

# **Trust Fund for the People of the Federated States of Micronesia**

## **Annual Report Fiscal Year 2007 April 2008**

This report covers the Fiscal Year that began October 1, 2006 and ended September 30, 2007. Information regarding the quarter from October 1, 2007, to December 31, 2007, also appears below, as available.

### **Performance of Trust Fund's Assets in Fiscal Year (FY) 2007: (see the attached Executive Summary and Performance Summary)**

The market value of the Trust Fund's net assets stood at \$86,528,461 as of September 30, 2006, and at \$122,639,462 on September 30, 2007. The United States contribution of \$17,688,605 on October 6, 2006, and investment appreciation and earnings of \$19,129,858 account for the increase. These earnings represented a total return on assets for the Fiscal Year of 17.4 percent.

### **Organization:**

Pursuant to the provisions of the Compact of Free Association and its subsidiary Trust Fund Agreement, the Trust Fund for the People of the Federated States of Micronesia (FSM) was incorporated in Washington, D.C., on August 17, 2004. The Trust Fund Agreement established the organization and structure of the Trust Fund, including a Joint Trust Fund Committee (TFC), which exercises all the powers of the Trust Fund.

The Trust Fund Agreement provides for the TFC to be composed of three members who represent the United States, and two members who represent the FSM. Members of the Trust Fund Committee as of September 30, 2007, were the following:

David B. Cohen, Chairman	United States
C. Steven McGann	United States
William R. Steiger, Ph.D.	United States
Evelyn Adolph	FSM
Epel K. Ilon	FSM

**Contributions:**

The following is a history of contributions made to the Fund's A Account:  
(The second column shows fiscal year of payment obligation.)

<u>Date</u>	<u>for FY</u>	<u>Amount</u>	<u>Contributor</u>
October 1, 2004	FY2004	\$30,258,383	FSM
October 5, 2004	FY2004	16,000,000	United States
October 5, 2004	FY2005	16,188,000	United States
October 6, 2005	FY2006	16,441,694	United States
October 6, 2006	FY2007	17,688,605	United States
Contributions through FY 2007:		\$96,576,682	
October 6, 2007	FY2008	\$18,995,680	United States
Contributions through calendar year 2007:		\$115,572,362	

**Implementation of the Asset Allocation Plan:**

During FY 2007, the TFC completed Step Two of the approved Mercer Investment Allocation Plan.

On August 30, 2006, the TFC approved two private-equity managers and two international-equity managers recommended from a list provided by Mercer and reviewed by a sub-committee of the TFC. The TFC funded or partially funded these accounts during FY 2007.

**Private-Equity Managers:**

-HarbourVest Partners, including four private-equity funds with a total commitment of \$15 million, of which the Trust Fund paid \$2.3 million through capital calls throughout FY 2007.

-Portfolio Advisors, to which the Trust Fund committed \$10 million, of which the Trust Fund paid \$3.5 million in response to capital calls during FY 2007.

**International-Equity Managers:**

-The TFC funded Grantham Mayo Otterloo (GMO) International Opportunities Equity Fund with \$24 million on October 23, 2006.

-The TFC funded Newton Capital Management International Equity Fund with \$6 million on November 6, 2006.

The TFC completed the last part of Step Two with the engagement of Aberdeen Asset Management's Core Plus Fixed-Income Fund. The TFC selected Aberdeen as fixed-income manager in December 2006, and funded this account with \$17 million on June 7, 2007.

**Money Managers, Balances and Fees:**

Following are the year-end balances managed by each money manager, and the fees paid to each during FY 2006:

	<u>Balance</u>	<u>Fees</u>
<b>Large-Cap Equity:</b>	(thousand)	
State Street Global Advisors, Russell 3000 Index Fund.	\$60,106	\$29,790
<b>International Equity:</b>		
Grantham, Mayo, Van Otterloo (GMO): International Equity Allocation Portfolio	\$20,995	\$174,474
Newton Investment Management, EAFE Plus International Portfolio	\$7,789	\$69,896
<b>Emerging-Markets Equity:</b>		
Aberdeen Fund Management, Core Plus Fixed-Income Portfolio	\$17,383	\$20,372
<b>Private Equity:</b> (note: fees are based on total commitment)		
Portfolio Advisors, PAPEF IV Private-Equity Fund	\$3,647	\$87,500
HarbourVest Partners, VIII Buyout Fund	\$787	\$51,656
VIII Mezzanine and Distressed Debt Fund	\$127	
VIII Venture Fund	\$315	
International Private-Equity Partners V	\$1,121	
<u>Total Money-Manager Fees, FY 2007:</u>		<u>\$433,687</u>

**Service Provider Fees:**

JP Morgan Chase, as Trustee, received \$11,546 in fees during Fiscal Year 2007. JP Morgan Chase charges one basis point (.01 percent) on balances of up to \$200 million, plus transaction fees.

Mercer Investment Consulting, as Investment Adviser, received \$94,855 in Fiscal Year 2007. Mercer charges \$125,000 annually, billed quarterly.

DLA Piper, Counsel, received a total of \$2,438 during Fiscal Year 2007. The TFC paid most of the fees billed in FY 2007 in FY 2008.

Beard Miller Company, Auditor, received \$22,166 during FY 2007.

The Trust Fund paid no general administrative fees in FY 2007; however, in FY 2008, under its contract with Richard W. Miller as Executive Administrator, it may incur up to \$90,000 in hourly fees.<sup>1</sup>

Total service fees, FY 2007: \$131,000

The Trust Fund’s total expenditure in FY 2007 for money managers and services was approximately \$564,700. This represented 0.46 percent of the Trust Fund’s end-year assets of \$122,639,462. Expenditures will increase in FY 2008, because the TFC engaged most money managers for only part of FY 2007, newly engaged managers have higher fees, some service fees were postponed from FY 2007 and the TFC has added additional service providers.

**Engagement of Auditor and Executive Administrator:**

A joint subcommittee of the Trust Funds on behalf of the people of the FSM and Republic of the Marshall Island in December 2006 recommended an auditor for the Trust Funds after interviewing three finalists. On March 8, 2007, after the TFC reissued the RFP to obtain additional responses, it approved the selection of Beard Miller Company (BMC) to audit the fund for Fiscal Years 2004 to 2006, and 2007.

After passing a resolution, the TFC conducted a search during August 2007 for an Executive Administrator for the Trust Fund. As a result of the search, the Chairman of the TFC signed a contract on September 19, 2007, between the Trust Fund and Richard W. Miller. The duties of the Executive Administrator are to assist the Chairman in his capacity as Chairman in the Administration of the Trust Fund for the People of the Federated States of Micronesia and in the operations of the Trust Fund Committee.

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<sup>1</sup> The U. S. Department of the Interior estimates its contribution--mainly in staff time, but also including equipment use and incidental expenses--at about \$100,000 in FY 2007.

**Reports on Trust Fund Investment and Performance:**

The Trustee, JPMorgan Chase, provides monthly reports on the Trust Fund's Assets. The Trust Fund's Investment Advisor, Mercer, also issues quarterly reports on performance. An Executive Summary and a Performance Summary for Fiscal Year 2007 are attached to this *Annual Report*.