then makes adjustments authorized by the Marine Resources Act. The requirement that Congress approve any arrangement involving ten or more vessels ensures consistency and conformity with the statutory guidelines. Such a program is surely within the requirements of *J.W. Hampton* and its progeny, and is constitutional. [10]

Probably *the clearest indication that the fishing revenues are viewed as "taxes"* by the decisionmakers in the FSM is that the business gross revenue tax is not imposed upon the foreign and domestic based fishing companies' revenues from the export sales of fish caught in FSM waters. See 54 FSMC 112(5)(h). The gross revenue tax (GRT) of 3% that applies to all other entrepreneurial activity in the FSM is *not imposed upon these companies*, because it is

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[10] Both the Briefs of the National Government and the Congress raise concerns about the third prong of the trial court's test to determine whether an exaction is a tax or a fee, namely "whether it is voluntary, and produces a benefit to the payor which is commensurate with the payment." The States pointed out at page 30 of their Opening Brief that this distinction is not "helpful in determining the nature of an assessment," because "[e]very payment to the government produces a benefit to the taxpayer because the taxpayer receives government services..." The National Government cites *Wright v. McLain*, 835 F.2d 143 (6th Cir. 1987), as example of a tax without a benefit, but of course in that case the taxpayer – a parolee – gained the very substantial benefit of being out of jail and on parole, and the moneys collected were utilized to cover "the cost of his supervision and rehabilitation." *Id.* at 144. Congress asserts at page 4 of its Brief that "appellants cite no authority supporting the notion that an employee who has not paid his income tax can be precluded from working." This is an odd assertion, because in many jurisdictions, such as the United States, employees can be and are put into jail for not paying their income tax, and so in that sense they are very definitely "precluded from working." In the FSM, employers are given the responsibility of paying the taxes on behalf of the employees, but self-employed individuals, such as attorneys, can definitely lose their license to practice, and thus be "precluded from working," if they do not pay their gross revenue tax. In any event, these and the many other examples offered in the States' Opening Brief support the conclusion that a distinction based on whether an exaction is "voluntary" will not be helpful, because every payment is in some sense voluntary and in another sense obligatory and burdensome.

understood that the revenues collected from them are "in lieu of" the GRT tax, *i.e.*, they are another form of tax.

D. The Assertion in Congress's *Amicus* Brief That the Fishing Revenues Could Be Taxes That Are Not Included in Sharing Requirements of Article IX, Section 5 Is Groundless Because These Taxes Are Collected Based on Income and They Are Deposited into the General Fund.

1. The Fishing Revenues Are Taxes on Income.

The revenues collected from fishing licenses are taxes based on "income"and are deposited in the General Fund,[11] just like any other tax. At page 35, the National Government's Brief argues that these revenues are not "income" tax because they are based on "a percentage of the *estimated value* of the *estimated* gross receipts or income"of the fishing company, rather than on the actual value of the actual landed catch (emphasis in the National Government's Brief). As explained in the States' Opening Brief at 28, this formula has been used for the very practical and important reason that the revenues must be collected in advance, because the companies have no assets in or permanent commitment to the FSM. It is not unusual to assess a tax on the appraised value of an asset or revenue stream rather than on its actual value, and such a system is commonplace when practical obstacles prevent a precise valuation.[12] For those companies that do fish in FSM waters for a number of years, the annual adjustments based on the previous year's catch constitute the "rebate" that the National Government's Brief recommends on page 35. But for

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[11] The National Government Brief acknowledges at page 26 that these revenues "are deposited in their entirety in the General Fund of the FSM."

[12] Other examples utilizing estimated values or rough approximations to collect taxes include the flat $80 tax imposed on all incomes in the FSM below $10,000, and the practice of some of the States to impose excise taxes based on the estimated fair market value of imported cars, rather the actual purchase price of the vehicles. See FSMC Section 141(1).

those foreign companies that fish for only one year, the "up-front" payment is essential to ensure that the government receives a fair payment for the opportunity to harvest the rich bounty of Micronesia's waters.[13] A ruling by this Honorable Court that interpreted the words "income," "tax," or "revenue" so narrowly that it denied the government the opportunity to adopt logical taxing programs to deal with the practicalities of unique industries could cripple the country's efforts to be flexible and creative in order to build a sound economic base.

