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North Korea-Japan Relations: The Normalization Talks and the Compensation/Reparations Issue

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Summary

Japan and North Korea have not established official relations since North Korea was founded in 1948. In 2000, the two countries held three rounds of normalization talks, which had been frozen since 1992. The negotiations, however, broke down in November 2000. In late August 2002, Japanese Prime Minister Junichiro Koizumi announced that, after months of behind-the-scenes negotiations with North Korea, he would travel to Pyongyang on September 17 for a day-long summit with North Korean leader Kim Jong-il to attempt to restart the normalization talks.

The most pressing issue for Prime Minister Koizumi is obtaining North Korean cooperation in resolving the cases of several Japanese allegedly kidnapped by North Korean agents in the 1970s and 1980s. Apparently, it was after receiving signs of progress on this issue that Koizumi decided to make the trip to Pyongyang. Japan also is seeking North Korean commitments to curb its missile program and to allow international inspections of its nuclear facilities. Koizumi is also likely to raise the incursions by espionage and drug-running ships thought to be of North Korean origin into Japanese waters.

For its part, one of Pyongyang's key demands is that Tokyo compensate North Korea for Japan's colonization of the Korean Peninsula from 1910-1945. Though Japan has resisted using terms such as "compensation" and "reparations," Tokyo has offered to provide North Korea with a large-scale economic aid package, much as it gave South Korea economic assistance when Tokyo and Seoul normalized relations in 1965. North Korea, however, insists that it will only accept "compensation." This disagreement over terminology has contributed to the current deadlock in the normalization negotiations. There are a number of estimates for the present value of the 1965 Japan-South Korea settlement, ranging from as low as \$3.4 billion to over \$20 billion. Reportedly, Japanese officials are discussing a package on the order of \$5-\$10 billion.

Background

Many medium- and long-term policy approaches to engaging North Korea envision the eventual provision of a large-scale economic assistance package to Pyongyang, conditional upon North Korea's cooperation on various military and economic issues. It is widely believed that one of the largest source of economic aid to Pyongyang would come from a prospective Japanese offer of monetary "compensation" for its colonization of the Korean peninsula in the first half of the 20th Century. Japan has agreed in principle to offer an economic package to North Korea, but has been vague about its amount, form, timing, and characterization. Tokyo has played an important economic role in other diplomatic initiatives toward North Korea. Japan, for instance, funds nearly one-quarter of the operations of the Korean Peninsula Energy Development Organization (KEDO), the organization established under the 1994 U.S.-DPRK Agreed Framework to provide North Korea with light-water nuclear reactors in exchange for North Korea's commitment to halt its existing nuclear program.

Ever since the signing of the Agreed Framework, Japan has often appeared torn between a desire to move slowly and deliberately on normalizing relations with North Korea, and worry about becoming isolated from U.S.-South Korea-North Korea diplomacy. Such worries mounted after Kim Dae Jung was elected president of South Korea in 1997 and began pursuing a "sunshine policy" of engaging North Korea, with the support of the Clinton Administration. Tokyo's policy toward Pyongyang has been hardened by North Korea's launching of a long-range Taepodong Missile over Japan in August 1998, new revelations about alleged kidnappings by North Korean agents, and incursions by espionage and drug-running ships thought to be of North Korean origin into Japanese waters. Most recently, in January 2002 Japan suspended food aid shipments – which had been resumed only in October 2001 in hopes of obtaining progress on the alleged kidnapping issue – to North Korea after a confrontation at sea with a suspected North Korean spy boat, which had penetrated into Japan's territorial waters. Japanese officials and commentators generally have welcomed the Bush Administration's hard-line stance toward North Korea, though many have said they are in favor of the two countries resuming a high-level dialogue.

