



**U.S.-Korea Relations:
Finally Progress on the Feb. 13 Joint Agreement**

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Concerted efforts by the U.S., China, South Korea, and Russia in mid-June finally overcame “technical problems” and led to the return of approximately \$25 million in frozen funds to North Korea. After helping to break this logjam, U.S. chief envoy to the Six-Party Talks Christopher Hill traveled to Pyongyang for meetings with the DPRK foreign minister and chief delegate to the Six-Party Talks.

Hill strived to accelerate North Korea’s compliance with the Feb. 13, 2007 joint agreement by urging Pyongyang to quickly accept inspectors from the International Atomic Energy Agency (IAEA), shut down its nuclear facilities, and participate in a new round of nuclear negotiations in July. Hill’s meetings were the highest level of U.S. bilateral contacts with North Korea’s regime since October 2002.

The U.S. and South Korea signed the free trade agreement (FTA) at the end of the quarter, just one day before President Bush’s “fast track” authority to negotiate trade agreements expired. Despite the positive notes struck by U.S. and Korean trade officials, however, Democratic Congressional leaders immediately announced they would oppose the FTA because it adversely affected U.S. auto manufacturers and workers. Democrats, who control Congress following the 2006 mid-term elections, are likely to block ratification of the FTA unless the Bush administration undertakes a strong lobbying effort in the coming months.

Resolving the BDA issue

From the beginning of April through early June, U.S. diplomats struggled with transferring approximately \$25 million in North Korean funds held in a Macau bank to Pyongyang. The Banco Delta Asia (BDA) originally froze these funds at the request of the U.S. Treasury in the fall of 2005, because the monies were reportedly derived from counterfeiting and other illegal activities. When North Korea entered into the Feb. 13, 2007 joint agreement to shut down its reactors, the U.S. provided an explicit though unstated *quid pro quo* to facilitate return of the seized monies.

At the time that Ambassador Hill made this promise, he could not have anticipated the difficulties in transferring the funds. As he put it at the last round of Six-Party Talks in March, the “political will” to return the funds to North Korea existed among all the parties but “technical difficulties” prevented its immediate implementation.

As diplomats quickly ascertained, virtually all international banks refused to be conduits for monies associated with North Korea’s counterfeiting and money-laundering. Reportedly, Hill and other U.S. diplomats spent much of April and May making “cold calls” to U.S. and other financial institutions, seeking unsuccessfully to arrange a pipeline for returning the North Korean funds.

While the funds issue was percolating and holding up the next round of Six-Party Talks, U.S. Ambassador to the ROK Alexander Vershbow sent two important diplomatic signals in the first half of May. He first attempted to curb Seoul’s enthusiasm for moving ahead on bilateral relations with Pyongyang while the BDA funds issue remained unresolved and while Pyongyang was unwilling to move ahead on the nuclear negotiations. Vershbow chided Seoul saying that its engagement policy should run at the same pace as North Korea’s participation in the denuclearization process described in the Feb. 13 agreement. In spite of the U.S. ambassador’s intervention, South and North Korean officials worked feverishly to arrange for two trains to cross the Demilitarized Zone (DMZ) in mid-May for the first time since the Korean War.

Vershbow made a second important statement May 9, more in line with Seoul’s political aspirations and current policy direction. He suggested that even before President George W. Bush left office in early 2009, it might be possible to negotiate a new peace treaty for the Korean Peninsula that would replace the 1953 Armistice Agreement.

Despite Vershbow’s efforts to put the nuclear negotiations in a larger political context, North Korea was publicly unimpressed. On June 1, Pyongyang reaffirmed that it rejected any further steps to implement the Feb. 13 denuclearization agreement until it received back in full the \$25 million in funds frozen in the Macau bank.

Concerted efforts by the U.S., China, South Korea, and Russia led finally on June 17-19 to the return of North Korean funds at the BDA to Pyongyang, via a Russian commercial bank. North Korea had insisted on obtaining the monies through normal banking channels to reaffirm its access to the international financial system. In response, North Korea announced that it would allow IAEA inspectors to enter the country, as a means of implementing the Feb. 13 joint agreement.

The White House praised the announcement, saying “this is a good step. Now we can hopefully continue on the path set out in the agreed Feb. 13 framework that will lead to a nuclear-free Korean Peninsula.”