2. The National Government's Power to Tax Is Limited to Taxing Income and Imports.

The FSM National Government is a government of enumerated powers, and it has only those powers explicitly delegated to it in the FSM Constitution. FSM Constitution, Article VIII, Section 1. The only powers to tax included in the listing of enumerated powers of Article IX, Section 2 are the powers to tax imports and income. Article IX, Section 2(d) and (e). The power to establish a social security system is also authorized in Article IX, Section 3(d).

Congress's *Amicus* Brief argues at page 5 that the National Government also has the power to impose taxes incidental to other express powers of the National Government or other powers "indisputably national in character." But no citations or support are offered in support of that proposition, and the States would submit that something as an important as a tax can never be viewed as "incidental," but must always have its own explicit Constitutional authorization. *See, e.g., Pollock v. Farmer's Loan & Trust Co.*, 157 U.S. 429 and 158 U.S. 601

[13] Indeed, the National Government's Brief appears to concede on page 39 that the collection of revenues from fishing licensees is based on a fixed percentage of gross revenue when it says "fishing fees are indeed assessed at a rate which is a fair approximation of the benefits to the fee payer."

(1895)(declaring unconstitutional a tax upon income from real and personal property in the absence of apportionment); the long struggle in the United States regarding whether the national government could impose an income tax was resolved only with the passage in 1913 of the Sixteenth Amendment, which specifically authorized such a tax. (The National Government's Brief apparently agrees with the States on this matter, because it says at page 45 n.42 that the National Government's "taxing power is limited to taxes on imports and taxes on income.")

The Con Con history cited on pages 6-8 of Congress's *Amicus* Brief naturally refers only to the sharing of taxes based on income or imports, because those were the only national taxes authorized by the Constitution. Congress is correct at page 8 of its *Amicus* Brief that the sharing requirements of Article IX, Section 5 do not apply to the social security system, because that program is separately authorized in Article IX, Section 3(d), and is not characterized in the Constitution as a tax. The revenues collected under this program go into a separate retirement fund and thus do not go into the general fund, unlike the revenues collected from fishing licensees, the gross revenue tax (GRT), and import taxes.

E. The Collection of a Tax from Fishing Companies Is Not Inconsistent with the United Nations Law of the Sea Convention.

Congress's *Amicus* Brief argues at page 3 that imposing a tax on fishing companies would be inconsistent with the authority given to coastal and island countries in Article 62(4)(a) of the United Nations Law of the Sea Convention to collect "fees and other forms of remuneration." No evidence or authority is provided, however, to support the view that this phrase was meant to be interpreted narrowly, and in fact the Convention grants coastal and island countries broad and unreviewable authority to regulate their exclusive economic zones. The

Convention establishes mandatory sophisticated procedures for resolving disputes among countries, but explicitly exempts disputes involving "the terms and conditions established in [a coastal or island country's] conservation and management laws and regulations." Article 297(3)(a). Thus, each country has authority to establish the financial arrangements governing access to its fishing resources, and its decisions cannot be challenged elsewhere in any regional or international tribunal.

Perhaps more importantly, it must be reiterated that the FSM obtains its authority to collect revenues from fishing licensees from its own Constitution, not from the United Nations Law of the Sea Convention. The FSM did not accede to the Law of the Sea Convention until April 29, 1991, long after it had been collecting fishing license fees pursuant to its own constitutional structure. The Law of the Sea Convention confirms that collecting revenues is legitimate, but it is not the source of the authority to collect such revenues. And if the FSM Constitution and the Law of the Sea Convention were somehow found to be inconsistent, the principles of the Constitution would clearly prevail under Article II, Section 1 of the Constitution which says that any act "in conflict with this Constitution is invalid to the extent of conflict."

