Trust Funds in the Pacific

THEIR ROLE AND FUTURE

Benjamin Graham

Asian Development Bank

Pacific Studies Series

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Note: US$ refers to United States dollars, and A$ refers to Australian dollars.

Acronyms and Abbreviations

ADB	Asian Development Bank
BNTF	Basic Needs Trust Fund
CIF	Consolidated Investment Fund
COFA	Compact of Free Association
FSM	Federated States of Micronesia
FTF	Falekaupule Trust Fund
GDP	gross domestic product
GNI	gross national income
IADB	Inter-American Development Bank
MIITF	Marshall Islands Intergenerational Trust Fund
NPRT	Nauru Phosphate Royalties Trust
PDMC	Pacific developing member country (of ADB)
PNG	Papua New Guinea
RERF	Revenue Equalization Reserve Fund
RMI	Republic of the Marshall Islands
TTF	Tuvalu Trust Fund
UNDP	United Nations Development Programme
US	United States
USAID	United States Agency for International Development
WB	World Bank

Foreword

This is an important juncture for the Pacific. The development performance of the Asian Development Bank's (ADB) Pacific developing member countries over the past two decades has been mixed. All face significant challenges in generating broad-based and sustained economic growth from small, high-cost, and narrowly focused economies. They continue to struggle for even modest levels of economic growth despite significant amounts of foreign assistance. As these countries and their major development partners renew their commitments to more effective development outcomes, new approaches and ideas are needed.

Public trust funds hold some potential for serving as effective development mechanisms. While a few such funds are already in use in the Pacific, they are still relatively new to the development arena. The primary objective of this book is to provide an introduction to trust funds, how they function, how they differ from other financial modalities, what their comparative advantages and disadvantages may be, how they are structured, and how they have fared so far in the Pacific. Looking forward, as Pacific governments and development partners strive to improve development effectiveness, this analysis can help to identify and prioritize resource gaps and to determine whether and where trust funds may be appropriate.

Benjamin Graham, a graduate student at the McDonough School of Business of Georgetown University in Washington, DC, USA prepared this report during a 7-week summer internship at ADB supervised by Steve Pollard, Principal Economist, Pacific Department.

I commend this analysis to all who have an interest in the future of the finances, economies, and people of the Pacific.

Robert Y. Siy
Officer-in-Charge
Pacific Department

Executive Summary

The Asian Development Bank's (ADB) Pacific developing member countries continue to struggle for even modest levels of economic growth despite significant amounts of foreign assistance. As these countries and their major development partners renew their commitments to more effective development outcomes, new approaches and ideas are needed.

Public trust funds hold some potential for serving as effective development mechanisms. While a few such funds are already in use in the Pacific, they are still relatively new to the development arena. Donors and development institutions are finding that where sound policy and governance structures are in place, trust funds can be an effective way to accumulate, preserve, grow, and mobilize capital for development. This analysis aims to provide a better understanding of what trust funds are, how they are structured, and how they have fared so far in the Pacific.

Trusts are legal arrangements whereby one party gives control of financial assets to a second party to be administered on behalf of a third party. There are three primary types: true trust funds, revolving funds, and sinking funds. Development institutions most often use sinking or revolving funds. Public trust funds are established for public purposes by, with, or through governments.

Case analyses of existing trust funds in the Pacific reveal that those with proper governance and management structures not only provide sustainable financial resources for development but also fill resource gaps and gradually reduce reliance on direct foreign assistance transfers. On the other hand, several funds have not fared very well due to lack of transparency and to mismanagement. A set of good practices for trust fund establishment and management is developed based on these case studies.

Looking forward, as ADB strives to improve development effectiveness in the Pacific, it can help to identify and to prioritize resource gaps and to determine whether and where trust funds may be appropriate. ADB should also continue its efforts to help Pacific nations improve their overall fiscal systems to ensure that where trust funds are deemed appropriate, a sound management structure will be in place to support them.

Introduction

A government which must regularly go cap-in-hand to donors cannot hope to achieve financial self-reliance or plan effectively for the long term future of its people.

Tuvalu Trust Fund proposal

WHY TRUST FUNDS AND WHY NOW?

Development in the Pacific remains a great challenge. Despite receiving decades and billions of dollars worth of development assistance, including Asian Development Bank (ADB) disbursements worth well over US$1 billion,[1] the 14 Pacific developing member countries (PDMCs) still struggle to reach even modest levels of growth. Though their development performances vary and a few have demonstrated fair progress, altogether the results are not impressive.

This long-standing situation, the so-called Pacific Paradox, has led some of the region's more prominent development partners to begin seriously questioning the very feasibility of achieving financial and economic self-reliance. Nevertheless, as the PDMCs and their development partners renew their commitments to improved aid effectiveness and to combating poverty, new approaches need to be identified and deployed. One promising mechanism that has slowly penetrated the development scene is trust funds.

Trust funds are already in use in the Pacific, and the region has seen its share of successes and failures. What is new is their increasing popularity among both the PDMCs and their development partners. In fact, within the last 3 years, the Federated States of Micronesia (FSM) and the Republic of the Marshall Islands (RMI) have both established funds, and Niue, although

[1] Cumulative ADB loan disbursements alone (excluding grants) to the PDMCs totaled US$1.12 billion as of year-end 2003.

not a PDMC, established a national trust fund in mid-2004. More funds are in the pipeline. Nevertheless, some degree of uncertainty remains both within the region and among donors over exactly how trust funds function, how they differ from other financial modalities, and what their comparative advantages and disadvantages may be vis-à-vis traditional forms of development assistance. The primary objective of this analysis is to provide a basic introduction to trust funds and to address these and related issues.

SOME GUIDING QUESTIONS

Seven questions guide this analysis.

1. What exactly are trust funds, how do they work, and how do they differ from other financial mechanisms?
2. What are some of their advantages and disadvantages in the area of economic development?
3. How do trust funds fit into the general macroeconomic situation of the PDMCs?
4. What funds are already in use in the Pacific and what lessons can we learn from them?
5. How are trust funds used by development institutions like ADB and the World Bank?
6. What are some possible good practices for trust fund establishment and management that ADB and PDMCs can draw on?
7. What role can or should ADB play with respect to trust funds in the Pacific?

FOR WHOM?

This analysis intends to give input to decision and policy making at the Asian Development Bank. ADB occupies a special role in the Pacific as the region's premier development institution and as a purveyor of not only financial but also technical and intellectual capital. As it currently reexamines its past efforts and charts a new course for its operations in its *Pacific Strategy 2005–2009*, it is an opportune time to further explore relatively new development tools like trust funds.

This analysis also aims to serve as a general guidebook for those in the Pacific and elsewhere who may not be familiar with trust funds and how they fit into the overall landscape of foreign assistance, public finance, and economic development.

SCOPE AND METHODOLOGY

A thorough analysis of trust funds in the Pacific must address a number of critical areas. Seeing the bigger picture requires discussing major topics like economic development and smaller topics like fund governance and management. This analysis aims to cover at least the principle bases though given its limited timeframe and focus, technical issues like cost-benefit and economic impact analysis, more detailed case analyses, and trust investment management issues are not covered.

This analysis was conducted over the course of roughly 7 weeks at ADB headquarters in Manila (see Appendix 9 for the original terms of reference). Data and information were gathered through consultations and interviews with ADB staff in and outside the Pacific Department, with Pacific island experts, with independent consultants, and through general desk research.

1 Understanding Trusts

THE BASICS

A **trust** is a legal arrangement wherein one party, the **trustor** gives control of assets to another party, the **trustee**, to be administered on behalf of a third party, the **beneficiary**. Trustors, trustees, and beneficiaries can be individuals, groups of individuals, institutions, or governments. A **trust fund**, therefore, is a fund with financial assets that are managed under a legal trust arrangement.

Private trust funds originated in common law countries as a way of preserving capital while making the income from that capital available to designated persons or purposes. Private trusts are normally established with legal terms set out under a **trust deed**.

Public trust funds are those established for public purposes by, with, or through governments by some form of **enacting legislation** (local, national, or international) that forms the trust, sets out its legal terms, and assigns respective rights and responsibilities to different parties.

> Think of a trust as an empty shell. You fill it with your assets and create rules that designate how and when the shell is opened and its contents distributed...
> ING Group (www.ing-usa.com)

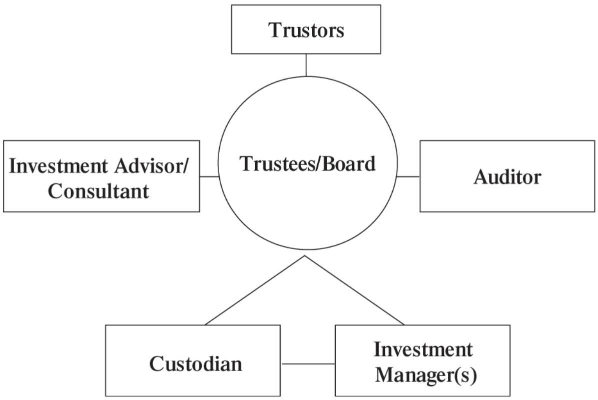
THE KEY PLAYERS, SERVICE PROVIDERS, AND MANAGEMENT STRUCTURE

Trustors (grantors, donors, or settlors) create the trust, determine its legal terms, and usually provide the initial capital for the trust fund. **Trustees** have legal responsibility for management and oversight of trust assets and carry out the terms of the trust in the best interest of the beneficiaries. Trustees also usually select, hire, and monitor the various **service providers** who help manage the fund's resources. **Beneficiaries** are entitled (as stipulated in the terms of the trust) to income or principle from the trust either currently or at some time in the future.

Service providers help manage, monitor, and administer trust funds and are usually contracted by and report directly to the trustees. **Investment**

advisors (also called monitors or consultants) give financial management advice to the trustees and help select and monitor the custodian, investment manager, and any other financial service provider. **Fund custodians** (sometimes also called trustees) hold and safeguard fund assets and act as intermediaries between the trustees and the investment managers. **Investment managers** (also called money or asset managers) implement the investment of funds in capital or other markets (through brokers and other intermediaries) as stipulated by the trustees and the trust fund's general investment policy. **Auditors** conduct regular (usually annual) audits and examinations of the trust fund's financial management, reporting, and internal controls. Figure 1.1 illustrates the generic management structure of a trust fund.

Figure 1.1
Generic Management Structure of Trust Fund



TRUE TRUST FUNDS, SINKING FUNDS, AND REVOLVING FUNDS

Different types of trust funds and related financial mechanisms exist, and there is often confusion over their true definitions. For the purposes of this analysis, only three general types will be defined and discussed. These are **true trust funds** (also known as **endowments**), **sinking funds,** and **revolving funds**.

A **true trust fund** has the following characteristics:

- the principal capital (including the initial capital and subsequent contributions) is to be preserved, kept in perpetuity, and not consumed under any circumstances other than dissolution;
- the principal capital (or at least part thereof) is invested in capital or other markets in order to earn investment income;[2]
- the real (inflation-adjusted) value of the principal capital is maintained;
- investment income (or part thereof) minus investment costs can be consumed or re-invested.

Endowments are structurally identical to true trust funds so the terms can be used interchangeably. They are typically used by universities, museums, hospitals, or foundations.

With **sinking funds,** both investment income (if the fund is invested) and the principle capital are consumed over a fixed period. Sinking fund time frames are limited, and the capital is drawn down or "sinks" over a predetermined period until dissolution.

Revolving funds are those in which both the investment income (if the fund is invested) and principle capital are consumed but for which there exists a replenishment source (a tax, guarantor, donor, or other source) that contributes regularly to the fund. Replenishment usually occurs annually. Most revolving funds have limited or conditional terms and are not held in perpetuity (conditionality entails dissolution of the fund when certain conditions are satisfied or when predetermined goals are achieved).

The term "trust" is often attached to all these funds because of the fiduciary responsibilities that are transferred upon (entrusted to) trustees. Therefore, it is possible to have a **sinking trust fund** or a **revolving trust fund**. The term "foundation" is often used interchangeably with trust funds or endowments, but foundations are organizations (usually nongovernment or quasi-public) that are established to promote educational, cultural, environmental, charitable, or similar social causes and which may possess and administer a trust fund to finance activities.

The vast majority of funds that have been established for development purposes (e.g., funds at ADB, the World Bank, and related institutions) fall into the sinking or revolving categories. Unless otherwise stated, any reference to "trust fund" will be general (true, sinking, or revolving) and will entail public trust funds. Moreover, while all three types of funds will be discussed in this analysis, the primary focus will be on true trust funds.

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[2] The term "investment income" includes investment earnings (dividends and interest) as well as capital and valuation gains.

COMPARATIVE ADVANTAGES AND DISADVANTAGES

Relative to each other, the major advantages and disadvantages of the three general fund types are summarized as follows.

Figure 1.2
True vs. Sinking vs. Revolving Funds

Fund Type	*Comparative Advantage*	*Comparative Disadvantage*
True Trust Fund	• Most sustainable • Long-term planning • Less costly to donors • Can earn investment income	• More capital upfront • More sophisticated set up • Higher recipient costs • Can incur investment losses
Revolving Fund	• Flexible • Quicker setup, dissolution • More closely matches resources to needs	• Less sustainable • More frequent consultation • Disruption of resource flows
Sinking Fund	• Short-term initiatives • Usually less capital • Targeting	• All capital upfront • Least sustainable • Not as flexible

MULTIPLE FEATURES

Trust funds can have many features; it is important to be aware of them and their possible combinations. Figure 1.3 provides a limited illustration of some of those.

Impetus for Establishment. Trust funds are established for a variety of reasons that are usually on the supply side, i.e., when there is an excess supply of resources, when there is a current or expected shortfall in resources, or for both reasons. For example, some Pacific trust funds were established during boom periods or when there were windfall resources such as the Nauru Phosphate Royalties Trust (phosphate mining revenue) or the Tonga Trust Fund (passport sales). Some trust funds, on the other hand, are established primarily because of critical and long-term resource shortages such as the Tuvalu Trust Fund that was formed to offset oncoming budget gaps. Others,

Figure 1.3
Multiple Features of Trust Funds

Impetus For Establishment	**Life-cycle/ time frame**	**Capital Source**	**Terms of Capital**	**Capitalization Process**	**Trustee Composition**	**Investment Objective**
Windfall revenue, excess resources, etc.	Perpetual	Bilateral	Grant	Build-up Period	Single Entity	Capital Accumulation
Budget gap, chronic resource shortage, etc.	Limited-term	Multilateral	Loan	Front-loaded	Multi-party	Current Income
Mixed	Conditional	Internal (resource base, taxes, etc.)	Mixed	Mixed		Balanced Strategy
		Mixed				

like the Marshall Islands Compact Trust Fund, are formed when there is both a current windfall of resources and a foreseeable shortage. (For more details, see Section 5.)