Ambassador Hill travels to Pyongyang

Resolution of the long-standing BDA issue led to an apparently quick decision by Ambassador Hill to visit Pyongyang on June 21 for two days of talks with North Korean officials. The very fact of the visit – the first by a ranking U.S. ambassador since October 2002 – had critical significance since it demonstrated U.S. willingness to deal directly with North Korea, as Pyongyang has long demanded.

When Hill later traveled to South Korea for meetings with Foreign Ministry officials, he gave an upbeat review of his discussions in Pyongyang, saying “the talks were very detailed, very substantive, useful, and positive.” He said that based on his meetings with North Korea’s ambassador to the Six-Party Talks, Kim Gye-gwan, and Foreign Minister Pak Ui-chun, North Korea was prepared to promptly shut down its nuclear facilities consistent with its commitment in the Feb. 13 agreement.

During his press conference in Seoul, Hill underscored the U.S. intention to achieve a “comprehensive solution” of outstanding issues with North Korea, as referenced in the Feb. 13 agreement and the September 2005 statement of principles. Such a comprehensive solution could prospectively include a variety of measures:

- a denuclearization agreement;
- a new peace agreement that replaces the 1953 Armistice;
- a regional multilateral security mechanism;
- normalization of U.S.-North Korea relations; and
- a Japan-North Korea agreement.

North Korea gave its own assessment of talks with Ambassador Hill on June 23 in a Foreign Ministry statement that said that the discussions held by Washington and Pyongyang “were comprehensive and very productive.” The statement added that the two governments “agreed to consider the possibility of opening a meeting of six-party chief delegates in early July and a six-party foreign ministerial meeting on the sidelines of the ASEAN Regional Forum, which will be held in the Philippines in early August, and cooperate to achieve those goals.”

A North Korean Foreign Ministry spokesman also confirmed that Pyongyang would respect the wishes of U.S. Treasury Department officials who urged in March that any frozen funds obtained from the BDA be used for humanitarian purposes. He said that “the released money is planned to be used to improve the livelihood of the people and other humanitarian purposes as agreed” with the U.S.

After traveling from Seoul to Tokyo to brief Japanese officials, Hill stressed that the U.S. “really thinks this is the time to pick up the pace” in implementing the Feb. 13 joint agreement. He said that Washington expects Pyongyang to shut down its main reactor approximately three weeks after North Korea and IAEA nuclear inspectors agree on monitoring procedures. At that point, under the Feb. 13 agreement, North Korea would

receive 50,000 tons of heavy fuel oil which would be supplied by South Korea at a cost of approximately \$21 million.

For his part, South Korean President Roh Moo-hyun chose to highlight the broader significance of North Korea's decision to begin shutting down its nuclear facilities. He pointed out that "North Korea's denuclearization pledge will become an important milestone leading to permanent peace on the peninsula and a multilateral security structure for Northeast Asia. Sustained peace on the peninsula would eventually make possible an overland road trip from South Korea to the North, China and Russia, opening a new horizon for the Korean economy."

Despite the political breakthroughs in implementing the six-party agreement, the quarter came to an end on a sour note. On June 27, North Korea conducted its third short-range missile test in approximately 30 days. The White House National Security Council spokesman Gordon Johndroe, on the same day, said the U.S. was "deeply troubled" by the repeat missile launches and urged North Korea to refrain from activities that destabilized the region.

Ups and downs for KORUS

In early May, the U.S.-Korea Free Trade Agreement (KORUS) ran headlong into the new reality of Democratic Party control of Congress, following the November 2006 elections. Congressional leaders, led by Speaker of the House Nancy Pelosi, pushed hard and obtained Bush administration support for new "trade policy guidelines" for environmental and labor rights that must be included in all pending and future U.S. trade agreements.

Under the new guidelines, South Korea would have to agree to the following:

- Adopting and enforcing laws that abide by basic international labor standards that are outlined in a 1998 declaration of the International Labor Organization.
- Incorporating commitments to labor rights in the body of the free trade agreement, rather than in the usual form of a side agreement.
- Adopting and enforcing laws that implement a number of key multilateral environmental agreements.
- Taking steps that make it easier for poor people to obtain access to cheaper generic drugs.

Shortly after Congressional and administration officials announced the new guidelines, Ambassador Vershbow stressed in Seoul the need for South Korea to incorporate these requirements. He said that "we need to work together in the coming weeks. Both of us, global leaders in terms of labor and environmental standards, can find a way to reflect a strong commitment to these standards."

