

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND****STATEMENT OF FINANCIAL POSITION****31 December 2008 and 2007**

Expressed in Thousands of United States Dollars (Note B)

	2008	2007
<b>ASSETS</b>		
DUE FROM BANKS (Note B)	\$ 304	\$ 603
INVESTMENTS (Notes B, C, and D)		
Time deposits	—	6,749
SECURITIES PURCHASED UNDER RESALE ARRANGEMENT (Notes B, C, and D)	10,405	1,157
PROPERTY, FURNITURE, AND EQUIPMENT (Notes B and E)		
One-time Establishment Cost and Furnitures	\$3,398	\$2,733
Less—allowance for depreciation	3,398	2,733
Leased Property	243	196
Less—allowance for depreciation	146	78
DUE FROM CONTRIBUTORS (Note F)	7,759	11,716
OTHER ASSETS	2,512	2,024
<b>TOTAL</b>	<b>\$21,077</b>	<b>\$22,367</b>
<b>LIABILITIES AND UNCOMMITTED BALANCES</b>		
ACCOUNTS PAYABLE AND OTHER LIABILITIES (Notes B, E, and H)	\$ 5,354	\$ 4,075
UNCOMMITTED BALANCES (ADBISF-2)		
Unrestricted net assets	15,723	18,292
<b>TOTAL</b>	<b>\$21,077</b>	<b>\$22,367</b>

The accompanying notes are an integral part of these financial statements (ADBISF-4)

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND****STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS****For the Years Ended 31 December 2008 and 2007**

Expressed in Thousands of United States Dollars (Note B)

	<u>2008</u>	<u>2007</u>
CHANGES IN UNRESTRICTED NET ASSETS		
CONTRIBUTIONS (Notes B and F)	\$ 7,759	\$ 11,716
REVENUE		
Income from investments (Notes B and C)	85	71
Income from other sources (Note G)	256	7
Total	<u>8,100</u>	<u>11,794</u>
EXPENSES		
Administrative expenses	9,743	8,782
Program expenses	3,814	2,388
Total	<u>13,557</u>	<u>11,170</u>
CONTRIBUTIONS AND REVENUE (LESS THAN) IN EXCESS OF EXPENSES	(5,457)	624
EXCHANGE LOSSES—NET	(159)	(93)
TRANSLATION ADJUSTMENTS (Note B)	3,337	730
EFFECT OF FASB STATEMENT NO. 158 (Note I)	<u>(290)</u>	<u>(377)</u>
(DECREASE) INCREASE IN UNRESTRICTED NET ASSETS	(2,569)	884
NET ASSETS AT BEGINNING OF YEAR	18,292	17,408
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 15,723</b>	<b>\$ 18,292</b>

The accompanying notes are an integral part of these financial statements (ADBISF-4).

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND****STATEMENT OF CASH FLOWS****For the Years Ended 31 December 2008 and 2007**

Expressed in Thousands of United States Dollars (Note B)

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Contributions received	\$ 12,163	\$ 11,144
Interest on investments received	87	70
Expenses paid	(13,009)	(10,839)
Others—net	97	(86)
Net Cash (Used in) Provided by Operating Activities	<u>(662)</u>	<u>289</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Maturities of investments	220,580	155,105
Purchases of investments	(212,945)	(156,267)
Net (payments for) receipts from securities under resale arrangement	(7,406)	511
Net Cash Provided by (Used in) Investing Activities	<u>229</u>	<u>(651)</u>
Effect of Exchange Rate Changes on Due from Banks	<u>134</u>	<u>269</u>
Net Decrease in Due from Banks	(299)	(93)
Due from Banks at Beginning of Year	<u>603</u>	<u>696</u>
Due from Banks at End of Year	<u>\$ 304</u>	<u>\$ 603</u>
RECONCILIATION OF (DECREASE) INCREASE IN UNRESTRICTED NET ASSETS TO NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES:		
(Decrease) Increase in unrestricted net assets (ADBISF-2)	\$ (2,569)	\$ 884
Adjustments to reconcile (decrease) increase in unrestricted net assets to net cash (used in) provided by operating activities:		
Depreciation	48	177
Change in due from contributors	4,404	(572)
Change in other assets	(488)	(233)
Change in accounts payable and other liabilities	1,279	808
Translation adjustments	(3,337)	(730)
Others—net	1	(45)
Net Cash (Used in) Provided by Operating Activities	<u>\$ (662)</u>	<u>\$ 289</u>

The accompanying notes are an integral part of these financial statements (ADBISF-4).

## ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND

### NOTES TO FINANCIAL STATEMENTS

31 December 2008 and 2007

#### NOTE A—NATURE OF OPERATIONS

In 1996, the Asian Development Bank (ADB) approved the establishment of the Asian Development Bank Institute (the Institute) in Tokyo, Japan as a subsidiary body of ADB. The Institute commenced its operations upon the receipt of the first funds from Japan on 24 March 1997, and it was inaugurated on 10 December 1997. The Institute's funds may consist of voluntary contributions, donations, and grants from ADB member countries, non-government organizations, and foundations. The objectives of the Institute, as defined under its Statute, are the identification of effective development strategies and capacity improvement for sound development management in developing member countries.

#### NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### *Presentation of the Financial Statements*

The financial statements of the Institute are presented on the basis of those for not-for-profit organizations.

The Institute reports donor's contributed cash and other assets as unrestricted support as these are made available to the Institute without conditions other than for the purposes of pursuing the objectives of the Institute.

##### *Functional Currency and Reporting Currency*

The functional currency of the Institute is the Japanese yen. The reporting currency is the United States dollar.

##### *Translation of Currencies*

Assets, liabilities, and uncommitted balances are translated from the functional currency to the reporting currency at the applicable rates of exchange at the end of a reporting period. Commitments included in the financial statements during the year are recognized at the applicable exchange rates as of the respective dates of commitment. Revenue and expense amounts in currency other than the United States dollar are translated for each semi-monthly period generally at the applicable rates of exchange at the beginning of each period; such practice approximates the application of average rates in effect during the period. Translation adjustments are ac-

counted for as exchange gains or losses and are credited or charged to operations.

##### *Investments*

All investment securities held by the Institute are reported at estimated fair value which represents their fair market value. Realized and unrealized gains and losses are included in revenue. Time deposits are reported at cost which is a reasonable estimate of fair value.

##### *Securities Purchased Under Resale Arrangements*

ADBI accounts for transfer of financial assets in accordance with FAS 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – a replacement of FAS 125." In general, transfers are accounted for as sales under FAS 140 when control over the transferred assets has been relinquished. Otherwise, the transfers are accounted for as repurchase/resale arrangements and collateralized financing arrangements. Securities purchased under resale arrangement are recorded as assets and reported at estimated fair value, while securities received are not recorded as liabilities and are not re-pledged.

##### *Property, Furniture, and Equipment*

Property, furniture, and equipment are stated at cost and depreciated over their estimated useful lives using the straight-line method. Maintenance, repairs and minor betterments are charged to expense.

The Institute distinguishes between capital leases and operating leases based on the objective of the expenditure. Expenditures amounting to more than \$30,000 for a single asset or a combination of assets forming an integral part of a separate asset are capitalized.

##### *Contributions*

Contributions from donors are included in the financial statements from the date committed.

##### *Accounting Estimates*

The preparation of the financial statements in conformity with generally accepted accounting principles requires

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Management to make estimates and assumptions that affect the reported amounts of assets and liabilities as at the end of the year and the reported amounts of revenue and expenses during the year. Actual results could differ from those estimates.

*Accounting and Reporting Developments*

In December 2008, the FASB issued FASB Staff Position (FSP) FAS 132(R)-1, which amends 132(R) to require more detailed disclosures about employers' plan assets, including employers' investment strategies, major categories of plan assets, concentration of risk within plan assets, and valuation techniques used to measure the fair value of plan assets. This aims to address financial statement users' concerns "about the lack of transparency surrounding the types of assets and associated risks in an employer's defined benefit pension or other postretirement plan and events in the economy and markets that could have a significant effect on the value of the plan assets." An entity must provide the FSP's disclosures in financial statements for fiscal years ending after 15 December 2009.