Trust Fund Life Cycles. Trust funds can be perpetual (in the case of true trust funds), limited, or conditional.

Capital Sources, Terms, and Process. Trust funds receive initial capital from bilateral, multilateral, or domestic sources or from a combination of these. Capital can take the form of grants, loans, or both. Trust funds can be funded with a one-off, front-loaded payment; through a build-up period; or again by a combination of both.

Trustee Composition. Trustees can represent single entities (like the host government) or multiple entities.

General versus Specific Use. A popular way to categorize trust funds relates to their use. In the Pacific, there are general-use funds for fiscal and budgetary support or for general economic development, and there are specific-use funds that have narrower purposes like outer island development or nuclear compensation. Naturally, there is a rough positive correlation between the scope and size of funds (with some exceptions). See Figure 1.4 for an illustration of size and scope.

Figure 1.4
Simplified Relative Size and Scope

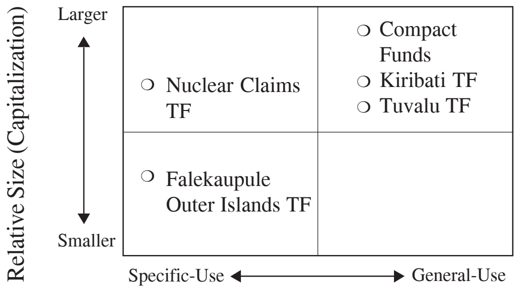
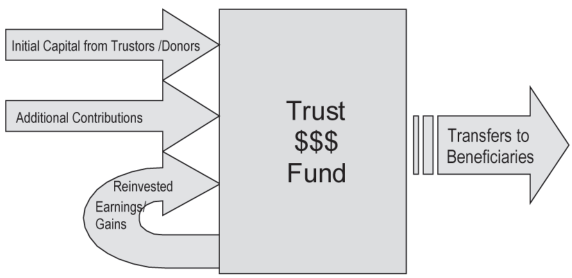


Figure 1.5
Generic Resource Flows of True Trust Funds

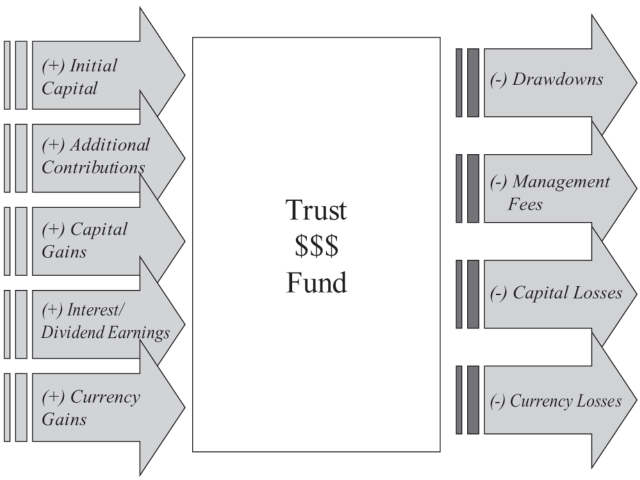


RESOURCE FLOWS

A trust fund is established with initial capital and subsequent contributions. As mentioned previously, in true trust funds, investment income (or part thereof) is re-invested in order to maintain the real value of the principal capital whenever possible. Funds are then drawn down according to the distribution policy and transferred to beneficiaries. Figure 1.5 illustrates the simplified flow of resources into and out of a generic true trust fund.

Figure 1.6 illustrates the debits and credits on the trust fund asset. The overall value of the invested trust fund is a function of capital contributions, gains, and earnings (on the positive side) and drawdowns, fees, and losses (on the negative side).

Figure 1.6
Positive and Negative Factors that Affect Fund Value



2 Trust Funds, Public Finance, and Development

The art of prophecy is very difficult—especially with respect to the future.
Mark Twain

TRUST FUNDS AND PUBLIC FINANCE

Sound public financial management is a complex and challenging process; even the most advanced nations often demonstrate erratic fiscal performances. Constructing *pro forma* budgets can be a painstaking process, and studies of the accuracy of past forecasts made by some of the brightest budget analysts often show disappointing results (Heller 2003). Such challenges are even more acute in the Pacific. While public financial management has been a focus for a number of years as part of the overall public sector reforms that have taken place, and whereas donors like ADB have offered millions of dollars worth of technical assistance, training, and system upgrades, the corresponding outputs and outcomes remain weak.

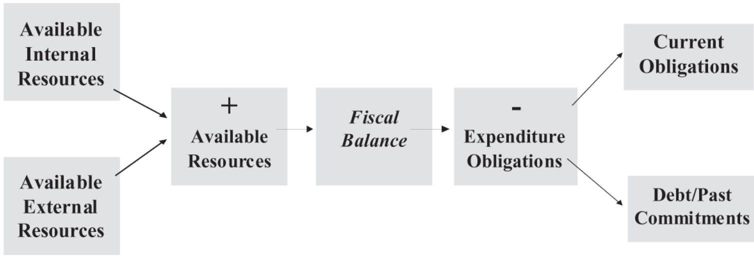
Some constraints to better fiscal management in the region are deeply rooted. For instance, economic volatility often creates a "bull-whip" effect on fiscal management making forecasting of both revenues and expenditures a highly uncertain exercise. (See Section 4.) While efforts to improve PDMC fiscal systems continue, it is worthwhile exploring how trust funds fit on a theoretical level into the overall public finance picture.

As part of the overarching principle of fiscal management (see text box), fiscal systems should help manage and mitigate macroeconomic instability and should distribute resources in an equitable and efficient manner. Moreover, today fiscal systems are increasingly called upon to help alleviate poverty. What role can trust funds play in this context? Well-managed funds are proving

> The primary operating principle of public financial management is to ensure that the discounted present value of all future government spending on goods and services does not exceed the discounted value of future government revenue, less the current stock of net government debt to the public.
> Jeffrey Sachs (Heller 2003).

to be useful tools in hedging against some of the uncertainties and risks inherent in the management of public finances. This can be illustrated through a simple analysis of the public finance revenue and expenditure balance. Public financial resources flow into and out of the management system as illustrated in figure 2.1.

Figure 2.1
Public Finance Resource Flows



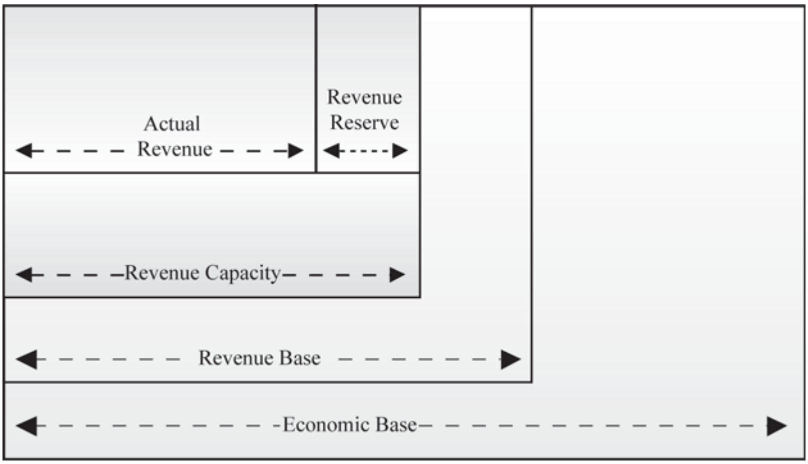
(Source: modified from Berne, 1986)

On the resource or revenue side, public financial systems rely on available internal and external resources to fund public activities. In all of the PDMCs, available internal resources are limited by the size and efficiency of their economic and revenue bases as well as by their revenue capacity. This is explained more easily in Figure 2.2.

All nations possess given and created attributes that make up their economic bases. This **economic base** forms the foundation from which public resources and revenue can be drawn. The extent to which governments can tap into the economic base makes up the **revenue base**. **Revenue capacity** is the maximum extent to which governments can collect resources through tax and non-tax means from the revenue base, and **actual revenue** is the current level collected within revenue capacity. What remains uncollected is the **revenue reserve**. The economic base, revenue base, revenue capacity, and actual revenue grow and shrink over time depending on a multitude of variables.

In the Pacific, exogenous factors such as smallness and remoteness have long been identified as key constraints to expansion of the economic base that in turn affect the downstream revenue base, revenue capacity, and actual revenue. Meanwhile, endogenous factors like institutional weaknesses (such as inefficient tax collection) are seen as common constraints to growing revenue capacity and actual revenue.

Figure 2.2
Economic Base and Revenue Implications



While the debate continues over the extent to which these and other factors have led to poor fiscal and economic performance, there is converging acknowledgement among both PDMCs and their development partners that, at least for a handful of island nations, there exist real limitations to growing the economic base. This has fueled the emphasis on enhancing revenue capacities in the PDMCs (endogenous factors) and the acceptance of utilizing trust funds as supplements to small and low-growth-potential economic bases.

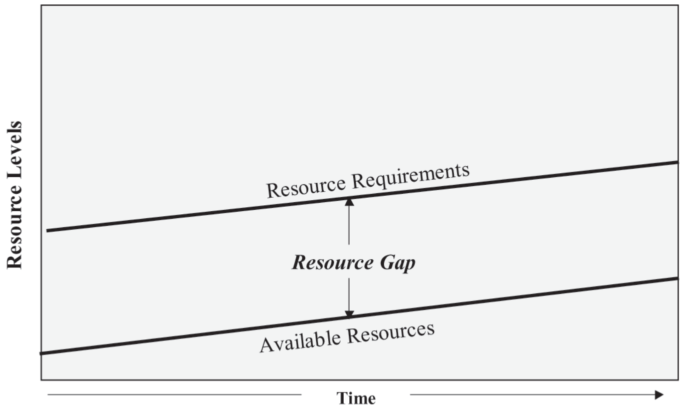
On the expenditure side, resources flow to either current obligations (recurrent or capital) or to past commitments (debt, overdue appropriations, etc.). In the Pacific, effective management of expenditure varies; some countries (like Samoa) show far better progress than others. Most PDMCs are committed to improving transparency and accountability of public expenditure, and some are currently attempting to move towards more integrated, medium-term, performance-based frameworks.

In general, however, expenditure management including key issues like forecasting, control, reporting, auditing, and expenditure-outcome linkages remains seriously weak. Furthermore, and perhaps most significantly, expenditure levels have continued to rise over time.

TRUST FUNDS AND DEVELOPMENT

Small and slow-growing economic bases, weak revenue capacities, and steadily rising expenditure levels have all contributed to increasing fiscal stress and to widening resource gaps in the Pacific. As illustrated in Figure 2.3, these gaps exist whenever resource requirements exceed available supply. The options for eliminating resource gaps are reducing requirements, increasing available supplies, or filling the gap with an alternate source (or a combination of these). All these options have been attempted with varying success throughout the region. Foreign assistance has been the primary gap filler to date, but for two PDMCs, namely Kiribati and Tuvalu, trust fund contributions are slowly gaining importance (see Box 1). Furthermore, in several other PDMCs, trust funds are being built up in anticipation of eventually supplanting foreign assistance.

Figure 2.3
The Resource Gap



(Source: Corbin)

While trust funds have been used for many years in family and institutional endowments and for charitable purposes, they have only recently crossed over into the economic development arena, primarily in the environmental sector. Major development institutions are increasingly using trust funds to carry out their work although until now most have been limited-term and either sinking or revolving. (See Section 6 for more details on trust fund use at ADB, the World Bank, and other institutions.)

Box 1
Applying Portfolio Theory and Asset Management to Public Finance

Increasingly, public finance managers are adopting principles of private and corporate finance, such as the practice of presenting public assets and liabilities via government balance sheets. Another useful (albeit limited) analogy is the use of private asset management principles in public asset management.

Portfolio theory, in simple terms, explores how an investor can identify his or her tolerance for market risk and then builds a portfolio of different investment holdings that maximizes the expected rate of return given that level of risk (i.e., diversification). Like individual investors, corporations must also decide on how much and where to allocate resources in order to maximize returns. Indeed, every investment, whether private or public, carries different size, timing, and risk characteristics that must be taken into consideration.

A government, like a private investor, can also determine its risk thresholds and can set out to find the optimal portfolio that maximizes returns given its risk criteria. A government allocates assets to a wide variety of areas: recurrent obligations, payment of debt and liability, social transfers, subsidies, and so on. In deciding on how and where to allocate resources, governments should consider the size, timing, and risk (return) of each respective investment. The challenge facing public financial managers, therefore, lies in determining exactly what constitutes an optimal, diversified portfolio.

How do trust funds fit into this analogy? Trust funds are alternative public investments that hold, relative to most other public investments, fairly clear and measurable size, timing, and risk characteristics. Investing in a diversified and professionally managed trust fund (with the optimal mix of equity, fixed income, and other holdings) can, in and of itself, constitute a step towards diversification of the public asset portfolio.

The experiences of the Kiribati and Tuvalu trust funds clearly show that governments can hedge against uncertainty and can demonstrably improve the overall performance of their portfolios (by lowering volatility and increasing returns) through direct investment in capital markets via trust funds.

Development thinking has evolved significantly over the past half century, and it has become evident that the dominant paradigm of this period—that shortage of capital was the main constraint to economic growth—has not been helpful. The new consensus holds that whereas capital remains a crucial factor in development, appropriate policies and sound institutions must first be in place in order for capital (both private and public) to be attracted and effectively utilized (Duncan and Pollard 2002). While capital accumulation no longer plays a central role in development theory, resources (including financial) remain a critical factor in the development equation.

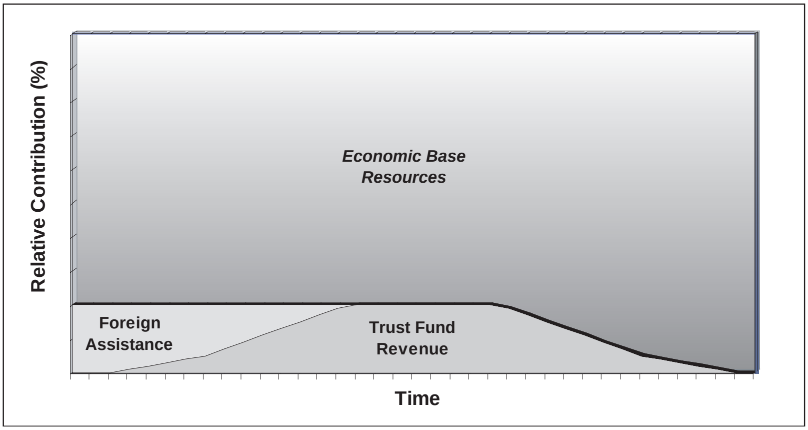
Trust funds, simply put, are a mechanism for pooling, growing, and spreading out financial resources over time. They represent a basic redirection of capital and a foregoing of current spending in favor of future spending. They can, therefore, help to ensure more stable and sustainable resource flows for development. The security and sustainability of development resources are critical elements in the new development thinking and are especially relevant in small, volatile, and vulnerable economies like those of the PDMCs. This security and sustainability can foster more effective, longer-term planning, a key weakness in the Pacific.