Although the new U.S. policy applied broadly to current trade negotiations and agreements with Peru, Panama, and Colombia as well as South Korea, Korean officials initially rejected the idea of “renegotiating” the FTA. Trade Minister Kim Hyun-chong initially told Vershbow that such a renegotiation would be “impossible.” Even more emphatically, chief South Korean negotiator Kim Jong-hoon said “if the U.S. demands South Korea renegotiate to reflect its unilateral view, we could break down the agreement. We couldn’t one-sidedly accept a request to renegotiate the agreement that already reflects the balance of interests.”

Three days later, on May 18, chief negotiator Kim announced a change in position, after intervention by South Korea’s Blue House. Kim said “if the U.S. officially asks for renegotiation of the South Korea-U.S. FTA, we will thoroughly consider whether the proposal has an aspect of reflecting interests on both sides.”

The result of final negotiations in Seoul that began June 21 was not surprising, given the strong desire of President Roh to achieve the FTA as a main element of his legacy. South Korea accepted the U.S. demands to include new policy guidelines in the FTA. Prime Minister Han Duck-soo justified the South Korean decision on two grounds. For one thing, he said, “if the amendments aren’t reflected in the agreement, the South Korea-U.S. FTA may not be endorsed by the U.S. Congress.” Additionally, he pointed out, in accepting the new policy guidelines, Korean negotiators were able to “block further requests by the U.S. Congress on automobiles, rice, and other items.”

On June 30, one day before President Bush’s “fast-track” authority to negotiate trade agreements expired, the U.S. and South Korea officially signed their FTA in Washington. U.S. Trade Representative Susan Schwab struck a positive note when she said that “America’s economic future depends heavily on more free trade agreements like the one we are signing today with Korea.”

However, signs that the FTA faced an uncertain fate in both Korea’s National Assembly and the U.S. Congress were fully evident on the day of signing. In Seoul, thousands of farmers and workers marched and chanted anti-FTA slogans, apparently not mollified by government promises of assistance to economic sectors that could be hurt by U.S. imports.

In Washington, Speaker Pelosi and other House Democratic leaders issued a public statement opposing the FTA. They said that “Unfortunately, the [FTA] as currently negotiated is a missed opportunity. We cannot support the [FTA] as currently negotiated.” House Democrats are particularly upset that the FTA, as signed, does not sufficiently open the Korean market to U.S. automobiles at the same time as it eliminates U.S. tariffs on Korean-made cars and pick-up trucks.

Prospects

The Six-Party Talks are once again moving forward, after overcoming the unexpectedly difficult problem of transferring frozen bank funds back to North Korea. Mired in Iraq, the U.S. administration is seeking a diplomatic “win” in these negotiations. North Korea increasingly appears to want a settlement as well – although it likely will resist pressure to give up the nuclear material it has already produced. It is hard to believe that late last year, North Korea defied the world by exploding a nuclear device and the Six-Party Talks appeared destined to fail.

In statements issued following Ambassador Hill’s visit to Pyongyang, both the U.S. and North Korea referred to seeking a “comprehensive” solution of issues taken up in the Six-Party Talks. Along with denuclearizing North Korea, these issues include: 1) achieving a permanent peace arrangement for the Korean Peninsula that replaces the 1953 Armistice; 2) establishing a multilateral security mechanism in Northeast Asia; 3) resolving bilateral U.S.-North Korea disputes leading to normalization of relations; and 4) striving for a resolution of outstanding conflicts between Japan and North Korea.

Clearly, the U.S. would not be willing to move forward significantly on these additional issues until North Korea has frozen its nuclear facilities and is proceeding down the path of denuclearization. Once that occurs, however, parallel negotiations on these other important issues could lead to an even bigger negotiating breakthrough than occurred in the 1994 Agreed Framework.

The U.S.-Korea FTA has encountered serious obstacles in the U.S. Congress that, left unaddressed, will block ratification of this agreement. The most critical issue is the automobile sector, where Michigan members of Congress, with the support of organized labor, have the backing of Speaker Pelosi and other Democratic leaders. Sen. Hillary Clinton has also voiced opposition to this agreement, as currently drafted. Although members of Congress publicly call for greater opening of South Korea’s auto sector, their core concern is reportedly USTR’s decision to give up tariff protection for U.S. autos, particularly a 25 percent tariff on imports of pick-up trucks.