*Statement of Cash Flows*

For the purposes of the Statement of Cash Flows, the Institute considers that its cash and cash equivalents are limited to "DUE FROM BANKS."

*Reclassification*

Certain non-material reclassifications of prior year's amounts and information have been made to conform to the current year's presentation.

**NOTE C—INVESTMENTS**

The main investment management objective is to maintain security and liquidity. Subject to these parameters, ADB administers the Institute's investments and seeks the highest possible return on its investments. Investments are governed by the Investment Authority approved by the Board of Directors in 1999, and reviewed in 2006. The review endorsed a portfolio approach that is largely consistent with the 1999 approach.

The investment portfolio was composed wholly of investments denominated in Japanese yen as of 31

December 2007. All such investments were due within one year. The total investment income reported as of 31 December 2008 consisted of interest income earned during the year.

The annualized rate of return on the average investments held during the year including receivable for securities purchased under resale arrangement, based on the portfolio held at the beginning and end of each month was 0.58% (0.58% - 2007).

**NOTE D—FAIR VALUE MEASUREMENTS**

FAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability at measurement date (exit price) in an orderly transaction among willing participants with an assumption that the transaction takes place in the entity's principal market, the most advantageous market for the asset or liability. The most advantageous market is the market where the sale of the asset or transfer of liability would maximize the amount received for the asset or minimize the amount paid to transfer the liability. The fair value measurement is not adjusted for transaction cost.

FAS 157 also establishes a fair value hierarchy that gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1), next priority to observable market inputs or market corroborated data (Level 2), and the lowest priority to unobservable inputs without market corroborated data (Level 3). FAS 157 requires the fair value measurement to maximize the use of market observable inputs.

The following guidelines are applied in determining the fair values of financial instruments:

*Investments and securities purchased under resale arrangements*

Readily marketable investments are fair valued using active market quotes in Level 1 category. Level 2 category includes investments and securities purchased under resale arrangements which are fair valued with significant other market observable inputs.

The fair value of the following financial assets of ADBISF as of 31 December 2008 were reported based on the following:

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	31 December 2008	Fair Value Measurements		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
Securities purchased under resale arrangement	\$10,405,000	\$ –	\$10,405,000	\$ –

See Note B for discussions relating to investments and securities purchased under resale arrangements. In all other cases, the carrying amounts of ADBISF's assets, liabilities, and uncommitted balances are considered to approximate fair values for all significant financial instruments.

**NOTE E—LEASED ASSETS**

On 6 January 2006, the Institute concluded an agreement regarding the lease of a server, which requires ADBI to pay a total amount of \$205,000 over the period of 60 months for the lease of the server.

The following is a schedule by years of future minimum lease payments under capital lease together with present value of the net minimum lease payment as of 31 December 2008:

Year ending 31 December	
2009	\$ 53,000
2010	53,000
Total minimum lease payment	106,000
Less: Amount representing interest	3,000
Present value of net minimum lease payments	<u>\$103,000</u>

**NOTE F—CONTRIBUTIONS**

In 2008, the Government of Japan committed its 13<sup>th</sup> contribution to ADBI amounting to ¥700,900,000 (\$7,759,000 equivalent), which was transferred to the Fund on 15 January 2009. The amount contributed was reported in 31 December 2008 balance sheet as “Due from Contributors.”

**NOTE G—INCOME FROM OTHER SOURCES**

Income from other sources in 2008 primarily consists of sublease rental income of \$171,000, received according to a space sharing agreement with the Japanese Representative Office of ADB. The transactions with ADB were made in the ordinary course of business and were negotiated at arm's length.

**NOTE H—DUE TO ADB**

Accounts payable and other liabilities include amounts due to ADB of \$847,000 and \$341,000 at 31 December 2008 and 2007, respectively. The payable results from transactions in the normal course of business.