> Trust funds should be viewed as short- to medium-term instruments that help the economy to buy time whilst a strong domestic economy that utilizes domestic factors and resources is created.
> Duncan et al, 1993

Donors and development institutions are finding that where sound policy and governance structures are in place, trust funds can be an effective way to accumulate, preserve, grow, and mobilize capital for development (see Box 2). Trust funds do not, however, spur economic growth. At best they can provide a steady base for some development initiatives while real, sustainable growth continues. This train of thought underpins what has emerged as something of an "ideal life cycle" principle of trust funds in the context of development (Duncan, et al. 1993).

As illustrated in Figure 2.4, under this ideal life cycle, once a trust fund is established and growing, its contribution to overall available resources steadily increases while the contribution from foreign assistance steadily decreases. Eventually, trust fund contributions totally replace foreign assistance. As the economy develops and grows over time, so too will its ability to draw on resources from its own economic base. This will continue until eventually there will no longer be a need for the trust fund.

Figure 2.4
Ideal Life Cycle of Trust Fund



This ideal scenario is perhaps a response to what could be considered a philosophical case against the use of trust funds in development. The argument holds that trust funds do not liberate developing nations from their dependence on outside resources but instead merely shift their dependence from one external source to another. Trust funds, the argument continues, may actually discourage small nations from seeking true, self-derived economic growth and development. The analysis of the Pacific's two oldest national trust funds in Section 5 will shed more light on this debate.

Box 2
Domestic Savings and the Endowment Effect: Some Behavioral Economics

Can trust funds catalyze domestic savings and do PDMCs manage trust fund resources better than they do direct aid transfers? Trust funds present interesting behavioral economics questions that deserve attention.

Trust Funds and Domestic Savings. By their very nature, trust funds favor savings over consumption; resources (domestic or donor aid) that would otherwise be spent are directed into a separate fund to be preserved and spent more judiciously and over a longer period. Does a trust fund encourage PDMC leaders to adopt more fiscally conservative mindsets? While fiscal discipline has long been identified as a major challenge among the PDMCs, a handful of cases (namely in Kiribati, Tuvalu, and to a limited extent, the Marshall Islands) suggests that the existence of trust funds has, indeed, helped encourage more prudent and forward-looking fiscal behavior.

The Endowment Effect. Trust funds may encourage savings, but are donor resources used in this way more effectively managed and utilized than are regularly transferred resources? In other words, are trust fund resources better managed than direct aid transfers? The "endowment effect," one of the chief principles of prospect theory and a popular issue among behavioral economists, holds that people place an extra value on things they own (Economist.com 2003). Over the past decade, prospect theorists have found support for the endowment effect based on empirical research. If this theory holds true for Pacific islanders and trust funds, and if islanders have a greater sense of ownership over trust fund resources relative to direct aid resources, then the argument could be made that trust fund resources will be better managed. Of course, like most other things in the Pacific, the results so far appear mixed. The cases of Kiribati and Tuvalu seem to support this argument. In fact, both governments have been criticized in recent years for adopting overly conservative management principles that have resulted in over-reinvestment and under-utilization of trust fund resources for development. On the other hand, the experiences of Nauru and Tonga where national trust funds were grossly mismanaged directly counter the endowment effect argument.

3 Trust Funds in the Asian Development Bank and Other Institutions

A review of trust funds at ADB and other development institutions reveals the following major trends. (For listings of trust funds administered by ADB, the World Bank and other institutions, see Appendices 3–7.)

- The use of trust funds in general is rising, but most are sinking and revolving funds; true trust funds are still relatively rare.
- The United States Agency for International Development (USAID) took an early lead with the use of true trust funds (endowments) in the late 1970s and uses them far more commonly than other organizations do.
- Environmental trust funds are the most common type of true trust funds used in the development arena. (See Appendix 8 and Box 3.)
- There is increasing diversification of trust fund financing (more multidonor funds) accompanied by an increase in targeted, specific-use, sectoral, and thematic funds (i.e., a diversification of sources and a concentration of uses).
- Where the right prerequisites and conditions have prevailed, trust funds have been largely successful in accomplishing their development objectives.

THE ASIAN DEVELOPMENT BANK

ADB administers numerous in-house funds that it calls “thematic,” “special,” or “trust” funds. All of these funds are fairly specific in their purposes and are typically established via bilateral or multilateral agreements with member countries. Thematic and special funds are established with ADB resources whereas trust funds use outside resources and ADB serves as trustee. Generally speaking, these funds would all fall into the sinking or revolving categories although some of them do earn interest.

ADB usually receives resources through channel financing and acts as administrator applying its own guidelines and procedures in recruiting consultants, making disbursements, and supervising projects. Since 1980,

Box 3
Environmental Trust Funds

With the ratification of the Convention on Biological Diversity in 1992 and other related developments, environmental preservation has become a clear global priority. As a result, environmental trust funds have proliferated and are now the most common type of specific-use trust fund in existence. Since 1990, more than 50 environmental trust funds have been established throughout the world and another 40 or so are estimated to be in the pipeline.

Trust funds are an effective mechanism for providing modest but sustainable income for environmental activities. They attract and disburse funding and are flexible, allowing money to be donated in many ways. Some environmental trust funds take the form of true trust funds, or endowments, and are therefore invested in capital markets. For a good example of a national environmental trust fund, visit the United Nations Development Programme (UNDP) Mongolian Environmental Trust Fund Program Web site at www.un-mongolia.mn

ADB has entered into channel financing agreements for trust funds with Australia, Belgium, Canada, Denmark, Finland, France, Italy, Japan, the Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland, and United Kingdom (UK). These funds cover many initiatives (renewable energy, climate change, poverty reduction, governance, water, gender and development, and poverty and environment) and several of them allow for multiple donors. (See Appendix 3.) In the Pacific, ADB has been instrumental in the establishment of several true trust funds by providing either technical or financial resources or both. They include the Falekaupule Trust Fund (Tuvalu), the RMI Trust Fund, and the Vanuatu Skills Training Fund.

In the case of the Falekaupule, ADB provided both technical assistance and a loan of A$6.5 million from 1999 to 2001. For the RMI Trust Fund (which initially stood alone but has since been incorporated into the Compact of Free Association agreement with the United States), ADB again provided technical assistance and a loan totaling US$3.8 million (US$1.8 through the Public Sector Reform Program and US$2 million through a program loan). For the Vanuatu Skills Training Fund, which is still being established, ADB provided technical assistance for setting up the organizational structure and implementation plans for the Fund, and further assistance has been programmed.

WORLD BANK

The World Bank (WB) has a long history (nearly 30 years) of administering mostly sinking and revolving funds and has developed an extensive social fund program. Most WB trust funds are set up through financial and administrative arrangements with outside donors (bilateral or multilateral including the private sector and foundations) although a handful of funds has received direct WB resources. WB funds are intended to provide grant funding in such areas as technical assistance, advisory services, debt relief, postconflict transition, and cofinancing. The WB trust fund portfolio was worth US$3.8 billion as of mid-2000 (value of funds held in trust), and 76% of assets were funded from bilateral donors between 1998 and 2000.

The WB recently improved the efficiency with which it manages trust funds, standardizing fund agreements and improving donor and reporting coordination. Trust Fund management is carried out by four organizational units: Trust Fund Operations, Strategy and Donor Relations, Trust Fund Accounting, and Trust Fund Quality Assurance and Compliance.

In addition to its many regular trust funds, starting in 1987 WB began administering what it calls social funds designed for shorter-term initiatives like emergencies and small, community-managed projects. In the past decade, WB has financed 108 social funds and similar demand-driven, multisector projects in 57 countries primarily in Latin America, the Caribbean, and sub-Saharan Africa for everything from water supply and sewerage rehabilitation to nutrition programs for mothers and infants thus benefiting more than 100,000 poor communities. Social funds are the most quickly disbursed part of WB's portfolio and are flexible because their use can quickly be adjusted to changing circumstances. However, the funds provide only limited, short-term financing, they do not always build institutional and technical capacity, and they may not always reach the very poor.

WB has occasionally used true trust funds but established the Global Environmental Facility in 1990 with the United Nations Development Programme (UNDP) and the United Nations Environment Program. The International Finance Corporation and the Multilateral Investment Guarantee Agency also administer several small trust funds.

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

USAID has had experience with both sinking and revolving funds, but most of its work has shifted towards true trust funds. Starting in the 1970s, USAID established, funded, or administered numerous endowments (see Appendix 6) and is considered the lead entity on using true trust funds for development. Most USAID endowments are focused on the environment and agriculture sectors although it has established some for economic and social development. USAID often partners with local institutions with established track records and sometimes creates new foundations to house endowments providing both extensive initial an ongoing technical assistance in addition to financial resources.

USAID endowments have targeted Latin America, Africa, and Asia with Latin America receiving the most attention. USAID has used endowments to help Latin American countries with debt reduction in return for establishing local currency trust funds for environmental and child survival programs (US$875 in debt relief had been granted to Argentina, Bolivia, Chile, Colombia, El Salvador, Jamaica and Uruguay as of 1996). USAID also provided endowments as part of its exit strategy in four "graduating" nations: Costa Rica, Korea, Panama, and Portugal. In Costa Rica and Portugal, these USAID-funded "legacy" endowments (founded in 1996 and 1985, respectively) were available for general economic and social use purposes. The Korea endowment was for science and technology, and the Panama endowment was for environmental activities. Very few endowments have been set up in or for the Pacific islands.

UNITED NATIONS DEVELOPMENT PROGRAMME

UNDP also uses what it calls "thematic" trust funds for development. They allow outside donors to provide supplementary funding to existing UNDP initiatives in its practice areas. Thematic trust funds follow a multiyear framework and cover such areas as democratic governance, poverty reduction, energy, environment, information and communication technology, HIV/AIDS, gender, and crisis prevention and recovery.

THE CARIBBEAN DEVELOPMENT BANK

The Caribbean Development Bank and USAID jointly established the regional, revolving Basic Needs Trust Fund (BNTF) in 1979. Subsequently, member countries also made contributions. The BNTF targets unemployment in rural communities and initially aimed to reduce short-term unemployment by financing public works. Through 2003, contributions to the BNTF reached US$105 million and the Caribbean Development Bank provided more than 414,000 person-weeks of employment to residents of poor communities across the region. Over time, the focus of the BNTF has shifted to human development and poverty reduction.

OTHER DEVELOPMENT INSTITUTIONS

The Inter-American Development Bank (IADB) and the African Development Bank also administer their own set of special-use and donor-directed trust funds (again, mostly sinking or revolving) structured similarly to those administered by ADB and the World Bank. (For a listing of IADB trust funds, see Appendix 5.)

4 The Development Setting

Pacific governments deny that they have serious economic and social problems. They do not indicate any intention of reforming their economies.
Helen Hughes *(Aid Has Failed the Pacific)*

There is significant cultural, socioeconomic, geographic, and political diversity among the PDMCs, so generalizations and blanket statements such as the one above should be avoided. Nevertheless, the PDMCs do share a number of common characteristics[3] that affect their overall development prospects.

COMMON CHARACTERISTICS AFFECTING DEVELOPMENT

High Population Growth. As of mid–2004, the 14 PDMCs had an estimated 8.6 million residents over half of whom resided in Papua New Guinea (PNG). In the 50 years leading up to 2000, they tripled their total population, (see Figure 4.1)

By 2050, the populations of Kiribati, PNG, Solomon Islands and Timor-Leste are expected to at least double and Fiji Islands, RMI, Nauru, Tuvalu, Tonga, and Vanuatu are all expected to nearly double growing by multiples of between 1.6 and 1.9 (see Figure 4.2). The low-growth countries (multiples of 1.4 or less) include Cook Islands, FSM, Palau, and Samoa.

[3] The majority of these are summarized in ADB's Pacific Strategy 2005-2009: Responding to the Priorities of the Poor.

Figure 4.1

Mid-Year Population of Pacific Developing Member Countries 1950 to 2050 (estimated)

PDMC	*1950*	*2000*	*2050*
TOTAL	2,526,593	7,858,335	16,347,123
Growth Multiple		3.1	2.1
PNG	1,412,466	4,926,984	10,670,394
Timor-Leste	435,529	846,599	1,942,734
Fiji Islands	287,348	832,494	1,447,573
Solomon Islands	106,647	466,194	1,110,514
Samoa	81,858	179,466	170,739
Vanuatu	52,000	189,618	310,486
Tonga	45,744	102,321	188,340
Kiribati	33,448	91,985	235,342
FSM	30,715	107,754	74,296
Cook Islands	14,575	20,407	24,930
RMI	10,904	53,064	102,761
Palau	7,251	18,766	26,300
Tuvalu	4,676	10,838	20,018
Nauru	3,432	11,845	22,696

Source: US Bureau of the Census, International Data Base

Figure 4.2

Estimated Growth of Pacific Developing Member Countries Populations 2000 to 2050

PDMC	*2000*	*2050*	*Growth Multiple*
Kiribati	91,985	235,342	2.6
Solomon Islands	466,194	1,110,514	2.4
Timor-Leste	846,599	1,942,734	2.3
PNG	4,926,984	10,670,394	2.2
RMI	53,064	102,761	1.9
Nauru	11,845	22,696	1.9
Tuvalu	10,838	20,018	1.8
Tonga	102,321	188,340	1.8
Fiji Islands	832,494	1,447,573	1.7
Vanuatu	189,618	310,486	1.6
Palau	18,766	26,300	1.4
Cook Islands	20,407	24,930	1.2
Samoa	179,466	170,739	1.0
FSM	107,754	74,296	0.7

Source: US Bureau of the Census, International Data Base

Low and Poorly-Diversified Economic Growth. With very few exceptions, PDMC economies are not keeping up with their high rates of population growth. Among the five regions of ADB, the Pacific has seen the lowest average rate of economic growth in recent years, and this trend is not expected to change any time soon (see Figures 4.3 and 4.3a).