III. THE FOUR STATES ARE THE UNDERLYING SOVEREIGN OWNERS OF THE MARINE RESOURCES IN THE EXCLUSIVE ECONOMIC ZONE.

A. The Marine Resources in the Exclusive Economic Zone Are Within the Sovereign Control of the Adjacent Coastal or Island Country.

The National Government's Opening Brief devotes considerable energy to trying to establish that the marine resources of the exclusive economic zone are not capable of being

"owned" by anyone and hence that the States cannot be the underlying owners of these resources, and even claims to have discovered a "concession" in the Pohnpei State Brief that such resources cannot be "owned." National Government Brief at 5 n.3 and 14. It is true, of course, that swimming fish are not "owned" by anyone until they are caught and put into the hold of a vessel. It is also true that the exclusive economic zone is a unique legal construct that carefully balances the competing rights of the coastal populations and the need for maritime mobility. The 1982 United Nations Law of the Sea Convention avoids explicitly using the words "own" or "ownership" to describe the rights of the coastal and island countries, because the *waters* in the exclusive economic zone are *not* owned by the coastal country even though it can exercise *exclusive sovereign control* over the *resources* in and under those waters.[14]

Article 56 of the Convention says that the coastal country has "*sovereign rights* for the purpose of exploring and exploiting, conserving and managing the natural resources, whether living or non-living" (emphasis added). The strong term "sovereign" was utilized to make it clear that the coastal country has the capacity to control these resources, to harvest them itself, or to determine who else can harvest them. Later in this same article, the drafters used the somewhat weaker term "jurisdiction" with regard to other rights of the coastal country, to make it clear that the coastal country had reduced capacity to control other activities.

The question in the present case does not concern the international regime governing ocean resources, but instead involves the underlying sovereignty over these resources as between the Four States and the National Government of the FSM. The States' position is that the FSM

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[14] The Convention seeks to keep the waters free from coastal ownership in order to preserve the maximum amount of navigational freedom through and over those waters.

Constitution preserves their underlying sovereignty over these resources, even though the authority to *regulate* them has been delegated to the National Government, much like a beneficiary delegating management authority of assets to a trustee.

The *Amicus* Brief of the Congress cites the case of *Baldwin v. Fish and Game Commission of Montana*, 436 U.S. 371 (1978), and that case is instructive regarding the concepts of "ownership" involved in the present case. In the *Baldwin* opinion, the U.S. Supreme Court emphasizes that recognizing "ownership" of natural resources by the residents of the 50 states within the United States is more than a legal fiction because it acknowledges "'the importance to its people that a State [referring to one of the 50 states within the United States] have power to preserve and regulate the exploitation of an important resource.'" *Id.* at 386 (quoting from *Douglas v. Seacoast Products, Inc.*, 431 U.S. 265, 284 (1977), and *Toomer v. Witsell*, 334 U.S. 385, 402 (1948)). The Court went on to say in *Baldwin* that "[t]he fact that the State's control [again referring to the 50 states] over wildlife is not exclusive and absolute in the face of federal regulation and certain federally protected interests does not compel the conclusion that it is meaningless in their absence." *Id.* The U.S. Supreme Court thus recognized the different meanings that the concept of "ownership" can have, particularly in the context of wild living creatures, and affirmed that the 50 states in the United States do have a form of "ownership" over the wild creatures within their borders, even in situations of extensive regulation by the national government.

B. The Districts That Formed the Federated States of Micronesia Relinquished to the National Government the Rights Enumerated in the FSM Constitution, But Retained All Other Rights.

The National Government's Brief at 8 correctly notes that the States "relinquished" their "separate political status" when they came together to form the FSM and are not now "states" as that term is used under international law, to refer to independent political entities. But the fact that the States did have separate political status prior to their creation of the FSM[15] provides important guidance to the relationships between the States and the National Government and, in particular, to the question of whether the States "relinquished" their marine resources to the National Government. The National Government acknowledges that those Districts that did not join the FSM retained their marine resources,[16] and that the Four States could also have done so had they not formed the FSM. This recognition is important, in light of the fact that the FSM National Government is a limited government of enumerated powers, because it must be concluded that the States continue to retain the underlying sovereign ownership of their marine resources unless something in the FSM Constitution indicates that it has been conveyed to the

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[15] The National Government's Brief acknowledges at page 21 n.18 "the *independent political status enjoyed by the districts* under the Trust Territory administration."

