



Highlights of [GAO-07-1258T](#), a testimony to the Committee on Energy and Natural Resources, U.S. Senate

## Why GAO Did This Study

In 2003, the U.S. government extended its economic assistance to the Republic of the Marshall Islands (RMI) through an Amended Compact of Free Association. From 2004 to 2023, the United States will provide an estimated \$1.5 billion to the RMI, with annually decreasing grants as well as increasing contributions to a trust fund. The assistance, targeting six sectors, is aimed at assisting the country's efforts to promote economic advancement and budgetary self-reliance. The trust fund is to be invested and provide income for the RMI after compact grants end. The Department of the Interior (Interior) administers and oversees this assistance. Drawing on prior GAO reports (GAO-05-633, GAO-06-590, GAO-07-163, GAO-07-513, GAO-07-514R), this testimony discusses (1) the RMI's economic prospects, (2) implementation of the amended compact to meet long-term goals, and (3) potential trust fund earnings. In conducting its prior work, GAO visited the RMI, reviewed reports, interviewed officials and experts, and used a simulation model to project the trust fund's income.

Prior GAO reports recommended, among other things, that Interior work with the RMI to address lack of progress in implementing reforms; plan for declining grants; reliably measure progress; and ensure timely reporting on the fund's likely status as a source of revenue after 2023. Interior agreed with GAO's recommendations.

To view the full product, including the scope and methodology, click on [GAO-07-1258T](#). For more information, contact David Gootnick at (202) 512-3149 or [gootnickd@gao.gov](mailto:gootnickd@gao.gov).

## COMPACT OF FREE ASSOCIATION

### Implementation Activities Have Progressed, but the Marshall Islands Faces Challenges to Achieving Long-Term Compact Goals

#### What GAO Found

The RMI has limited prospects for achieving its long-term development goals and has not enacted policy reforms needed to achieve economic growth. The RMI economy depends on public sector spending of foreign assistance rather than on private sector or remittance income. At the same time, the two private sector industries identified as having growth potential—fisheries and tourism—face significant barriers to expansion because of a costly business environment. RMI emigrants also lack marketable skills needed to increase revenue from remittances. Despite declining grants under the compact, RMI progress in implementing key policy reforms to improve the private sector environment, such as tax or land reform, has been slow. In August 2006, the RMI's compact management committee began to address the country's slow progress in implementing reforms.

Although the RMI has made progress in implementing compact assistance, it faces several challenges in allocating and using this assistance to support its long-term development goals. RMI grant allocations have reflected compact priorities by targeting health, education, and infrastructure. However, political disagreement over land use in Kwajalein Atoll, where the United States has a missile testing facility, and over management of public entities has negatively affected infrastructure projects. The RMI also has not planned for long-term sustainability of services that takes into account declining compact assistance. Inadequate baseline data and incomplete performance reports have further limited the RMI's ability to adequately measure progress. Although single-audit reporting has been timely, insufficient staff and skills have limited the RMI's ability to monitor day-to-day sector grant operations. Interior's Office of Insular Affairs (OIA) has conducted administrative oversight of the sector grants but has been constrained by competing oversight priorities.

The RMI trust fund may not provide sustainable income for the country after compact grants end. Market volatility and the choice of investment strategy could cause the RMI trust fund balance to vary widely, and there is increasing probability that in some years the trust fund will not reach the maximum disbursement level allowed—an amount equal to the inflation-adjusted compact grants in 2023—or be able to disburse any income. In addition, although the RMI has supplemented its trust fund income with a contribution from Taiwan, other sources of income are uncertain or entail risk. Trust fund management processes have also been problematic; as of June 2007, the RMI trust fund committee had not appointed an independent auditor or a money manager to invest the fund according to the proposed investment strategy.