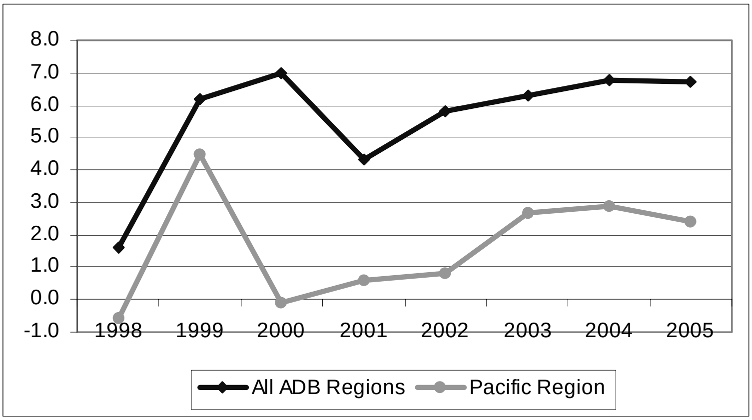
Figure 4.3
Gross Domestic Product Growth Rate: 1998 to 2005
(2004–05 estimated)

Region	*1998*	*1999*	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*	*Avg*
All Regions Avg	1.6	6.2	7.0	4.3	5.8	6.3	6.8	6.7	5.6
East Asia	2.8	7.0	8.0	4.6	6.7	6.5	6.9	6.8	6.2
Southeast Asia	6.8	4.1	6.3	1.9	4.2	4.6	5.7	5.4	4.9
South Asia	6.0	5.7	4.5	5.2	3.9	6.9	7.0	7.2	5.8
Central Asia	1.7	4.8	8.2	10.8	8.1	8.4	8.1	8.4	7.3
The Pacific	-0.6	4.5	-0.1	0.6	0.8	2.7	2.9	2.4	1.7

Source: ADB, Asian Development Outlook 2004

Moreover, most PDMC economies are poorly diversified and remain heavily reliant on a few industries with some clinging to just one or two.

Figure 4.3a
Gross Domestic Product Growth Rate: 1998 to 2005
(2004–05 estimated)



Falling Per Capita Gross Domestic Product. As a result of high population growth and low economic growth, per capita gross domestic product (GDP) is falling in most of the PDMCs. Per capita GDP grew in all ADB regions except for the Pacific which was projected to achieve an annual average of negative .5% from 1998 through 2004 (see Figures 4.4 and 4.4a).

Figure 4.4

Per Capita Gross Domestic Product Growth Rate: 1998 to 2005

(2004–05 estimated)

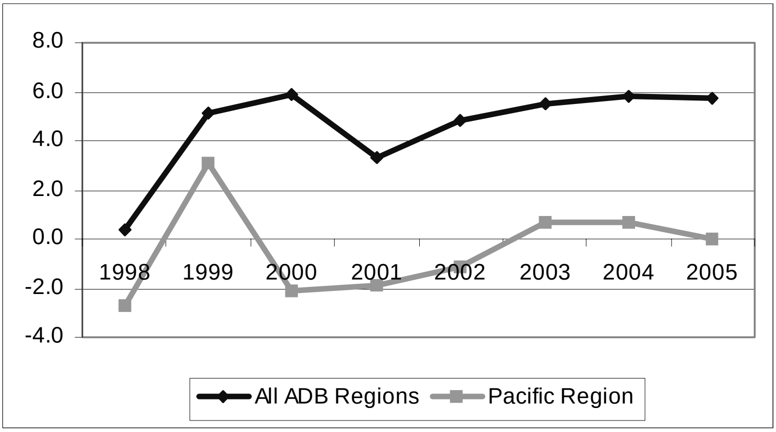
Region	*1998*	*1999*	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*	*Avg*
All Regions Avg	0.4	5.1	5.9	3.3	4.8	5.5	5.8	5.7	4.6
East Asia	2.0	6.2	7.2	3.9	6.0	6.2	6.3	6.2	5.5
Southeast Asia	-8.6	2.6	4.8	0.3	2.7	3.1	4.3	4.0	1.7
South Asia	4.0	3.8	2.7	3.3	2.1	5.1	5.3	5.5	4.0
Central Asia	1.5	4.3	7.7	12.9	9.0	8.1	9.0	8.9	7.7
The Pacific	-2.7	3.1	-2.1	-1.9	-1.1	0.7	0.7	–	-0.5

Source: ADB, Asian Development Outlook 2004

Figure 4.4a

Per Capita Gross Domestic Product Growth Rate: 1998 to 2005

(2004–05 estimated)



Fiscally Stressed. Maintaining fiscal balance is a major challenge for all PDMCs. Revenue collection has not grown sufficiently to keep up with increasing demands on publicly provided goods and services; consequently, some PDMCs continue to face fiscal gaps and generally weak fiscal positions (see Figure 4.5).

Figure. 4.5

Central Government Budget Balance as a Percentage of Gross Domestic Product: 2000 to 2005

(2004–05 estimated)

PDMC	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*
Palau	-15.6	-20.9	-28.1	-2.3	-12.4	–
Solomon Islands	-4.2	-11.5	-11.1	0.9	0.0	–
Federated States of Micronesia	-6.9	-6.2	2.5	1.9	1.9	-1.1
Fiji Islands[a]	-3.4	-6.6	-5.6	-6.1	-3.5	-0.8
Papua New Guinea	-2.0	-3.6	-4.1	-1.0	-1.5	-1.0
Cook Islands	-1.9	1.5	0.2	-3.2	–	–
Samoa	-0.7	-2.3	-2.1	-0.6	-1.5	–
Timor-Leste [b]	-6.2	-9.0	-10.1	–	–	–
Tonga	0.8	-0.9	-1.6	-3.1	-1.8	–
Tuvalu	15.4	-54.3	76.5	-16.3	-1.3	–
Vanuatu	-6.8	-3.7	-3.2	-1.1	0.4	0.4
Republic of Marshall Islands	8.9	2.2	14.8	14.1	6.2	–
Kiribati	26.4	7.6	21.4	-13.4	–	–
Nauru	–	–	–	–	–	–

Notes: a) excluding asset sales; b) excluding grants
Source: ADB, Asian Development Outlook 2004

Still Highly Dependent on Aid. Donors have long played an important role in financing development in the Pacific, and this is unlikely to change any time soon. The United States General Accounting Office reported in 2001 that between 1987 and 1999, about US$12 billion (in 1998 US$) in assistance was given to the Pacific islands (this includes aid to Niue and excludes aid to Timor-Leste). As shown in Figure 4.6, in the decade between 1993 and 2002, many PDMCs received foreign assistance levels representing more than one fifth of their gross national incomes (GNI). In 2002, Timor-Leste, RMI, FSM, Kiribati, and Palau all received assistance representing 20% or more of their respective GNIs.

Figure 4.6

Foreign Aid as Percentage of Gross National Income

Country	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Timor-Leste	–	–	–	–	–	0.0	57.0	71.0	48.0	53.0
RMI	36.0	51.0	33.0	67.0	60.0	46.0	56.0	49.0	61.0	48.0
FSM	30.0	47.0	32.0	48.0	42.0	35.0	46.0	41.0	57.0	46.0
Kiribati	28.0	23.0	19.0	17.0	17.0	19.0	22.0	20.0	13.0	22.0
Palau	–	242.0	145.0	56.0	33.0	76.0	24.0	28.0	25.0	22.0
Tonga	22.0	24.0	25.0	19.0	15.0	15.0	13.0	12.0	14.0	16.0
Samoa	31.0	26.0	22.0	14.0	11.0	16.0	10.0	12.0	18.0	15.0
Vanuatu	19.0	22.0	21.0	14.0	12.0	18.0	16.0	21.0	15.0	12.0
Solomon Islands	22.0	17.0	15.0	13.0	10.0	13.0	13.0	24.0	20.0	11.0
Papua New Guinea	7.0	6.0	8.0	8.0	7.0	10.0	7.0	8.0	7.0	7.0
Fiji Islands	4.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0

Note: Nauru, Tuvalu, and Cook Islands are not shown as they are not World Bank members.
Source: World Bank, World Development Indicators Database

While the flow of assistance to the region remains steady, donors are closely re-evaluating their programs and placing increasing emphasis on accountability and improved effectiveness.

Weak Private Sector and State-Owned Enterprises. The private sectors in the PDMCs have not grown sufficiently and have not created enough jobs to match the high population growth rates. Moreover, state-owned enterprises, most of which are inefficient and place heavy burdens on government finances, still play prominent roles in their economies (ADB 2004d).

Slow Progress in Social Development. Most indicators suggest that progress in social development is slow. Recent analyses by both ADB and the World Bank suggest that overall progress towards the Millennium Development Goals in the Pacific is mixed but generally off target (ADB 2003b and World Bank 2004a).

Weak Infrastructure. Much of the foreign assistance provided to the PDMCs over the past several decades has gone towards capital infrastructure. However, due to poor design and maintenance (among other factors), infrastructure remains a key weakness. This includes transportation, communication, energy, water, education, and health.

Uneven Development. Development has focused on urban centers and has left the rural areas and outer islands with insufficient infrastructure.

Emergence of Poverty and Rising Inequality. While extreme poverty has yet to emerge in the PDMCs, mild poverty and inequality are rising. Ongoing analysis by both ADB and the World Bank indicate widening gaps between the lowest and highest income groups. ADB studies on poverty have found that it most commonly manifests itself as hardship in meeting basic needs rather than as absolute or food poverty (Abbott and Pollard 2004). An estimated 25% of the population in Fiji Islands, Kiribati, FSM, PNG, Solomon Islands, Timor-Leste and Vanuatu are estimated to be living in poverty.

Weak Policy and Institutional Environments. These pose significant constraints to development and will be a primary focus of the new ADB Pacific strategy.

Threatened Natural Environments. High population growth coupled with urbanization and poor planning have led to increasing environmental degradation. Environmental and natural resource management is gaining wider attention in the region as ecosystems and resource stocks are threatened.

Economically Vulnerable. The PDMCs have higher probabilities of macroeconomic, trade, and natural shocks that can cause sudden declines in economic activity and push more people into poverty (World Bank 2004a). In the event of such shocks, PDMC economies will be harder hit and will take longer to recover than those less vulnerable.

POSITIVE DEVELOPMENTS AND LOOKING FORWARD

On the positive side, several developments are noteworthy. The PDMCs have not seen any major macroeconomic and fiscal crises in the recent past aside from those in the Solomon Islands and Nauru. Some PDMCs are successfully building key niche industries that are contributing to overall development and job creation including tourism and marine industries. Some PDMCs have undergone significant reforms that have helped to optimize their public sectors and to gear them towards continued progress. Foreign direct investment is also rising in some countries.

Looking forward, a number of issues and trends in both the near and far term will continue to shape and influence developments in the Pacific. These include such issues as high population growth and other demographic trends, urbanization and outmigration, climate change and other environmental threats, political stability and security issues, and globalization.

5 Case Analyses: Trust Funds in the Pacific Developing Member Countries

The use of trust funds for development and other purposes is not new to the Pacific. In fact, the Kiribati Revenue Equalization Reserve Fund (established in 1956) and the Tuvalu Trust Fund (established in 1987) have gained worldwide attention as pioneering cases, each illustrating how trust funds can be used with relative effectiveness to support development in small nations (see Box 4).

For both Kiribati and Tuvalu, the establishment of trust funds generally coincided with their political coming of age, and today their funds are proud expressions of their sovereignty. While on the whole both of these trust funds are deemed successful in meeting their objectives, each offers some lessons worth discussing.

In addition to the Kiribati Revenue Equalization Reserve Fund (RERF) and the Tuvalu Trust Fund (TTF), the Compact of Free Association (COFA) Trust Funds between the United States and Palau, FSM, and RMI; the Nauru Phosphate Royalties Trust; the Tonga Trust Fund; the Tuvalu Falekaupule Trust Fund; and the Marshall Islands Nuclear Claims Fund are analyzed. Each analysis will look at why the fund was established, its primary objectives, general governance and structure, and overall performance.

KIRIBATI REVENUE EQUALIZATION RESERVE FUND

The RERF was established in 1956 during the United Kingdom's colonial administration of the Gilbert (now Kiribati) and Ellice Islands (now Tuvalu). The RERF was capitalized using tax revenue from phosphate mining and was established in anticipation of phosphate exhaustion and to help balance the government's future recurrent budget. The Government of Kiribati acts as both the trustee and beneficiary and, therefore, has sole authority over investment, distribution, and utilization of RERF resources. The RERF is considered a special fund, established through the Public Finance (Control and Audit) Act, and its governing policies are proposed by the Minister of Finance and approved by the parliament. A Reserve Fund Committee has oversight and management responsibility for the fund. It consists of the

Box 4
The Smallest States: Perennially Disadvantaged?

A 2001 study on foreign assistance to the Pacific conducted by the US General Accounting Office stated that, "Most donors expect long-term dependence on assistance in the Pacific." (GAO 2001). While all Pacific nations are currently very dependent on assistance (and have been for many years), they are not all created equal. Some PDMCs are unquestionably better suited for growth than are others. This long-term dependence sentiment, therefore, is perhaps most applicable to the region's smallest states as measured by population, natural and other endowments, and propensity for sustained economic growth. One long-term expert on the region poignantly noted that some may have permanent diseconomies of scale because of their small, scattered populations.

If, in fact, some PDMCs have low propensities for sustained growth, then trust funds may indeed be an ideal compensating mechanism. This argument may already be immaterial, however: five out of the six smallest PDMCs (by population) have already established funds.

Minister of Finance and Economic Planning (Chairman), the Secretary to the Cabinet, the Chief Accountant, and two other persons appointed by the Chairman. The Committee sets overall policies and guidelines.

During the Reserve Fund's formative years, the Kiribati Government strictly followed a conservative capital accumulation and reinvestment policy that allowed the fund to grow from its original A$556,000[4] in 1956 to $69 million by 1979. From 1973 to 1979 alone, $33 million was paid into the fund. The Government has gradually shifted from a conservative, fixed income-heavy capital growth strategy to a balanced portfolio strategy that aims to maximize interest income and capital growth (Teuea 1993). The fund currently has internationally diversified debt, equity, and foreign exchange holdings.

The RERF operates on a minimal draw-down principle preferring instead to reinvest most annual earnings. In the early 1990s, however, as other revenue sources waned and overall fiscal expenditure steadily increased, there was

[4] All figures for this trust fund are in Australian dollars

mounting pressure to draw on the fund. In response, the government set an annual draw-down limit. Under a new policy, the real per capita value of the fund is not to fall below the 1996 level of $4,500. (The Australian Consumer Price Index is used to determine the fund's real value.) Investment income above the maintained real per capita 1996 level is transferred to the government's annual budget for general-purpose use.