[16] It is significant also that the United States currently returns *all* the revenues collected from fishing licensees in the exclusive economic zone (EEZ) around the Commonwealth of the Northern Marianas Islands (CNMI) to the CNMI treasury for conservation and management purposes (and similarly returns revenues collected from fishing licensees in the EEZs around Guam and American Samoa to their treasuries). 16 U.S.C.A. sec. 1824(e)(6)(1999). In other words, the United States recognizes just exactly what the Four States are seeking in the present case – that each of its affiliated Pacific Island political entities is entitled to share in the revenues collected from those fishing in the waters surrounding its islands. With regard to the CNMI, this recognition is particularly significant, because the United States has confirmed that a political entity that was once a district in the Trust Territory of the Pacific Islands retains sufficient autonomy, even after it has come under the formal sovereignty of the United States, to share in the revenues generated by the resources harvested in its surrounding waters. If the CNMI can share in the fishing revenues its waters generate, certainly the Four States of the FSM should also be able to share in the bounty generated by their surrounding waters.

National Government. FSM Constitution, Article VIII, sec. 2.[17]

This conclusion is confirmed by reviewing the decisions made by the delegates to the 1975 Micronesian Constitutional Convention. They met at a time when it seemed probable that extended maritime zones would be recognized by the international community, and while the Micronesian Delegation to the Law of the Sea Conference was working hard to promote that outcome. Everyone accepted that the States had jurisdiction over the nearshore coastal resources in the territorial sea. But what would be the status of the waters beyond the territorial sea? Were these waters and their resources to be like a "black hole," unclaimed and unowned by any sovereign entity? That seems to be the position of the National Government, which has reiterated on page 10 of its Opening Brief its belief that "neither Article I, section 1, nor any other section of the Constitution confers ownership rights over the marine resources on either the national government or the States."

But is it possible that the delegates to the 1975 Con Con were content to leave such an important subject in a state of limbo? In fact, whenever the subject came up, the delegates made it clear that they understood these waters and their resources to belong to the States. This result can be confirmed by examining Article I, Section 1 (referring to "the waters connecting the islands of the archipelago" as "internal waters"),[18] Article I, Section 2 (giving a generous

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[17] Contrary to the characterization in Congress's *Amicus* Brief at 11, the States did not convey their underlying sovereign "ownership in trust to the national government when they ratified the Constitution, retaining beneficial ownership." They retained their underlying sovereign ownership over the marine resources, but conveyed the right to regulate these resources, just as a person conveys to a trustee the right to manage assets for the benefit of the person.

[18] Although at page 2 n.12, the National Government's Brief dismisses the idea that

definition to "state boundaries," which were to be determined by "equidistance," and which could not be changed except "with the consent of the state legislatures involved"), Article IX, Section 6 (recognizing the rights of the States to their share of the revenues from "ocean floor mineral resources"),[19] and Standing Committee Report No. 9, which anticipates the States receiving revenue from marine resources by saying that "It is the intent of the Committee that this method [i.e., the principle of equidistance] be utilized to establish fair and equitable marine boundaries in the event marine resource revenues should accrue to the State wherein the resources are found." 2 *J. of 1975 Micro. Con. Con.* 777, Standing Committee Report No. 9.[20]

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waters in the FSM could qualify as "archipelagic waters," other authors have argued that at least some waters in the FSM could meet the Law of the Sea Convention's definition of archipelagic waters. *See* Sequoia Shannon, *An Exercise in Maritime Delimitation for Archipelagic States*, in *Ocean Yearbook 12* at 334-57 (E.M. Borgese, N. Ginsburg, & J.R. Morgan eds. 1996). If archipelagic waters do exist, these waters would certainly be within the boundaries of the States in which they are located.