Thus, Prime Minister Koizumi's August 30 announcement that he would travel to Pyongyang came as a surprise to most observers, notwithstanding the fact that Japanese and North Korean officials had made some incremental progress in bilateral talks during the spring and summer of 2002. The most pressing issue for Koizumi is obtaining North Korean cooperation in resolving the alleged kidnapping cases. According to Japanese press reports, the prime minister also is likely to press Kim Jong-il to unilaterally extend its missile-testing moratorium – due to expire in 2003 – and to allow international inspections of its nuclear facilities, one of the Bush Administration's key demands of North Korea. Koizumi reportedly will deliver a message from President Bush to Kim Jong-il regarding steps necessary to restarting U.S.-North Korea diplomatic talks, which have been stalled since the Bush Administration took office.

Koizumi's trip to Pyongyang poses some risks at home and abroad. Although the impending trip has boosted his public opinion ratings in Japan, his political standing is likely to take a sharp fall if he does not return home with evidence of tangible progress on the abduction issue, particularly if North Korea is seen as winning concessions on Japanese economic and humanitarian assistance. Diplomatically, Pyongyang's overtures

to Tokyo – coinciding with recent improvement in talks between North and South Korea and with significant economic policy changes in North Korea – may be a tactic by North Korea to isolate the U.S. from its Northeast Asian allies, thereby increasing pressure on the Bush Administration to enter into talks with North Korea.¹ The outcome of the Koizumi-Kim summit is likely to factor into the Administration decision on whether and when to restart high-level talks, which had been scheduled for July but were postponed indefinitely following a North-South Korean naval battle in June.

The Japan-North Korea Normalization Talks

Disagreements over the Economic Settlement Package. Regarding the size of Japan's economic package to North Korea, official figures have not been released by either side, though Pyongyang reportedly has demanded \$10 billion at minimum. Some Japanese experts believe that North Korea will ask for a settlement in the \$20 billion range. According to Japanese North Korea-watchers, no consensus has been reached in Tokyo on Japan's bottom line, though there have been reports that Japanese officials are discussing a package on the order of \$5-\$10 billion. According to one report in the Japanese press, Japanese officials in October 2000 were considering a \$9 billion package.² Observers suggest that Tokyo will argue that \$2 billion be deducted from the final amount in order to give Japan credit for its \$1 billion contribution to the Korean Peninsula Energy Development Organization (KEDO) and the \$1 billion North Korea owes Japanese sources (mainly Japanese banks) from unpaid debts incurred in the 1970s and 1980s.³

In addition to the size of the settlement, the two sides have clashed over terminology. Japan is refusing North Korea's demand that the package be labeled as "reparations," or even "compensation." Instead, Tokyo has offered to characterize the monies as "economic assistance," as it did in the 1965 Japan-South Korean normalization negotiations.⁴ This semantic dispute has momentarily stalled the talks. Other issues likely to be contentious include the conditions placed on Pyongyang's use of the aid/reparations, and the composition of the money – grants or loans.⁵ Additionally, North Korea is demanding that Japan issue a formal, "legally binding apology" from the Japanese emperor and/or prime minister. Japan has countered that a sufficient apology was extended as part of 1995 statement by then-Prime Minister Tomiichi Murayama expressing regret for Japan's past actions.

Other Issues. Any normalization agreement will be politically difficult for the Japanese government. In recent years, relations with North Korea have become a high-profile political issue in Japan, due to North Korea's 1998 Taepodong missile launch over Japan, its 1999 naval incursion into Japanese waters, and the release of new evidence that

¹ "Koizumi's Pointless Pilgrimage," *The Asian Wall Street Journal*, September 4, 2002.

² Tokyo Shimbun, October 26, 2000.

³ Author's conversations with Japanese North Korea experts following CRS Workshop, "Dealing with North Korea," March 2, 2000; see also Cha, "DPRK Dialogue."

⁴ "Kono Confirms Offering Economic Cooperation to N. Korea," *Kyodo*, August 25, 2000. Japan's position is that since it has never been at war with North Korea, it is not required to pay reparations.

⁵ Cha, "DPRK Dialogue."