**NOTE I—STAFF RETIREMENT PLAN AND POSTRETIREMENT MEDICAL BENEFITS***Staff Retirement Plan*

The Institute participates in the contributory defined benefit Staff Retirement Plan (the Plan) of ADB. Every employee, as defined under the Plan, shall, as a condition of service, become a participant from the first day of service, provided that at such a date, the employee has not reached the normal retirement age of 60. Retirement benefits are based on length of service and highest average remuneration during two years of eligible service. The Plan assets are segregated and are not included in the accompanying Balance Sheet. The costs of administering the Plan are absorbed by ADB, except for fees paid to the investment managers and related charges, including custodian fees, which are borne by the Plan.

Participants hired on or before 30 September 2006 are required to contribute 9 1/3% of their salary to the Plan while those hired after that date do not anymore

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contribute to the plan. Participants may also make additional voluntary contributions. ADBI's contribution is determined at a rate sufficient to cover that part of the costs of the Plan not covered by the participants' contributions.

*Expected Contributions*

The expected amount of contributions to the Plan for 2009, based on the Institute's contribution rate for the coming year of 19%, and the participants' mandatory contribution are \$221,000 and \$62,000, respectively (2007 - \$158,000 and \$58,000).

*Investment Strategy*

Contributions in excess of current benefits payments are invested in international financial markets and in a variety of investment vehicles. The Plan employs nine external asset managers and one global custodian who function within the guidelines established by the Plan's

Investment Committee. The investment of these assets, over the long term, is expected to produce higher returns than short-term investments. The investment policy incorporates the Plan's package of desired investment return, and tolerance for risk, taking into account the nature and duration of the Plan's liabilities. The Plan's assets are diversified among different markets and different asset classes. The use of derivatives for speculation, leverage or taking risks is prohibited. Selected derivatives are used for hedging and transactional efficiency purposes.

The Plan's investment policy is periodically reviewed and revised to reflect the best interest of the Plan's participants and beneficiaries. The current policy, adopted in January 2003, specifies an asset-mix structure of 70% of assets in equities and 30% in fixed income securities.

At present, investments of the Plan's assets are divided into three categories: US equity, Non-US equity, and US fixed income.

As of 31 December 2008 and 2007, the breakdown of the fair value of plan assets held is as follows:

	2008		2007	
	Amount	Percentage	Amount	Percentage
Equity Securities				
US	\$ 770,000		\$1,139,000	
Non-US	518,000		856,000	
	1,288,000	58.6%	1,995,000	73.0%
Fixed income securities	872,000	39.7	762,000	27.9
Other Assets (Liabilities)—net	38,000	1.7	(24,000)	(0.9)
Total	\$2,198,000	100.0%	\$2,733,000	100.0%

All investments, excluding time deposits, are valued using market prices. Time deposits are reported at cost which is the reasonable estimate of the fair value. Fixed income securities include US government and government guaranteed obligations, corporate bonds and time deposits. Other assets include forward exchange contracts in various foreign currencies transacted to hedge currency exposure in the investment portfolio, which are reported at fair value.

For the year ended 31 December 2008 the net return on the Plan assets was -29.5% (6.0% – 2007). ADB expects the long-term rate of return on the assets to be 8%.

*Assumptions*

The assumed overall rate of return takes into account long-term return expectations of the underlying asset classes within the investment portfolio mix, and the expected duration of the Plan's liabilities. Return expectations are forward looking and, in general, not much weight is given to short-term experience. Unless there is a drastic change in investment policy or market environment, the assumed investment return of 8% on the Plan's assets is expected to remain broadly the same, year to year.

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**Postretirement Medical Benefits Plan**

The Institute participates in the cost-sharing plan of ADB for retirees' medical insurance premiums. Under the plan, the Institute is obligated to pay 75% of the Group Medical Insurance Plan premiums for retirees and their eligible dependents who elected to participate. The cost-sharing plan is currently unfunded.

Generally accepted accounting principles require an actuarially determined assessment of the periodic cost of postretirement medical benefits.