[19] This provision is designed to ensure that the National Government receives administrative costs to reimburse it for the expected substantial investments required to exploit these minerals. The provision was *not* included to give the States revenue, because the States would have been entitled to these revenues in the absence of any specific provision, but rather to ensure that the National Government would receive enough revenue beyond its administrative costs to provide an incentive to exploit these minerals. No comparable provision was required for fishing revenues, because no comparable capital investment by the National Government was anticipated.

[20] At page 9 n.8, the National Government Brief refers to the decision of the trial division in *FSM v. Ting Hong Oceanic Enterprises Co.*, Crim. Case No. 1994-502 (Sept. 3, 1996)(Memorandum of Decision Regarding Order Denying Defendant's Motion to Dismiss). This unpublished decision of the trial division was issued in a case in which none of the Four States were parties, and hence cannot be viewed as binding upon them. More significantly, its facts are dramatically different from those in the present case. The issue was the proper venue for a criminal prosecution, as between the Chuuk and Pohnpei trial divisions of the FSM Supreme Court. The case did not involve any dispute between the States and the National Government. It was essentially a *forum non conveniens* dispute, regarding which branch of the trial division was most appropriate in light of the competing interests of the litigants. After

The only constitutional provision arguably pointing in the other direction is Article IX, Section 2(m), but this section is also carefully drafted to delegate to the National Government *only* the power and responsibility *"to regulate"* the ownership and exploitation of marine resources, and makes no mention of the power *to distribute* the revenues from these resources.[21] *See* Opening Brief of the States at pages 43-45. The National Government's Brief does not dwell at length on Article IX, Section 2(m), but instead relies heavily on Article IX, Section 1, which gives the National Government authority over matters that are of "an indisputably national character." In the States' Opening Brief at pages 43-45, it is explained that although collecting fishing revenues can be considered to be a matter of "national character," it is impossible to support the view that distributing these funds is also of such a character. The National

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balancing these interests, the court determined that venue in the Pohnpei trial division was proper. The comments regarding whether the arrest occurred within one of the Four States are purely dicta and unnecessary for the decision rendered, and in any event they are clearly contrary to the explicit language in Article I, Section 2 of the FSM Constitution, which declares that the boundaries of each State extend to the boundary of the adjacent State, utilizing "the principle of equidistance."

[21] The National Government Brief asks rhetorically at page 15 whether the National Maritime Act, 19 FSMC sec. 101 *et seq.* would be unconstitutional under the States' view that all the waters surrounding the islands of the FSM are state waters. The States would, of course, answer that question in the negative, because the National Maritime Act is a logical and constitutional enactment under the power delegated to the National Government in Article IX, section 2(m) to "regulate" the resources in those waters.

Government's Brief agrees with this conclusion at page 19,[22] but at page 20 contradicts itself by asserting (without support, logic, or elaboration) the opposite result.[23] Congress's *Amicus* Brief asserts at page 14 that the States' view that the power to collect and distribute revenues are different in nature and kind "betrays some naivete." If so, the framers of the FSM must have been naive, because they clearly required in Article IX, Section 5 that half of all revenues collected to be shared with the States. With regard to other taxes, these revenues have been shared, so we know that this practice does not, as the Congress warns in its *Amicus* Brief at page 14, "distort incentives" or "worsen...relations between the two levels." It should also be noted that the National Government's Brief makes no attempt whatsoever to respond to or distinguish the historical material and analysis in Section V(6) of the States' Opening Brief (pages 47-53), which explains why the FSM Constitution does not specifically address the question of how fishing revenues should be distributed.

IV. CONCLUSION.

For these reasons, and those articulated in the States' Opening Brief, the Four States respectfully request this Honorable Court to reverse the Judgment and Order issued by the Trial Division in this case.

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[22] "The States are correct in their assertion that the power to distribute revenues is not 'indisputably national' in nature."

[23] "The authority to regulate the FSM EEZ is inherently national in character, and includes the capacity to collect and distribute revenues from fishing fees."

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CERTIFICATE OF SERVICE

I certify that a copy of Appellants' Reply Brief was served by hand this 7th day of March, 2000 on

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