Pyongyang kidnapped Japanese citizens in the 1970s and 1980s.⁶ Public opinion polls indicate that most Japanese favor adopting a cautious approach toward North Korea.⁷ Conservative groups in Japan – including many members of the dominant Liberal Democratic Party – opposed the government’s decisions in March and October 2000 to resume shipments of food aid to North Korea, arguing that Japanese assistance should be conditioned on Pyongyang’s cooperation on the abduction cases and on missile and nuclear weapons issues.⁸ An additional concern expressed by these groups is that Japanese compensation or food aid might be used for North Korea’s military rather than for its populace. During the April 2000 talks, the Japanese delegation also raised the issues of North Korea’s alleged drug-trafficking, and its alleged biological and chemical weapons programs.

North Korea may raise the issue of the status of the estimated 200,000-plus pro-Pyongyang ethnic Korean residents of Japan. In late 2001, Japanese authorities arrested a number of officials from credit unions serving this community, on charges of secretly channeling hundreds of millions of dollars to North Korea. Many of these unions have collapsed in recent years, requiring the Japanese government to spend over \$4 billion to repay depositors, a move that has been politically unpopular in Japan. The prospect of future government bailouts could be affected by a negative outcome of the Koizumi-Kim summit.

April 2000 Talks. In the April 2000 Japan-North Korea talks, North Korea insisted that relations be normalized only after completing a “settlement of the past,” a phrase Pyongyang defines to include four items: an apology, compensation, the return of cultural assets taken from Korea during the occupation, and the granting of legal status to ethnic Koreans living in Japan. For future negotiating rounds, North Korea proposed establishing panels to deal with other outstanding issues, including Pyongyang’s missile development program and the whereabouts of ten Japanese allegedly kidnapped by North Korean agents. Japan, seeking to avoid decoupling the compensation/apology issue from the kidnaping and missile disputes, rejected the North Korean proposal.

August 2000 Talks. On July 26, 2000, the Japanese and North Korean Foreign Minister staged an unprecedented meeting at the ASEAN Regional Forum meeting in Bangkok. The two officials agreed to hold another round of talks in Tokyo in August. They also agreed to resume discussions over further visitations to Japan by women who married Korean husbands and emigrated to North Korea. At the August 21-24, 2000 bilateral meetings in Japan for the first time formally raised the possibility of providing an economic assistance package – *i.e.* not a compensation payment – to North Korea.

⁶ For more on how the North Korea threat has caused many Japanese policymakers to rethink Japan’s defense posture, see Richard Cronin, *Japan’s Changing Security Outlook*, CRS Report RL30256, July 9, 1999. See also Rinn-Sup Shinn, *North Korea: A Chronology of Provocations, 1950-2000*, March 15, 2000.

⁷ According to a 2000 poll, only 36% of Japanese surveyed believed Japan should resume food aid to North Korea, compared with 51% in August 1997. *Mainichi Shimbun*, February 27, 2000.

⁸ On March 7, 2000, Japan announced its intention to deliver 100,000 tons of rice to North Korea, its first shipment since the food aid program was suspended following Pyongyang’s launch of a two-stage Taepodong missile over Japan in August 1998. In October 2000, Japan announced it would send an additional 500,000 tons of rice aid to North Korea.

Reportedly, no figures were discussed, and North Korea did not respond to the offer. The two sides agreed to hold another round of talks in a third country in October, with a goal of establishing diplomatic ties by the end of 2000. The negotiators also agreed to expand bilateral contacts to include politicians and business enterprises, and to set up committees to handle two of North Korea's demands: the return of cultural treasures taken from Korea during the Japanese occupation, and improving the legal status of Koreans living in Japan. Reportedly, North Korea asked Japan to resume trade insurance and full-scale economic aid, but Japanese negotiators declined.

October 2000 Talks. Almost no progress was achieved during the October 30-November 1, 2000 bilateral meetings in Beijing. Reportedly, North Korea flatly rejected Japan's proposal to offer economic assistance in lieu of compensation. Japan again turned down North Korea's demand that the abduction issue be discussed outside the normalization talks.