Figure 5.1

Kiribati Economic Data (A$ millions): 1991 to 2002

Subject	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Nominal GDP	43.5	46.2	48.6	54.4	62.1	63.8	64.3	76.3	83.3	83.2	91.3	98.2
Total Budget Revenue (Recurrent & Grants)	65.0	80.9	69.0	64.8	72.2	62.8	92.5	117.2	99.2	106.3	–	–
RERF Year-end Market Value	263.2	295.8	353.4	318.3	367.9	371.8	458.9	570.1	601.5	658.0	635.9	576.0
RERF Draw downs	2.0	6.5	5.5	4.4	7.5	13.6	8.0	0.0	0.0	0.0	8.0	0.0
% of GDP	5	14	11	8	12	21	12	0	0	0	9	0
% Total Budget Revenue	3	8	8	7	10	22	9	0	0	0	–	–
Budgetary Aid/Grants	25.9	22.4	34.7	20.5	16.7	12.2	16.6	18.1	25.8	17.8	19.0	–
% of Total Budget Revenue	40	28	50	32	23	19	18	15	26	17	–	–
Current Acct Official Transfers (Credits)	15.1	13.1	14.9	7.9	7.6	13.2	10.4	8.0	8.4	18.9	–	–
% of GDP	35	28	31	15	12	21	16	11	10	23	–	–
Foreign Aid as % of GNI	32	43	28	23	19	17	17	19	22	20	13	22

Sources: Kiribati Government Budget reports, ADB, World Bank, PRISM

Key Issues and Lessons

Prudence Pays... but not Excessive Prudence? The Kiribati government has been very prudent in preserving, growing, and contributing to the RERF. As result, the fund has grown over one thousand fold in nominal terms since inception from $556,000 to nearly $600 million today. While this is certainly laudable, some have criticized the government for being too frugal, especially when revenue from other sources has dipped and with respect to priority areas like social sectors. The Kiribati government might have better utilized the RERF for macroeconomic stabilization. The government's continued frugality suggests that perhaps its target capital level for the fund has yet to be reached although available literature on the RERF does not indicate any such target exists.

RERF Contributions Significant. To date, the fund has injected nearly $114 million into the Kiribati budget, a significant amount considering the size of the economy (nominal GDP is under $100 million). From 1991 to 2002, the fund's annual average contribution as a percentage of total government revenues was about 7%.

RERF Contributions too Erratic. RERF contributions to the national budget have been quite erratic. From 1991 to 2002 (see Table 5.1) drawdowns ranged from $13.6 million (22% of the annual budget revenues for 1996) to zero. These erratic contributions have likely complicated Kiribati's fiscal and economic planning especially with the accompanying volatility seen in other important revenue sources like fishing license fees.

Recently, the government has expressed intentions to restructure the RERF into a "protected reserve fund" or "core reserve fund" which can't be accessed and a second, accessible "reserve fund" from which drawdowns can be made. This structure matches that of the Tuvalu Trust Fund which has proven to be ideal for smoothing out trust fund contributions (see case analysis on the Tuvalu Trust Fund).

RERF Governance too Thin? Three government officials and two additional persons (appointed by the Minister of Finance and Economic Planning who serves as Chairman) have authority over the RERF, its investment policies, and its operating guidelines subject to the consent of the cabinet (Nimmo-Bell 1999). This setup has raised some concern that decision-making authority rests with too few people and that additional oversight and advice should be provided perhaps via an independent advisory committee like that for the Tuvalu Trust Fund. While the government has exercised great caution with RERF spending, some argue that it would not be difficult for this trend to quickly reverse especially in times of political transition.

Recently proposed statutory restructuring of the RERF would make it more robust and would increase transparency, but it is unclear whether this restructuring and the additional protective measures have been implemented.

Kiribati's Reliance on Foreign Aid has Fallen. While the causal relationship between RERF contributions and reliance on foreign aid is still tenuous, during the last decade Kiribati's reliance on foreign assistance appears to have fallen. As indicated in Table 5.1, budgetary aid and grants (in absolute terms and as a percentage of budgetary revenue) as well as foreign aid as a percentage of GNI have all decreased over time. Official transfers in the current account have remained somewhat stable in absolute terms but have slightly declined as a percentage of GDP.

THE TUVALU TRUST FUND

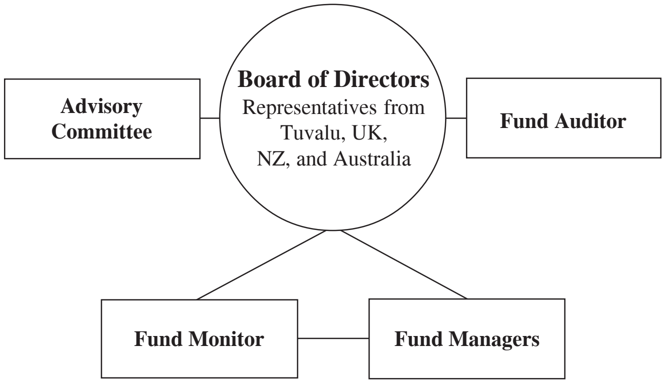
The Tuvalu Trust Fund is considered the most successful public fund in the Pacific, and Tuvalu, which became independent in 1978, has gained a reputation as a model for the effective use of trust funds for small-state economic development. The TTF was established in 1987 through a multilateral international agreement among Tuvalu, New Zealand, the UK, and Australia. The fund was initially capitalized with A$27.1 million[5] in contributions from the UK ($8.5 million), New Zealand ($8.282 million), Australia ($8 million), Tuvalu ($1.6 million), Japan ($.695) million and the Republic of Korea ($0.031 million). It was set up to contribute to the financial stability of Tuvalu by providing an additional source of revenue for recurrent expenses and to set the country on a path towards greater financial autonomy (Saitala 1995).

The TTF is governed by a Board of Directors consisting of one representative each from Tuvalu (who serves as Chairman), Australia, New Zealand, and UK. Moreover, a separate Advisory Committee consisting of government and donor representatives provides additional advice and input to trustees' decision making (refer to Figure 5.2 for management structure). Like the RERF, the TTF is subject to parliamentary scrutiny. Although governance of the TTF is multinational, Tuvalu has significant autonomy over investment decisions and the use of fund proceeds. Trust fund assets are invested primarily in Australian capital markets and are currently managed by two investment managers holding a mixed portfolio of equities, fixed income, and cash. Tuvalu has set an initial target market capitalization value of $100 million after which it may consider a halt to reinvestment.

In an effort to smooth out trust fund contributions to the recurrent budget and to therefore improve the predictability and consistency of transfers, the Tuvalu government established a second fund into which trust fund earnings would be deposited. This "buffer account" greatly benefits planning by reducing the volatility of drawdowns and allowing the government to continue making them during years when the primary trust fund earnings are zero or

[5] All figures for this trust fund are in Australian dollars.

Figure 5.2
Tuvalu Trust Fund Management Structure



negative. Unlike the primary trust fund, governance of the buffer account falls entirely upon the Tuvaluan government.

The buffer account, later named the Consolidated Investment Fund (CIF), receives transfers from the primary fund and serves as a repository for other intermittent income like revenue from Tuvalu's Internet domain name (".tv") and fishing license sales. On the other hand, withdrawals from the CIF include drawdowns into the recurrent budget as well as capital reinvestments that are back-transferred into the primary trust fund. In essence, Tuvalu has devised a unique, binary structure with a primary true trust fund operating alongside a secondary revolving fund (see Figure 5.3 for details on the resource flows). The value of the fund had grown from its original \$27.1 million to \$81.3 million as of spring 2004.

Figure 5.3
Tuvalu Trust Fund Resource Flows

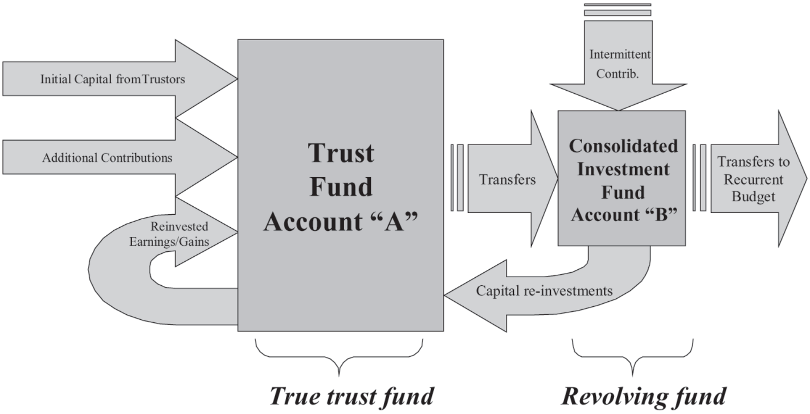


Figure 5.4
Tuvalu Economic Data (A$ millions): 1996 to 2002

Subject	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Nominal GDP	15.8	17.1	20.3	21.2	24.0	26.4	27.5
Total Budget Revenue (Recurrent & Grants)	24.3	27.2	32.1	32.1	56.2	34.9	45.3
TTF Year-end Market Value	48.9	59.1	57.0	59.9	66.6	62.9	70.6
Distributions from TTF	–	3.9	11.1	2.7	4.2	11.5	–
% of GDP	–	23	55	13	17	44	–
% Total Budget Revenue	–	14	35	8	7	33	–
Budgetary Aid/Grants	16.0	11.7	5.1	9.9	8.9	1.4	2.0
% of Total Budget Revenue	66	43	16	31	16	4	4
Current Acct Official Transfers (Credits)	15.1	11.7	4.7	–	–	–	
% of GDP	96	68	23	–	–	–	–

Sources: Tuvalu Government Budget Reports, ADB, PRISM

Key Issues and Lessons

Multinational and Multiparty Governance Effective. This fund is unique in that it is overseen by a multinational board in conjunction with a multinational advisory committee. The two entities serve to collectively manage the fund, adding an extra layer of oversight diligence. The advisory committee (consisting of qualified economists and other experts) has been especially instrumental in bringing the management of the fund into the larger public financial and development management picture.

Binary Trust Fund Structure Innovative and Efficient. Like the two management bodies, the two fund accounts work in conjunction to improve the overall efficiency of the fund. This binary structure has evolved over time. The CIF account initially served as a simple stabilizer for drawdowns, but its role has grown and it now also serves as a conduit and management tool for other development resources.

Trust Fund Contributions Economically Significant. Between 1997 and 2001, the fund's annual average contribution to government revenues was 20%. In its first 9 years (from 1987 to 1996) the fund yielded $25.1 million: $9.7 million to the recurrent budget, $7 million reinvested, and $8.4 million transferred to the CIF.

Reliance on Foreign Aid Appears to be Falling. Again, while the evidence and causality are questionable, there appear to be downward trends in budgetary aid in both absolute terms and in percentage of total budget revenue as well as in current account official transfers in absolute terms and as a percentage of GDP, at least for the period 1996 to 1998 (see Figure 5.4).

PALAU COMPACT OF FREE ASSOCIATION TRUST FUND

The Palau Compact of Free Association (COFA) Trust Fund was established in 1995 under section 211 of the Compact of Free Association with the United States. This was a front-loaded fund capitalized with a US$66 million[6] contribution from the US in 1995 and a $4 million follow-up contribution in 1997. The primary objective of the fund is to augment the government's recurrent budget. It was designed with a 50-year horizon commensurate with the life of the Compact to produce a net return of $15 million by its 15th anniversary and to continue providing for another 35 years. This, by design, is a sinking fund.

[6] All figures for this trust fund are in US dollars.

The Compact states that the fund shall be owned by the Government of Palau and that the expiration of the Compact shall not affect this. The Palauan Board of Trustees is overseen by the President and is to meet with the US every 5 years to review the management and progress of the fund. Palau must inform and receive approval from the US on all investment decisions and drawdowns (with at least 60 days notice).

The Compact allowed Palau to begin making drawdowns 4 years after the fund's inception; however, Palau has not exercised this option choosing instead to continue growing the fund until it can sufficiently augment government revenue by its 15th anniversary. The fund had grown from its original $66 million to nearly $150 million as of March 2004 including the $4 million subsequent contribution in 1997 (Government of Palau 2003).

Key Issues and Lessons

Original Performance Goal too Ambitious? The fund's original objective of producing $15 million in net returns by its 15th anniversary required a sustained annual rate of return of 12.5% which is not a very conservative assumption. By early 2004, the fund had an average annual return of 10.3% (Merrill Lynch 2004).

Palauan Owned and Managed. This Compact trust fund is unique in that it is wholly owned and managed by the recipient government with relatively little oversight from the donor. This differs markedly from the two newly established Compact funds for RMI and FSM.

Sinking Fund Turned True? By its design, this is a sinking fund; however, Palau has taken the conservative path and is managing it as a true trust fund. While Palau has had the option of drawing down $5 million annually from the fund beginning in 2000, it has opted instead to stick to a strict capital growth strategy and has delayed the draw-down process.

MARSHALL ISLANDS INTERGENERATIONAL TRUST FUND AND COFA TRUST FUNDS

RMI established its Marshall Islands Intergenerational Trust Fund (MIITF) in 1999 to help the government achieve budgetary self-reliance. A number of sources capitalized the fund: US$0.75 million[7] from RMI, ADB injections of $1.8 million (under the Public Sector Reform Program loan)

[7] All figures for this trust fund are in US dollars.

and $2 million (under the Fiscal and Financial Management Program loan), and supplementary Compact funds in fiscal years 2002 and 2003 worth $15.5 and $14 million, respectively (these were the so-called “bump-up” funds). As of late 2003, the fund had reached just over $33 million but had yet to be formally invested.

Meanwhile, Compact renegotiations with the US commenced and the concept of a Compact trust fund was introduced by the government with strong backing from ADB. Initially reluctant, the US eventually agreed to incorporate a trust fund as a core component of the new 20-year Compact economic package. The new fund is designed to replace annual grant assistance from the US beyond 2023 and more generally to contribute to economic advancement and long-term budgetary self-reliance.

Under the new Compact trust fund terms, the US will contribute annually to the fund for 20 years with the first contribution totaling $7 million and each subsequent contribution growing by increments of one-half million dollars each year (with inflation adjustments). US contributions are contingent upon an initial RMI contribution of at least $25 million and two subsequent $2.5 million contributions in 2004 and 2005. The US and RMI shall also seek additional contributions from other sources. The fund situs and governing law is within the US. It is governed by a US-dominated Trust Fund Committee consisting of three US members (including the Chairman) and two RMI members. Annual audits and reports are required.

The US can withdraw the present market value of its contributions if RMI fails to use fund income for the agreed purposes, if RMI fails to meet its mutual security obligations (under separate sections of the Compact), or if RMI takes any action which is deemed incompatible with US security and defense interests in or relating to RMI.

Structurally, the fund has a fairly sophisticated setup with three primary accounts serving the following functions.

- Account A (a true trust fund established as of the effective date of the Compact) serves as the corpus, is kept in perpetuity, and is not to be consumed.
- Account C (a revolving fund established at the same time as account A) serves as a repository for annual investment income from account A in excess of 6% during the initial 20-year term but is to maintain a balance of no more than three times the estimated real value of the FY2023 annual grant assistance and thereafter serves as a buffer between accounts A and B.