The Bush administration will have to undertake a strong lobbying effort on Capitol Hill to achieve ratification of the U.S.-Korea FTA. In so doing, it would be well advised to reach an accommodation with Michigan members and representatives of organized labor that compensates for any negative impact of the FTA on the U.S. automobile sector.

Chronology of U.S.-Korea Relations

April-June 2007

April 1, 2007: U.S. and South Korea concludes free trade agreement.

April 26, 2007: The second ROK-U.S. Consultations on Reconstruction and Stabilization is held to share experiences with providing emergency relief and reconstruction assistance for countries hit by natural disasters.

May 4, 2007: U.S. Ambassador to South Korea Alexander Vershbow says South Korea's policy of engagement with North Korea should keep pace with denuclearization process.

May 9, 2007: Amb. Vershbow says a peace treaty ending the Korean War could be negotiated before President George W. Bush's term ends.

May 10, 2007: Washington announces new trade policy that incorporates labor, the environment, and intellectual property rights protection.

May 11, 2007: ROK Trade Minister Kim Hyun-chong tells Amb. Vershbow that FTA renegotiations would be "impossible."

May 15, 2007: Amb. Vershbow says the U.S. seeks to revise U.S.-Korea FTA based on new U.S. trade policy guidelines that call for higher labor and environmental standards.

May 16, 2007: Chief South Korean FTA negotiator Amb. Kim Jong-hoon tells *Yonhap News* in a phone interview that "if the U.S. demands South Korea renegotiate to reflect its unilateral view, we could break down the agreement. We couldn't one-sidedly accept a request to renegotiate the agreement that already reflects the balance of interests."

May 16, 2007: Washington presents Seoul with specific text based on the new trade policy guidelines incorporating labor and environment concerns and a request to hold additional bilateral consultations in the later half of June.

May 17, 2007: North and South Korea do a test-run of linked train lines. To do the test, South Korea agreed to supply the North with \$80 million of aid to develop light industry.

May 18, 2007: South Korea says it will "thoroughly consider" the U.S. request for renegotiation of the FTA.

May 22, 2007: PM Han Duck-soo says that Korea will not renegotiate the FTA even if requested by the U.S., however further talks are possible as "additional negotiations."

May 25, 2007: The full text of the U.S.-Korea FTA is released.

May 29-June 6, 2007: Korean and U.S. FTA delegations meet in Washington to complete the legal review process of the FTA text.

June 1, 2007: North Korea rejects implementing the Feb. 13 denuclearization agreement until the BDA dispute is resolved.

June 7, 2007: North Korea conducts a short-range missile test off its western coast.

June 8, 2007: The 13th Security Policy Initiative is held in Seoul. Topics covered relocation of U.S. bases and transfer of wartime control from the U.S. to South Korea.

June 19, 2007: Ambassador Hill says BDA funds have been transferred to North Korea.

June 19, 2007: ROK FM Song Min-soon and Secretary Rice consult by phone over the North Korean nuclear issue and the KORUS FTA.

June 19, 2007: Seoul holds inter-agency ministers' meeting to discuss the ROK's position on Washington's proposal based on new U.S. trade policy guidelines.

June 21-22, 2007: U.S. head nuclear talks envoy Amb. Hill visits Pyongyang and has discussions on "all aspects of the six-party process" with DPRK Foreign Minister Pak Ui-chan and nuclear talks counterpart Kim Gye-gwan.

June 21-22, 2007: U.S. and South Korean negotiators begin talks in Seoul to negotiate additional FTA proposal submitted by the U.S.

June 22, 2007: Amb. Hill announces in Seoul that North Korea has reaffirmed its willingness to shut down its nuclear reactor under the Feb. 13 agreement.

June 25, 2007: North Korea announces that it has received funds from the BDA accounts.

June 26-29, 2007: IAEA inspectors visit the Yongbyon nuclear facility and the under construction facility in Taechon in North Korea.

June 27, 2007: A White House spokesman says the U.S. is "deeply troubled" by repeated North Korean short-range missile tests, which occurred on May 25, June 7, and June 27.

June 29, 2007: South Korean PM Han Duck-soo says Korea has accepted new U.S. labor and environmental standards in the FTA, to further U.S. congressional ratification.

June 30, 2007: U.S. and South Korean officials sign the FTA in Washington despite threat from Democratic Congressional leaders to oppose ratification of the agreement.

July 2, 2007: At a forum in Seoul, Gen. Burwell Bell, commander of U.S. Forces Korea, comments that North Korea remains a threat despite its move toward dismantling their nuclear program.