

*Prime Minister
Singapore*

11 April 2002

YAB Dato' Seri Dr Mahathir bin Mohamad
Prime Minister
Malaysia

Dear *Mahathir*,

I refer to your letter of 4 March 2002 to Senior Minister Lee Kuan Yew, and his reply of 11 March.

Before Kuan Yew visited KL in August 2000, he suggested that he discuss the outline of an agreement with Daim, which both of us could later consider and endorse. He hence addressed his letters to Daim. However, since you wrote to him, he corresponded and negotiated with you with my approval.

I have now decided to handle directly our discussion on the bilateral package.

I have taken some time to mull over my reply to you, because I wanted to find the best way forward from here to secure for the long-term, a stable, win-win relationship for our two countries.

I have discussed with my Cabinet colleagues the proposals contained in your letter, and have the following comments.

1. Bridge

Between a new bridge to replace the entire Causeway, and one to replace just the Malaysian side of the Causeway, I like the former better.

Once the new bridge is completed, the Causeway can be knocked down, which I prefer to be done after 2007.

But if you wish to proceed immediately to replace just your side of the Causeway with a bridge, I shall accept it, though I think this is not ideal.

2. Railway

I note that you have decided to relocate your CIQ to Johor Baru.

You also indicated that you would continue to operate the train service to Tanjong Pagar.

Under the 1990 Points of Agreement (POA), Malaysia had agreed to move the KTM railway station from Tanjong Pagar to Bukit Timah.

I recall, however, that you had proposed at our meeting in Hanoi in 1998, to relocate your railway station to Kranji. I agreed to this proposal in my meeting with Abdullah Badawi when he visited Singapore in February last year. I confirm here that Singapore is prepared to accommodate such a variation to the POA within the bilateral package.

You had later also proposed a railway tunnel from Johor to Singapore. But I read from your letter that you have now decided on a railway swing bridge because of the high cost of constructing the tunnel. I can go along with this proposal.

Since you intend to operate an electric train in the future, I suggest you revisit your Kranji station proposal. You could run your train in an underground tunnel from the Singapore end of your railway swing bridge to the KTM station in Kranji. This will take care of the problem of unsightly overhead catenaries. If you are concerned about the cost of constructing this tunnel, Singapore can help defray a portion of it.

3. Water

I do not want our bilateral relations to be always strained by the issue of water. I am saddened by the constant emotional rhetoric in the media over Malaysia's supply of water to Singapore.

For the sake of good long-term relations, my colleagues and I have decided that Singapore will produce as much water by ourselves as we can, to supplement the existing Water Agreements.

We have just called a tender for a 30mgd desalination plant, which will be ready by 2005.

We have also been operating a 2.2mgd plant to produce NEWater (reclaimed water) using membrane technology for two years now. It has proven to be successful and economical. We have therefore decided to ramp up our programme to produce NEWater, to replace the supply of water under the 1961 Water Agreement when it expires in 2011.

But we will be happy to still buy from Johor a modest quantity of treated water, say, 10mgd or 20mgd, from 2011, after the expiry of the 1961 Water Agreement, to 2061, if Johor remains keen to sell.

As for water after 2061 when the 1962 Water Agreement expires, I accept your offer of 100mgd of raw water and 150mgd of treated water.

However, your proposal for a new water agreement to run for 100 years from 1 January 2002, means, in effect, a water agreement of only 40 years, since the 1962 Water Agreement will expire only in 2061. Our discussions have always been on the basis of an agreement for 100 years from 2061.

On pricing, in your letter of 21 February 2001 to Kuan Yew, you had proposed that raw water be priced at 60 sen, which Johor considered a fair price. Singapore offered a revision from 3 sen to 45 sen for raw water under existing agreements, and accepted your proposal of 60 sen for raw water under a new agreement. I note that you have not accepted this counter-offer from us. May I explain that this counter-offer took into account our concessions in the other parts of the package, for example, the additional 12 parcels of Malayan Railway land.

You have now proposed another pricing arrangement where, among other things, a new formula for the price of raw water after 2061 is to be negotiated in 2058, and the formula for the price of treated water is to be renegotiated every 20 years, taking into account the circumstances then. Having reflected further on this matter of pricing, I agree that it would be difficult for us to fix now, the price of water to be supplied many decades in the future.

However, we need a definite basis for all future price revisions throughout the period of the agreement. Otherwise, there will be no certainty in the agreement, and it will be difficult for our negotiators to agree on the price revision when the time comes. We will periodically be locked in dispute over water, in spite of a new agreement.

I propose therefore a pricing mechanism that can stand the test of time. I propose that we peg the price of treated water from Johor (water after 2061, as well as the modest quantity from 2011-2061 mentioned earlier in the letter) to an agreed percentage of Singapore's cost of alternative sources of water ("peg-price"). This is similar to the way we price natural gas that Singapore purchases from Malaysia, where the price of gas goes up or down with the price of alternative fuel, i.e. oil.

The price of raw water after 2061 can be calculated by deducting Singapore's cost of treating the raw water (including abstracting the water from the river and delivering it to Singapore etc) from the agreed peg-price.

To work such a pricing mechanism, Singapore will disclose independently-audited accounts of its cost of alternative sources of water. This cost will, of course, vary with the price of fuel oil, technology etc. For example, when the price of fuel oil goes up, the peg-price will go up too.

Our Foreign Ministers and officials can discuss both your pricing formula and my counter-proposal when they meet.

4. CPF and Airspace

They should be able to make progress on these two issues as part of the package.

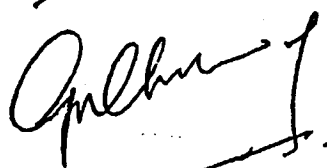
Basis for Further Discussion

Your letter of 4 March and my reply here can form the basis for further discussion between our Foreign Ministers and officials. They can proceed to set the dates of their meeting.

Should they run into roadblocks, I would be happy to meet you to help remove the blocks.

I hope we can now make progress in wrapping up this package of bilateral issues.

Yours *Sincerely,*



GOH CHOK TONG