- Account B (a revolving fund to be established in FY2023) is to hold each prior year's investment income, beginning in FY2023, to be drawn down into the following year's recurrent budget. Any excess in this account shall be transferred to account C if it needs replenishment (to maintain its target balance), or will be transferred back to account A as capital reinvestment.

Key Issues and Lessons

A Disappointing Start. The establishment of the MIITF and its quick capitalization of $33 million clearly demonstrated the government's seriousness about taking a longer-term outlook. However, two events that occurred shortly after the establishment of the fund raise concerns over governance, transparency, and basic economic rationale. In 2003, the government transferred $7 million from the trust fund to the Marshall Islands Development Bank for lending. Assets designated for the future well being of the nation were therefore redirected towards other interests. Moreover, an impulsive and ill-informed equity investment decision by some members of the then interim MIITF board resulted in a nearly $1 million loss to the fund. These actions will have certainly affected the US stance on the overall structure and governance of the proposed Compact trust fund.

US-Held and US-Controlled RMI Trust Fund. Quite unlike the Palau Compact, this fund is neither fully owned nor controlled by RMI.

Sophisticated Setup, but Will it Work? The trust fund setup is more complex than that of the Tuvalu Trust Fund, but there remains uncertainty over whether the fund will be of sufficient size to generate adequate returns to fully replace US grant assistance in 2023. Next door in FSM, advanced economic modeling conducted by ADB-funded economists found many shortcomings in the FSM fund's structure and agreed-to terms, many of which are directly applicable to the RMI fund (see FSM case study).

Other Trustors Welcome. The trust fund agreement allows RMI to seek other sources of funds, an option that the government is actively exploiting with ongoing solicitations to other development partners. This will help RMI hedge against the risk of having an under-capitalized fund in 2023.

FSM TRUST FUND AND FSM COFA TRUST FUND

Like RMI, FSM took the initiative to establish its own trust fund in 1999. It capitalized the fund with US$3 million[8] from national and state resources. Again like RMI, FSM entered into negotiations with the US shortly thereafter and the concept of a Compact trust fund was introduced. The idea followed through and the Compact fund was established as part of the overall renegotiated economic package. The Compact fund called for FSM to contribute $30 million before Sept 30, 2004. With this in place, the US agreed to provide $16 million from 2004 through 2006 and to increase its contributions by $0.8 million every year thereafter through 2023. The objectives and structure of the fund are practically identical to those of the RMI Compact fund.

Key Issues and Lessons

Trust Fund Not Likely to Meet All Objectives. Economists in FSM closely analyzed the proposed fund structure and terms and conducted a detailed economic modeling analysis to test different scenarios. While the details of this analysis will not be covered here, in short, it found a number of weaknesses in the proposed fund design and agreement and raised a number of important questions relevant to both the FSM and RMI funds, most of which remain unanswered.

Some of the critical conclusions reached by this analysis are that the negotiated FSM Compact Trust Fund agreement:

- fails to protect the real value of the trust fund;
- fails to provide a stable source of revenue through market downturns;
- places too much emphasis on making annual distributions equal to the real value of the FY2023 sectoral grants;
- fails to provide for the certain establishment of the C account (the B account is unnecessary).

Based on simulations, a collapsing real value of the fund is a likely outcome (Economic Management Policy Advisory Team 2002).

[8] All figures for this trust fund are in US dollars.

NAURU PHOSPHATE ROYALTIES TRUST

The Nauru Phosphate Royalties Trust (NPRT) is a legal entity that holds four separate funds: the Long-Term Investment Fund, the Land Owners Royalty Trust Fund, the Housing Fund, and the Rehabilitation Fund. As the names suggest, each fund was established for a specific purpose.[9] The NPRT was established in 1968 using dividends and taxes associated with phosphate mining (similar to the Kiribati Revenue Equalization Reserve Fund). While exact details of the governance structure are not available, authority over fund investment and use are entirely the responsibility of the Nauru Government.

The trust was established in anticipation of the exhaustion of phosphate deposits and revenues that was forecast to occur on or around 2000. Beginning in the late 1980s, however, demand for phosphate began to subside while extraction costs began to increase. As a result, Nauru's long-held competitive advantage and windfall revenues began to wane. With phosphate revenues falling throughout the 1990s, in order to maintain its recurrent spending levels the Government began to borrow from commercial banks (including its own) using trust fund assets as collateral. At one point, the government even resorted to drawing directly on fund assets to finance expenditures. This, coupled with significant investment losses (many in real estate), diminished trust fund resources from a high of A$1.5 billion[10] in 1990 to just under $100 million today (Hamilton 2003 and Government of Nauru 2003).

The collapse of the NPRT has occurred against a backdrop of other major national crises, and Australia has stepped in with humanitarian and development assistance. Nauru is currently attempting to cut expenditures, downsize its public sector, close some overseas consulates, sell off assets, diversify its governmental revenue, and restructure its trust funds. However, assets held by the NPRT are reportedly fully mortgaged.

Key Issues and Lessons

Rampant, Systemic Mismanagement. Mismanagement appears to have permeated all levels of the Nauruan fiscal system. The same forces that drove the macroeconomy into insolvency were also responsible for draining nearly all of the funds' assets.

[9] Nauru also established the Nauru Royalty Fund, the Nauru Development Fund and the Nauru Landowners Cash Royalty Fund, but these three were not managed under the NPRT and are not analyzed here.

[10] All figures for this trust fund are in Australian dollars.

Almost Every Rule Broken. Nauru broke almost every rule in the book; its trust fund governance structure was weak and not transparent, it made poor trust investments, it raided its funds and used them as collateral, and it maintained an unwarranted expansionary fiscal position.

TONGA TRUST FUND

The rise and fall of the Tonga Trust Fund is perhaps best summed up in the following Pacific Islands Report[11] headlines:

July 31, 2000	-	*Tonga Plans to Boost Foreign Reserves…*
August 29, 2001	-	*Gloomy US Economy Hurting Tonga…*
August 31, 2001	-	*Worried Tongan MP Fuko Seeks Report on Reserves Account…*
September 25, 2001	-	*Tongans Not Laughing After Losing Millions Invested By Court Jester…*
October 5, 2001	-	*Tonga Trust Fund: No Hard Cash…*
October 24, 2001	-	*Tonga Government Apologizes to the People Over Trust Fund Loss…*

The Tonga Trust Fund was established under the Tonga Trust Fund Act of 1988 as a repository for revenue from the sale of special person passports to provide funds for national emergencies and occasional projects. As stipulated under the Act, the fund is governed by three trustees: the Prime Minister (Chairman), the Minister of Finance, and the Minister of Justice who is also the Attorney General. The trustees make decisions on the investment and management of the fund with approval from a Privy Council that is chaired by the King.

The fund was initially invested in term-deposits with the Bank of America in 1988. It remained there unmanaged for 6 years earning less than 3% interest per annum. By 1991, deposits had reached US$30 million.[12] In 1994, an employee of the bank, a Mr. Bogdonoff, approached the Tongan government and recommended a more active investment strategy. With agreement from the government, Bogdonoff began managing fund resources investing in equity and bond holdings and earning the fund a healthy $11 million from 1994 to 1999 (Tupou 2001).

[11] www.pidp.eastwestcenter.org/pireport
[12] All figures for this trust fund are in US dollars.

In 1999, Bogdonoff resigned from the Bank of America and proposed (competing with two other firms) to be Tonga's investment advisor. Bogdonoff was chosen based on his track record and lower proposed management fees. Soon thereafter, Bogdonoff warned the trustees of a forthcoming downturn in the capital markets and recommended a set of alternative investments. The most prominent of these was a $20 million investment in life settlements (purchases of life insurance policies held by persons with limited life expectancies). While exact details on the amounts and placements of these investments are not clear, essentially within 2 years losses on these alternative investments (due to bankruptcies, erroneous valuations, and other mishaps) collectively drained the fund of approximately $26 million. In early 2001, the Tongan public began vocalizing its concern over the status of the fund's resources. Audit reports on the fund, which had been provided through 1999, had not been available in 2000 and 2001, causing widespread concern and suspicion among the public and some members of parliament who were also concerned over the status of a $6.9 million "loan" that the Tongan government had drawn from the trust fund in 1998. In 2002, after a series of government sackings and widespread public outcry and debate over the trust fund scandal, the Tongan government announced that it had initiated a lawsuit against three individuals and six companies seeking to recover $26 million (Government of the Kingdom of Tonga 2002).

Key Issues and Lessons

Trust Fund Losses Economically Significant. The Tongan people have suffered an immense loss over the trust fund scandal. The sum of $26 million is equivalent to about 20% of the nation's GDP (nominal GDP was just under $150 million in 2001) and about 75% of the nation's annual budget.

Trust Fund Falls Outside of Fiscal System. The trust fund was technically set up as a "rainy day" fund to be used for occasional activities (emergencies or projects) when and where deemed necessary. As such, the fund stands alone and its resources do not come under the same scrutiny and accountability as normal public funds. This is a structurally weak setup that increases the potential for the misuse of resources. Even after the passage of the Trust Fund Act in 1988, fund resources still fell outside of the fiscal system. As an example, the 1998 "loan" that was drawn from the fund was made with unclear repayment terms (Pacific Islands Report 2001). The loan's terms and status were still unclear even to some members of parliament as of 2001, 3 years after the loan had been made.

Trust Fund Law Broken (at least twice). According to the Trust Fund Act, US investments were never allowed in the first place. A legal interpretation of the Trust Fund Act in 1999 stated that trust fund resources could only be invested through trustee securities or bank deposits with certain British and European companies. Secondly, the trustees' approval of the alternative investments was made via a June 21, 1999 letter that pre-dated the Privy Council's approval of the investment by 4 days (Tupou 2001). These actions run contrary to the Trust Fund Act.

TUVALU FALEKAUPULE FUND

The Falekaupule Trust Fund (FTF) is a specific-use fund established in July 1999 as part of a larger decentralization process to help finance development in the outer islands. While it is structurally similar to the Tuvalu Trust Fund (with a binary setup), it is unlike the TTF in that it is entirely Tuvaluan held. Established under the Falekeupule Act, the fund manifests an agreement between the national and local governments (*kaupul*e). The trustees are representatives from the eight *falekaupule.*[13]

The fund was capitalized with A$9.6 million:[14] $4.8 million in contributions from the national government (a $4 million direct grant and an $800,000 incentive contribution), a $4 million loan from ADB (to the national government) and $800,000 in contributions from the eight *falekaupule* ($100,000 each). Subsequent contributions have added to the fund. As of mid-2002, the fund had grown to over $16 million. The *kaupule* are the beneficiaries of the fund, and distributions are made according to the proportion of each island's original contribution.

Key Issues and Lessons

So Far, So Good. While this is a relatively new fund, most indications on its progress are positive. A 2003 ADB report concluded that, "Almost all of the money has gone to worthwhile projects that benefit the community" (ADB 2003).

However, some projects were not deemed beneficial for the community at large and there has been reluctance to spend all FTF resources (there's been a preference to reinvest) as well as a preference to seek donor funding

[13] Falekaupule is the name for the traditional decision-making body comprising of island community elders and chiefs.

[14] All figures for this trust fund are in Australian dollars.

for some less-urgent projects. A “negative list” has been developed to better identify appropriate projects for the fund.

MARSHALL ISLANDS NUCLEAR CLAIMS FUND

Effective in 1986 under the Compact of Free Association between the US and RMI (section 177), the Nuclear Claims Fund was established to provide compensation to citizens of the Marshall Islands (or the Federated States of Micronesia or Palau) for effects related to the US nuclear testing that took place in the Marshall Islands between 1946 and 1958. Under the agreement, the US provided $150 million[15] to create and maintain (in perpetuity) a fund to address past, present, and future consequences of the testing program. The agreement had a built-in investment performance assumption of $18 million beginning in the first year (a 12% target return in the first year). Within a year of its formal investment, the fund incurred a 15% devaluation as a result of the US stock market crash in October 1987. As a result, the fund would have had to yield annual returns of nearly 14% to reach the $18 million annual income target.

Four additional trust funds (held by Bikini, Enewetak, Rongelap, and Utrik) were to be capitalized with Nuclear Claims Fund disbursements, and each of these funds was to be held in perpetuity to provide resources to its respective recipients. Each of the four funds received 60 quarterly disbursements beginning in 1987: Bikini received a total of $39 million, Enewetak $25.35 million, Rongelap $19.5 million, and Utrik $11.7 million (Nuclear Claims Tribunal 2004).

Key Issues and Lessons

Unrealistic Expectations and Unforeseen Events. The unrealistic investment performance assumptions built into this fund coupled with unforeseen events (like the stock market crash and compensation payments exceeding investment returns) have prevented the fund from fulfilling its original investment performance goal. This has forced RMI to draw on the fund’s corpus (this was allowed under the original agreement) and has led to the fund’s failure to satisfy its overarching objective of providing a perpetual means to address consequences of the testing program. As a result, while it was originally designed as a true trust fund, it effectively has become a sinking fund. The fund’s current value as of mid-2004 stood at just over $5 million.

[15] All figures for this trust fund are in US dollars.

6 A Summary of Good Practices

WHY AND WHEN A TRUE TRUST FUND SHOULD BE ESTABLISHED

The establishment of a true trust fund should be considered when one or more of the following conditions hold:

- when there are unanticipated, excess resources available (such as windfalls or rents) for which there are no immediate or urgent uses;
- when a critical, long-term (beyond 15–20 years) resource shortage is forecast and there are no foreseeable cheaper or more efficient means of financing available;
- as a hedge against economic volatility i.e., an "anchor to windward" in public sector asset management.

GOOD PRACTICES FOR THE ASIAN DEVELOPMENT BANK AND PACIFIC DEVELOPING MEMBER COUNTRIES TO CONSIDER

This study has gathered a number of important principles that can be integrated into a comprehensive set of good practices related to the establishment and management of trust funds (particularly true trust funds). These are put into the checklist of questions below that can guide those considering establishment of a trust fund or those evaluating an existing one. Some of these questions and criteria may be irrelevant for some situations and certain types of funds, and some may appear very simple and self-evident. Moreover, this list is by no means exhaustive.

Does a trust fund support the country's and ADB's strategy? First off, as simple as it sounds, the trust fund should satisfy and fit into the PDMC/ADB development strategy (assuming the PDMC and ADB strategies are aligned).

Is the trust fund idea locally owned? Ensure that the idea for a trust fund is locally owned and arrived upon through an internal needs assessment and consultative process and not prescribed from outside as an easy solution as has happened in at least one case in the Pacific.

Are trust funds well understood? Trust funds are complex mechanisms. Trust fund proponents—PDMC leaders and not just their hired consultants—must be very well versed in the mechanics of asset management, capital markets, forecasting, and other technical issues.[16]

Is the problem addressed long term and is there no better way to address it? Does the critical shortage of resources look to exist beyond a 15 to 20 year horizon? If so, is there absolute certainty that a true trust fund constitutes the most efficient and effective way to address the shortage?