2002 Talks. Several official and unofficial bilateral meetings were held in 2002, most notably talks between the two nations' Foreign Ministers in July and between Red Cross societies in April and August. At the August Red Cross meeting, North Korea agreed to broaden its investigation into the "missing Japanese" that Tokyo alleges were abducted. Pyongyang also took the unprecedented step of allowing Japanese officials to discuss the issue with an official with North Korea's Public Security Ministry. Additionally, in July 2002, the four remaining Japanese Red Army terrorists living in North Korea announced their desire to return to Japan. The Japanese government has called for their return to face charges of hijacking a plane to North Korea in 1970. The U.S. State Department has cited North Korea's harboring of Japanese Red Army terrorists as a reason for North Korea's inclusion on the U.S. terrorism list.

Japan's 1965 Economic Aid Package to South Korea

On June 22, 1965, Japan and South Korea signed a Treaty of Basic Relations, normalizing relations between the two countries for the first time since Japan annexed the Korean peninsula in 1910. As part of the final settlement, Japan agreed to provide South Korea with a total sum of \$800 million, which consisted of: a) an outright grant of \$300 million, to be distributed over a 10-year period; b) a \$200 million loan to be distributed over a 10-year period and repaid over 20 years at 3.5% interest; c) \$300 million in private credits over 10 years from Japanese banks and financial institutions. The disbursements were made in dollars.

Estimating the Present Value of the 1965 Settlement

There are a wide range of estimates for the present value of the 1965 Japan-South Korea settlement. At the low end is a method that adjusts for inflation in the U.S. economy, yielding a value of approximately \$3.4 billion in 1999 dollars.⁹ At the high end

⁹ This method uses the U.S. gross domestic product (GDP) deflator to adjust for inflation between 1965 and 1999. The GDP deflator is the ratio of nominal GDP in a given year to real GDP in that same year. In 1999 the GDP deflator was 104.37 (1996 = 100), 4.35 times the 1965 deflator of 23.98. Thus, \$800 million in 1965 dollars would be worth approximately \$3.4 billion

(continued...)

is a calculation that produces a value of \$20 billion in today's dollars by adjusting for inflation in the Japanese economy, appreciation of the yen, accrued interest, and differences in population in North and South Korea.¹⁰ One methodology that adjusts for Japanese inflation since 1965 and for inter-Korean population differences yields a present value of ¥418 billion (\$3.8 billion using an exchange rate of ¥110 = \$1). If the same disbursement formula used in 1965 were applied today, the ¥418 billion would break out as ¥157 billion (\$1.42 billion) in outright grants, ¥104 billion (\$950 million) in concessionary government loans, and ¥157 billion (\$1.42 billion) in private credits.¹¹

The above figures should be interpreted as rough approximations. Computing the present value of a past sum is an inherently inexact task. When more than one country is involved, the calculation is made even less precise by long-term changes and short-term fluctuations in exchange rates. Additionally, an exact calculation would take into account differences between North Korea and South Korea, including the extent of the claims for damage by the Japanese occupation. Finally, the 1965 settlement occurred before the revelation that Japan had forcibly used tens of thousands of Korean "comfort women" to provide sexual services to Japanese soldiers during World War II. In the past, North Korea has insisted that Japan's compensation take into account the comfort women's plight, a demand that (if it is met) presumably would raise the value of the settlement package.

⁹ (...continued)
in 1999 dollars.

¹⁰ Noland, "The Economics of Korean Unification," *Foresight Magazine*, February 2000. For his accrued interest adjustment, Noland assumes an annual rate of return of 5%. According to the U.S. Census Bureau, in 1965, North Korea's population was approximately 11.9 million, approximately 40% the size of South Korea's population of 28.7 million in the same year. In 1999, North Korea's population was estimated to be 21.4 million, around 45% the South Korean total of 47 million.

¹¹ This method uses the Japanese GDP deflator to adjust for inflation between 1965 and 1999. In 1999 the Japanese GDP deflator was approximately 3.5 times the size of the deflator in 1965. Using this figure, the 1965 compensation package of ¥288 billion would be worth roughly ¥1.01 trillion today (\$9.2 billion, at ¥110 = \$1). To adjust for population differences, multiply ¥1.01 trillion by 0.41, which is the ratio of North Korea's 1965 population (11.9 million) to South Korea's 1965 population (28.7 million). The result is ¥418 billion (\$3.8 billion).