The following table sets forth the pension and postretirement benefits at 31 December 2008 and 31 December 2007:

	Pension Benefits		Postretirement Medical Benefits	
	2008	2007	2008	2007
Change in benefit obligation:				
Projected benefit obligation at beginning of year	\$ 4,960,000	\$ 4,269,000	\$ 98,000	\$ 231,000
Service cost	163,000	126,000	20,000	14,000
Interest cost	305,000	258,000	7,000	15,000
Plan participants' contributions	322,000	49,000	–	–
Transfers	–	232,000	–	–
Actuarial (gain) loss	(818,000)	430,000	(8,000)	(152,000)
Benefits paid	(88,000)	(404,000)	(21,000)	(10,000)
Projected benefit obligation at end of year	<u>\$ 4,844,000</u>	<u>\$ 4,960,000</u>	<u>\$ 96,000</u>	<u>\$ 98,000</u>
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 2,733,000	\$ 2,623,000	\$ –	\$ –
Actual return on plan assets	(851,000)	149,000	–	–
Employer's contribution	82,000	84,000	21,000	10,000
Plan participants' contributions	322,000	49,000	–	–
Transfers	–	232,000	–	–
Benefits paid	(88,000)	(404,000)	(21,000)	(10,000)
Fair value of plan assets at end of year	<u>\$ 2,198,000</u>	<u>\$ 2,733,000</u>	<u>\$ –</u>	<u>\$ –</u>
Funded Status	<u>\$(2,646,000)</u>	<u>\$(2,227,000)</u>	<u>\$ (96,000)</u>	<u>\$ (98,000)</u>
Amounts recognized in the Balance sheet consist of:				
Current liability	\$ –	\$ –	\$ –	\$ –
Non-current liability	(2,646,000)	(2,227,000)	(96,000)	(98,000)
Net amount recognized	<u>\$(2,646,000)</u>	<u>\$(2,227,000)</u>	<u>\$ (96,000)</u>	<u>\$ (98,000)</u>
Amounts recognized in the Unrestricted net assets consist of:				
Net actuarial loss (gain)	\$ 994,000	\$ 761,000	\$ (395,000)	\$ (426,000)
Prior service cost (credit)	10,000	15,000	(1,000)	(32,000)
Net amount recognized	<u>\$ 1,004,000</u>	<u>\$ 776,000</u>	<u>\$ (396,000)</u>	<u>\$ (458,000)</u>
Weighted-average assumptions as of 31 December				
Discount rate	7.25%	6.00%	7.25%	6.00%
Expected return on plan assets	8.00%	8.00%	N/A	N/A
Rate of compensation increase varies with age and averages	5.05%	4.65%	5.05%	4.65%

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For measurement purposes, a 9.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for the valuation as at 31 December 2008. The rate was assumed to decrease gradually to 5.0% for 2013 and remain at that level thereafter.

	Pension Benefits		Postretirement Medical Benefits	
	2008	2007	2008	2007
Components of net periodic benefit cost:				
Service cost	\$163,000	\$126,000	\$ 20,000	\$ 14,000
Interest cost	305,000	258,000	7,000	15,000
Expected return on plan assets	(226,000)	(198,000)	–	–
Amortization of prior service cost	5,000	5,000	(31,000)	(31,000)
Recognized actuarial loss	26,000	–	(39,000)	(24,000)
Net periodic benefit cost	<u>\$273,000</u>	<u>\$191,000</u>	<u>\$(43,000)</u>	<u>\$(26,000)</u>

The accumulated benefit obligation of the pension plan as of 31 December 2008 was \$4,635,000 (\$4,726,000 – 2007).

A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	1-Percentage-Point Increase	1-Percentage-Point Decrease
Effect on total service and interest cost components	\$ 7,000	\$ (5,000)
Effect on postretirement benefit obligation	22,000	(19,000)

*Estimated Future Benefits Payments*

The following table shows the benefit payments expected to be paid in each of the next five years and subsequent five years. The expected benefit payments are based on the same assumptions used to measure the benefit obligation at 31 December 2008:

	Pension Benefits	Postretirement Medical Benefits
2009	\$ 215,000	\$ –
2010	179,000	–
2011	209,000	–
2012	241,000	–
2013	272,000	1,000
2014-2018	1,671,000	12,000