How does the trust fund fit into the larger picture? The trust fund (whether for fiscal stabilization or a more specific purpose) must be planned within the overall public resource management context. Proponents must demonstrate that the fund will fit into the greater public finance and development picture.

Is there a sound fiscal system in place? Trust funds must only be created within a sound, well-managed fiscal management system (whether hosted by the national government or another institution) where governance is robust and transparent. No donor should entrust resources to any country that does not demonstrate fiscal effectiveness.

Can the capitalization be syndicated? Syndicated capitalization reduces risk (from the donor's side) and fosters more collective oversight and management. Trends at development institutions point to a growing use of syndicated trust funds.

Is the outlook soundly quantified? How large must the fund be in 5, 10, 20 years? Trust fund planning must incorporate forecasts and tests of different supply and demand scenarios for fund resources. Failure to do this has left some funds unable to fulfill their purposes.

Can a fund-value target instead of a time target be used? The RMI and FSM Compact trust funds have concrete timelines for discontinuation of US contributions, regardless of whether the trust funds will be able to accomplish the very objectives for which they were established. Where possible, trust funds should follow capitalization targets and not time targets.

Is the fund legalized and formalized? All public trust funds, whatever their purpose, must be formally created through legal and public documentation. Legal documentation (whether legislation or trust fund agreements) must clearly state the terms, objectives, parties and responsibilities, protec-

[16] An excellent book for trustees and other trust fund administrators is The Analysis of Portfolio Management Performance: An Institutional Guide to Assessing and Analyzing Pension Fund, Endowment, Foundation, and Trust Investment Performance by Haight and Morrell (see references).

tions, and other detailed aspects of the trust. Clear investment strategies and distribution policies must also be documented.

Are reputable service providers being used? Trustees must ensure that service providers are reputable and knowledgeable. All candidates must be analyzed very closely. Performance data for at least 10 years should be demanded and scrutinized. (Remember that past performance has never proven to be a good indicator of future success.) Documentation and due diligence are key. Moreover, consultants and advisors should be entirely independent from trustees as well as custodians and money managers.

Are costs being monitored closely? Are management fees, investment expenses and other costs reported by service providers and prudently monitored by trustees and other administrators? Can service providers give the same results at lower costs? Be wary of costs and their effect on overall returns, know what competitors charge, and rebid contracts on a consistent basis.

What is the investment strategy and policy? Prudent trust fund management requires a well thought out investment strategy that is communicated via an official investment policy statement or similar document. An ideal investment policy statement clarifies the overall objectives, asset allocation, risk tolerance, diversification, rebalancing, liquidity, and performance measurement.

Are openness and transparency maintained? Public funds must be open to public scrutiny. Accounting for the trust fund in the overall public finance system and conducting and publicizing annual audits are effective ways to maintain transparency. Annual reports on the performance and status of the fund are also useful.

Is the fund maintaining its real per capita value? True trust funds aim to maintain their real value, but a more prudent measuring stick uses value per capita over time.

7 The Future, the Asian Development Bank's Role, and Conclusions

THE FUTURE AND ADB'S ROLE

Ensuring more effective development processes and reducing poverty are two key priorities of the new ADB Pacific strategy 2005–2009. Clearly, given the right conditions, trust funds can serve as mechanisms for more effective management of development resources. Looking forward, a number of major trends and issues will continue to shape the Pacific, many of which are discussed in Section 4. Two trends stand out, however, with respect to trust funds and development. First, population growth among the PDMCs is expected to remain relatively high. By 2050, the PDMCs will double their populations from the current 8 million to around 16 million. Second, there is converging acknowledgement from both inside and outside the region that the potential for high and sustained economic growth is not great, especially for some of the smaller states. Combined, these two trends foreshadow the emergence of critical resource gaps at all levels: local, national, and regional.

What can ADB do in light of this situation and in relation to trust funds? ADB can help identify (in advance, where possible) and prioritize these resource gaps and can determine whether and where trust funds are most appropriate if at all. ADB should also continue its efforts to assist PDMCs to improve their fiscal systems to ensure that where trust funds are deemed appropriate there is a sound management structure in place to support them. ADB should sharpen its trust fund skills and provide guidance and technical expertise in this area as it is already beginning to do in a number of sectors. The PDMCs are already heading down the trust fund path, so it is critical that the region's premier development partner stays one step ahead of the game. Finally, there is increasing interest in trust funds among all PDMC donors, so ADB can use its unique position to leverage these donors and their resources and can serve as a liaison between them and the PDMCs.

CONCLUSIONS

In summary, trust funds offer a wide range of potential advantages for development as they can:

- provide more reliable, longer-term funding over traditional development assistance;
- provide resources not currently or effectively provided by government, donor or private sources;
- stabilize and preserve windfall resource revenue flows for future use;
- catalyze additional fund raising serving as "magnets" for additional donors;
- allow for sharper, more targeted development (particularly specific-use and thematic funds);
- help to coordinate, harmonize, and centralize foreign assistance from multiple sources;
- enhance economic efficiency by ensuring that resources really to go for the greatest possible use;
- serve as mechanisms for improving governance and transparency (especially when they are managed on a multilateral basis or if resource distribution is decided upon through consultation);
- promote greater self-reliance and responsibility serving as a more hands-off form of foreign assistance;
- allow for more effective sector-wide approaches to development (especially thematic trust funds);
- cost less to administer from the donor's perspective (cheaper than the typical, often bureaucratic annual aid cycles);
- help hedge against economic uncertainties;
- benefit donors' own capital markets (sometimes donors can require that their contributions towards trust funds be invested in their own capital markets);
- improve cooperation between and among governments and local communities.

However, there are also some very real risks and drawbacks with trust funds as they can:

- tie up large amounts of capital (especially front-loaded funds);
- be misused or raided by recipient governments if governance is weak;
- promote complacency on the part of beneficiaries and weaken the

recipient government's drive to reform and take difficult-but-necessary measures;
- be inflexible (especially specific-use funds) and not allow resources to be used for more economically urgent or critical areas;
- spur expansionary fiscal policy;
- give a false sense of economic security;
- incur significant investment losses;
- not have the same "prestige factor" that is often associated with aid-funded projects especially in the case of multidonor trust funds wherein a donor's contribution is diluted and not directly tied to a tangible output like a hospital or school.

Trust funds, therefore, are not a panacea. They carry real potential risks and drawbacks and require careful attention at the planning, establishment, and management stages. Well-managed and strong performing trust funds can go from boom to bust in very short order if fundamental principles are not upheld. Fortunately, as trust funds become more commonly used in the development arena, the basic rules for success are becoming clearer.

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Appendix 1
Additional Data Tables

Mid-Year Population of PDMCs (with projections to 2050): 1950 to 2050

PDMC	*1950*	*2000*	*2010*	*2020*	*2030*	*2040*	*2050*
TOTAL	2,526,593	7,858,335	9,770,017	11,592,557	13,337,561	14,949,630	16,347,123
PNG	1,412,466	4,926,984	6,170,890	7,399,517	8,592,462	9,706,880	10,670,394
East Timor	435,529	846,599	1,152,984	1,385,106	1,594,308	1,778,082	1,942,734
Fiji Islands	287,348	832,494	957,603	1,088,822	1,217,339	1,340,950	1,447,573
Solomon Islands	106,647	466,194	609,682	748,107	881,683	1,005,000	1,110,514
Vanuatu	52,000	189,618	221,120	250,126	275,141	295,133	310,486
Samoa	81,858	179,466	176,265	178,172	175,171	171,143	170,739
FSM	30,715	107,754	107,151	102,378	94,760	85,089	74,296
Tonga	45,744	102,321	122,563	140,932	160,108	176,040	188,340
Kiribati	33,448	91,985	115,287	142,979	173,380	204,326	235,342
RMI	10,904	53,064	65,819	77,846	88,086	96,833	102,761
Cook Islands	14,575	20,407	22,254	23,571	24,354	24,742	24,930
Palau	7,251	18,766	21,557	23,492	25,036	25,971	26,300
Nauru	3,432	11,845	14,259	16,721	18,971	20,932	22,696
Tuvalu	4,676	10,838	12,583	14,788	16,762	18,509	20,018

Source: US Bureau of the Census, International Data Base

Aid Per Capita (Current US$): 1993 to 2002

Country	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Palau	–	11,876	8,372	3,501	2,132	4,692	1,518	2,059	1,709	1,563
RMI	673	1,028	794	1,489	1,259	1,007	1,233	1,101	1,396	1,178
FSM	628	991	723	1,035	865	703	930	861	1,147	915
Timor-Leste	1	0	0	0	1	2	194	316	259	282
Kiribati	206	197	193	156	189	201	237	196	134	220
Tonga	323	363	401	330	282	250	212	188	201	220
Samoa	322	295	263	196	164	216	135	159	248	215
Vanuatu	220	255	272	180	152	218	193	232	157	134
Solomon Islands	162	134	130	113	108	107	97	163	137	59
Fiji Islands	81	54	58	60	57	47	44	36	32	41
Papua New Guinea	72	74	82	82	73	74	43	54	39	38

Note: Nauru, Tuvalu, Cook Islands not shown
– means data not available
Source: World Bank, World Development Indicators Database

GDP Per Capita (Constant 1995 US$): 1993 to 2002

Country	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Fiji Islands	2,426	2,539	2,585	2,645	2,607	2,618	2,829	2,642	2,748	2,840
Kiribati	523	559	575	578	603	611	677	665	663	667
RMI	2,076	2,134	2,148	1,807	1,605	1,645	1,626	1,547	1,543	1,604
FSM	2,052	1,983	1,996	1,896	1,776	1,681	1,656	1,700	1,689	1,675
Palau	5,002	5,052	5,602	5,841	5,976	5,774	5,462	5,523	5,299	5,458
Papua New Guinea	1,048	1,081	1,018	1,068	990	939	985	949	895	870
Samoa	–	1,149	1,215	1,295	1,303	1,318	1,344	1,420	1,491	1,502
Solomon Islands	790	808	843	850	808	797	765	645	565	535
Timor-Leste	–	–	–	–	-	–	-	-	–	-
Tonga	1,479	1,554	1,595	1,589	1,574	1,596	1,628	1,733	1,772	1,800
Vanuatu	1,300	1,390	1,357	1,351	1,336	1,325	1,249	1,254	1,207	1,174

Note: Nauru, Tuvalu, Cook Islands not shown
– means data not available
Source: World Bank, World Development Indicators Database

Official Development Assistance and Official Aid (Current US$ millions): 1993 to 2002

Country	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Fiji Islands	61.43	40.96	44.85	46.94	44.48	36.82	34.88	29.12	25.96	34.07
Kiribati	15.85	15.35	15.41	12.83	15.68	17.31	20.86	17.87	12.43	20.87
RMI	32.29	49.36	38.89	72.94	62.93	50.33	62.90	57.23	74.01	62.42
FSM	64.07	104.07	77.34	112.86	96.03	80.09	107.87	101.62	137.60	111.68
Palau	–	201.89	142.32	63.02	38.38	89.14	28.84	39.13	34.18	31.25
Papua New Guinea	307.27	323.54	371.04	381.42	346.42	361.56	216.04	275.43	203.10	203.28
Samoa	52.41	48.37	43.36	32.46	27.41	36.48	23.02	27.37	43.07	37.76
Solomon Islands	56.39	47.93	47.76	42.71	41.75	42.62	39.69	68.40	58.84	26.31
Timor-Leste	0.42	0.23	0.02	0.08	0.43	1.67	152.82	232.85	194.95	219.77
Tonga	31.35	35.25	38.88	32.02	27.61	24.74	21.19	18.82	20.27	22.27
Vanuatu	35.15	41.74	45.64	31.07	27.16	40.64	37.21	45.80	31.58	27.51

Note: Nauru, Tuvalu, Cook Islands not shown
– means data not available
Source: World Bank, World Development Indicators Database

Appendix 2
Interviews and Consultations

1. Stephen Pollard, Principal Economist, Poverty Reduction, Pacific Department
2. Michaela Prokop, Economist, Pacific Department
3. Robert Siy, Jr., Director, Pacific Department
4. Luigi Bodda, Senior Project Economist, Pacific Operations Division, PARD
5. Giovanni Capannelli, Economist, Pacific Department
6. Andrea Iffland, Senior Economist, Pacific Department
7. Helen Baxter, Social Protection Specialist, Pacific Department
8. Bill Costello, Policy and Regional Cooperation Specialist, Pacific Department
9. Thuy Mellor, Financial Management Specialist, Pacific Department
10. Marcelo Minc, Senior Infrastructure Specialist, Pacific Department
11. Winfried Wicklein, Private Sector Development Specialist, Pacific Department
12. Kowsar Chowdhury, Education Specialist, Pacific Department
13. Robert Guild, Transportation Specialist, Pacific Department
14. Edy Brotoisworo, Senior Environment Specialist, Pacific Department
15. Richard S. Bolt, Economist, Economics and Research Department
16. R. Keith Leonard, Senior Evaluation Specialist, Operations Evaluation Department
17. David Abbott, Private Consultant and Executive Committee Member, Tuvalu Trust Fund
18. Brian Bell, Nimmo-Bell and Company, Ltd., Trust Fund Consultant
19. Anthony Hughes, Private Consultant
20. William Graham, Public Advocate, Marshall Islands Nuclear Claims Tribunal

Appendix 3
Asian Development Bank Administered Trust Funds

As of Spring 2004:

Australian Technical Assistance (TA) Grant
Belgian TA Grant
Canadian Cooperation Fund
Co-Financed TA Grants
Cooperation Fund for National Poverty Reduction Strategies
Cooperation Fund for the Water Sector
Danish TA Grant
DFID United Kingdom TA Grant
Finnish TA Grant
French TA Grant
Gender and Development Cooperation Fund
Governance Cooperation Fund
IBRD (Global Environment Facility)
Italian Cooperation Fund
Japan Fund for Information and Communication Technology
Japan Fund for Poverty Reduction
Japan Fund for Poverty Reduction
Japan Special Fund
Netherlands TA Grant
New Zealand TA Grant
Norwegian TA Grant
Poverty and Environment Fund
Poverty Reduction Cooperation Fund - UKNI
Spanish Cooperation Fund
Swedish TA Grant
Swiss Cooperation Fund
UNDP (Global Environment Facility)
United Kingdom and Ireland Cooperation Fund for TA
World Bank (Global Environment Facility)
(source: www.adb.org)

Appendix 4
World Bank Administered Trust Funds

As of Spring 2004:

Afghanistan Reconstruction
Africa Capacity Building Foundation (ACBF)
Africa Land and Water Initiative
Africa Water Resource Management
Africa Water Resources Management Initiative
African Program for Onchocerciasis Control (APOC)
African Virtual University (AVU)
Agriculture and the WTO
Asia –Africa Trade and Investment Facilitation
Asia Alternative Energy Program (ASTAE)
Asia-Europe Meeting (ASEM)
Bank-Netherlands Partnership (BNPP)
BioCarbon Fund
Capacity Development and Linkages for EIA in Africa
Caspian Environment Program (CEP)
Cities Alliance (CITIES)
Clean Air Initiative
Collaborative Program Livestock Development
Communities and Small-Scale Mining
Consultant Trust Fund (CTF) Program
Consultative Group for International Agricultural Research
Consultative Group to Assist the Poorest (CGAP)
Development Gateway Foundation
Development Market Place
East Timor Transition Support
Energy Sector Management Program (ESMAP)
Environment and Socially Sustainable Development (ESSD)
External Gender Consultative Group
Financial Sector Reform and Strengthening (FIRST)
Flagship Program on Health Sector Reform and Sustainable Financing

Food for Education Evaluation
Global Development Learning Network (GDN)
Global Development Network
Global Environment Facility (GEF)
Global Fund for AIDs, TB and Malaria
Global Fund for Indigenous Peoples
Global Gas Flaring Reductioning Public-Private Partnerships
Global Output-Based Aid Partnership
Global Transport Research
Information for Development (infoDev)
Italian Fund for Culture and Sustainable Development (CFCSD)
Japan Policy and Human Resources Development Fund (PHRD)
Japan Social Development Funds (JSDF)
Japan/World Bank Graduate Scholarship Program (JS/WBGSP)
Japan/World Bank Capacity-Building Partnership
Japan-WB Partnership Program for Building the Capacity of Japanese NGOs
Knowledge for Change Program
Managing the Environment in Sub-Saharan Africa
Mediterranean Environmental Technical Assistance Program (METAP)
Metropolitan Environment Improvement Program (MEIP) in Asia
Millenium Project:Research and Data Activities
Multilateral Fund for the Implementation of the Montreal Protocol (MFMP)/Ozone
Nile Basin Initiative
Norwegian Gender and Development
Norwegian Trust Fund for Environmentally Socially & Sustainable Development
Pacific Facility
Participatory Reforms in Irrigation and Drainage
Pilot Program to Conserve the Brazilian Rain Forest
Post Conflict Partnership Program (PCP)
Poverty Alleviation and Legal Rights (Egypt)
Poverty and Urban Mobility
Poverty Reduction Strategy Support Trust Fund (PRSTF)
Priority Reconstruction Program in Bosnia-Herzegovina
PROFOR – Forest Program
Prototype Carbon Fund (PCF)
ProVention Consortium
Public-Private Infrastructure Advisory Facility
Regional Clean Air Initiative Asian Cities

Regional Environmental Information Management
Robert McNamara Fellowships
Special Program for African Agricultural Research (SPAAR)
Standards and Trade Development Facility
Statistical Capacity Building (TFSCB)
Stop Tuberculosis Partnership
Strengthening LDC Governments Engagements
Sub-Saharan Transport Policy
Supporting Insurance Supervision
Trade Liberalization, Poverty & Environment
Water and Sanitation Program
West Bank and Gaza Program
(source: www.worldbank.org)

Appendix 5
Inter-American Development Bank Administered Trust Funds

As of Spring 2004:

Austria Hurricane Mitch Disaster Assistance and Reconstruction Trust Fund
Austrian Technical Cooperation Trust Fund
Belgian Trust Fund for Consultants
Canadian Technical Assistance Program, Cantap3
Danish Trust Fund for Consulting Services
Finnish Technical Assistance Program
French Technical Cooperation Trust Fund for Consulting Services and Training Activities- Caribbean Contribution
French Technical Cooperation Trust Fund for Consulting Services and Training Activities- Human Resources Contribution
French Technical Cooperation Trust Fund for Consulting Services and Training Activities- Indigenous Contribution
French Technical Cooperation Trust Fund for Consulting Services and Training Activities- Regular Fund
IDB-Canada Trade Fund
IDB-The Netherlands Water Partnership Program
Israeli Consultant Trust Fund
Italian Consulting Firms and Specialized Institutions Trust Fund
Italian Individual Consultant Trust Fund
Italian Special Trust Fund for the Sustainable Development of the Republic of Argentina
Italian Trust Fund for Cultural Heritage and Sustainable Development
Italian Trust Fund for Information and Communication Technology for Development
Italian Trust Fund for Microenterprise Development
Italian Trust Fund for MIF Project Preparation
Japan Special Fund
Japan Special Fund Poverty Reduction Program
Japanese Trust Fund for Consultancy Services
Korean Trust Fund for Technical Cooperation (for Central America)

Korean Trust Fund for Technical Cooperation to the Republic of Colombia
Norwegian Development Fund for Latin America
Norwegian Fund for Microenterprise Development
Norwegian Trust Fund for Consulting Services
Portuguese Technical Cooperation Fund
Social Inclusion Trust Fund
Spanish Framework, General Cooperation Fund
Spanish Fund for Consultants, ICEX
Swedish Framework Sida/IDB Partnership
Swedish Trust Fund for the financing of Small Projects
Swiss Technical Cooperation Trust Fund for Consulting Services and Training Activities
The Global Environment Facility
The Netherlands-IDB Partnership Program in Environment
The United Kingdom Technical Cooperation Trust Fund for Consulting Services
UK CABILICA Trust Fund and the Program on Capacity Building for Local Development Institutions in Central America
USDOE Hemispheric Sustainable Energy Trust Fund
USTDA Evergreen Fund for Technical Assistance
(source: www.iadb.org)

Appendix 6
United States Agency for International Development Administered Trust Funds

As of late 1990s:

Argentina EAI Fund
Bangladesh: International Centre for Diarrheal Disease Research
Bolivia EAI Fund
Chile EAI Fund
Colombia EAI Fund
Colombia: PROFAMILIA
Costa Rica/USA Foundation
Costa Rica: Agricultural College of the Humid Tropical Region
Costa Rica: Arias Foundation
Costa Rica: Foundation for the Development of the
Central Volcanic Cordillera
Costa Rica: FUNDATROPICOS
Costa Rican Export Promotion Fund
Dominican Republic: Agricultural Development Foundation
Dominican Republic: Junta Agroempresarial Dominicana
Dominican Republic: Pontificia Universidad Catolica Madre y Maestra
Dominican Republic: Superior Institute of Agriculture
Ecuador: Foundation for Agricultural Development
Ecuador: Institute for Agricultural Strategies
El Salvador EAI Fund
Ghana Community Enterprise Development and Investment Trust
Honduran Agricultural Research Foundation
Honduran Environmental Trust Fund
Honduras: CADERH
Honduras: Pan-American Agricultural School
Indonesia Biodiversity Foundation
Israel: U.S.-Israeli Binational Foundations
Jamaica National Parks Trust Fund
Jamaica: Environmental Foundation of Jamaica

Korea Development Institute and Korean Institute for Science and Technology
Madagascar National Environmental Endowment Foundation
Mexico Nature Conservation Fund
Nepal National Social Welfare Association
Panama: Ecological Trust Fund
Philippines: Foundation for the Philippine Environment
Portugal: Luso-American Development Foundation
Region
Swaziland: Family Life Association of Swaziland
Swaziland: Swazi Business Growth Trust
Uruguay EAI Fund
(source: USAID 1996)

Appendix 7
United Nations Development Programme Administered Trust Funds

As of mid-2004:

Democratic Governance, including Project Summaries
Poverty Reduction
Energy
Environment
Information and Communications Technology
HIV/AIDS
Gender
Crisis Prevention and Recovery
(source: www.undp.org)

Appendix 8
National Environmental Trust Funds

As of 2001:

ARGENTINA Fondo Iniciativa de las Américas
BELIZEProtected Areas Conservation Trust
Bhutan Trust Fund for Environmental Conservation
BOLIVIA Enterprise of the Americas Fund
Brazil Fundo Nacional de Meio Ambiente
Chile Fondo de las Américas
China Local Environmental Funds
Colombia Corporación ECOFONDO
Colombia National Environmental Fund
COSTA RICA Centro Agricola Siquirres
COSTA RICA Fondo Nacional de Financiamiento Forestal (FONAFIFO)
COSTA RICA Foundation "Funde-cooperación" for Sustainable Development
COSTA RICA Fundacion de Parques Nacionales
COSTA RICA FUNDECOR (Fundacion para el Desarrollo de la Cordilera Volcanica Central)
DOMINICAN REPUBLIC Fondo Pro Naturaleza (PRONATURA)
ECUADOR Fondo Ambiental Nacional
EL SALVADORFondo Iniciativa para las Américas
Fideicomiso para la Conservación en Guatemala (FCG)
Fiji Heritage Foundation (FHF)
FOGUAMA (Fondo Guatemalteco del
Fondo Ambiental de EI Salvador
Fondo Canada - Nicaragua para el Manéjo del Medio Ambiente
Fondo de las Américas – Uruguay
Fondo Mexicano para la Conservacion de la Naturaleza (FMCN)
Fondo Nacional para la Conservacion de la Naturaleza (FONACON)
Foundation for the Philippine Environment (FPE)
Fundación Hondurena de Ambiente y Desarrollo

Fundación para el Desarrollo del Sistema Nacional de Areas
Protegidas de Bolivia
Fundo Brasileiro para a Biodiversidade
Indonesian Biodiversity Foundation (IBF)
Jamaica National Park Trust Fund
MADAGASCAR Tany Meva - The Malagasy Environment Foundation
MAURITIUS National Environmental Fund
Medio Ambiente)
Mongolia Environmental Trust Fund
Namibia Nature Foundation
National Trust Fund for Protected Areas (FONANPE–Peru)
Nicaragua FONANIC
PANAMA Fundación para la Conservación de los Recursos Naturales
(NATURA)
PERU Fondo Nacional para las Areas Naturales Protegidas por el Estado
Philippine Foundation for Sustainable Societies, Inc.
PNG Conservation Trust Fund
Seychelles Island Foundation
SOUTH AFRICA The Green Trust
SOUTHERN AFRICA Peace Parks Foundation
Suriname Conservation Fund
Thailand Environment Fund
The Bahamas National Trust
The Environmental Foundation of Jamaica (EFJ)
The Ghana Heritage Conservation Trust
Turks and Caicos Conservation Fund
UGANDA Mgahinga and Bwindi Impenetrable Forest
Conservation Trust (MBIFCT)
West Africa Rural Foundation (WARF)
Wildlife Trust of Sri Lanka (WLTSL)
(source: Klug 2001)

Appendix 9
Terms of Reference for Analysis

PACIFIC DEPARTMENT (PARD)

PACIFIC OPERATIONS DIVISION (PAHQ)

PROJECT TITLE: PROJECT F
"Trust Funds in the Pacific, their Role and Future"

SCOPE OF ASSIGNMENT:
Research ADB records, review other relevant literature, and interview relevant staff.

The review will include an assessment of the following:
- The performance of the National and Outer Island Trust Funds of FSM, Kiribati, RMI, and Tuvalu
- A review of other Trust Funds in the Pacific region (Tonga – Passports, PNG – Mineral stabilization)
- The role of Trust Funds most especially as this relates to fiscal policy and other economic development policy
- A brief review of other Trust Funds in support of ecology, environment, conservation, others
- The future of government Trust Funds in Small Island, Pacific Economies
- Best practices in terms of ownership, management, and other operation of Pacific Trust Funds

FINAL OUTPUTS:
Report and Brown Bag seminar focusing on recommendations for future ADB assistance

QUALIFICATIONS:
Students in Economics and/or MBA; must have knowledge or strong interest in Pacific or Small Island Economies; knowledge of fiscal situation of small island economies.

PLACE OF ASSIGNMENT:
Pacific Department (PARD), Pacific Operations Division (PAHQ)
ADB Headquarters, Manila, Philippines

SPONSORS:
Mr. Stephen J. Pollard, Principal Economist, PAHQ
(Principal Sponsor)
Ms. Michaela Prokop, Economist, PAHQ
(Assistant Sponsor)

Appendix 10
Summary Matrix of Pacific Developing Member Country Trust Funds

Summary Matrix of Selected PDMC Trust Funds

Country	Fund Name	Year	Capital Source(s)	Capitalization	Primary	Time	Capital ($)
Kiribati	Revenue Equalisation Reserve Fund	1956	Phosphate mining tax revenue and other contributions	Build up of phosphate tax revenue and other contributions	Fiscal support and stabilization	Perpetual	A $0.556m
Tuvalu	Tuvalu Trust Fund	1987	Contributions from UK, New Zealand, Australia, Tuvalu, Japan and Korea, and subsequent contributions from other sources (".tv" and fishing license fees)	Front-loaded multilateral contributions along with subsequent contributions	Fiscal support and stabilization	Perpetual	A $27.1m
Palau	Palau Compact of Free Association Trust Fund	1995	US transfers under Compact of Free Association	One US$66m front-loaded contribution in 1995 with a follow-up $4m contribution in 1997.	Fiscal support and stabilization	Technically, designed as sinking fund (with 50 year horizon)	US $66m
RMI	RMI Compact of Free Association Trust Fund	2004	US transfers under Compact of Free Association, assets from ealier MIITF (est. 1999), other contributions	US$25m to be transferred from MIITF; $7m initial US contribution to grow by $.5m increments until 2023; other contributions	Fiscal support and stabilization	Perpetual	na

Summary Matrix of Selected PDMC Trust Funds (continued)

Country	Fund Name	Year Established	Capital Source(s)	Capitalization	Primary	Time Frame	Capital ($) at Inception
FSM	FSM Compact of Free Association Trust Fund	2004	Initial FSM contribution plus US transfers under Compact of Free Association	FSM $30m plus US transfers of $16m for 2004-06 and increasing by $.8m every year there-after through 2023.	Fiscal support and stabilization	Perpetual	na
Nauru	Nauru Phosphate Royalties Trust (Long-term Invest. Fund, Land Owners Royalty Trust Fund, Housing Fund, Rehab Fund)	1968	Dividends and taxes on phosphate mining activities	build up	Post-mining fiscal support, income for landowners, housing projects, rehabilitation of land	Perpetual	na
Tonga	Tonga Trust Fund	1988	Revenue from passport scheme and satellite space leasing	build up	Fiscal support, projects	Perpetual	na
Tuvalu	Falekaupule Fund	1999	National government, local governments, ADB	Initial contribu-tions totaling $9.6m: $4.8 from national govern-ment, $4 from ADB, and $.8 from local governments	Outer island development	Perpetual	A$9.6m
RMI	RMI Nuclear Claims Fund	1986	US lump sum transfer under Compact of Free Association (section 177)	Lump-sum transfer of $150 m	Compensations for nuclear testing in 1940s and 1950s	Perpetual	US$150