

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(A COMPONENT UNIT OF THE FEDERATED STATES
OF MICRONESIA NATIONAL GOVERNMENT)**

**FINANCIAL STATEMENTS,
ADDITIONAL INFORMATION AND
INDEPENDENT AUDITORS' REPORT**

YEARS ENDED DECEMBER 31, 2013 AND 2012

**FEDERATED STATES OF MICRONESIA SOCIAL SECURITY ADMINISTRATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA
NATIONAL GOVERNMENT)**

Years Ended December 31, 2013 and 2012
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INDEPENDENT AUDITORS' REPORT

Board of Trustees
FSM Social Security Administration:

Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia (FSM) Social Security Administration (the Administration), a component unit of the FSM National Government, which comprise the statements of fiduciary net position as of December 31, 2013 and 2012, and the related statements of changes in fiduciary net position for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the FSM Social Security Administration as of December 31, 2013 and 2012, and the changes in its net position for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. This supplementary information is the responsibility of the Administration's management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

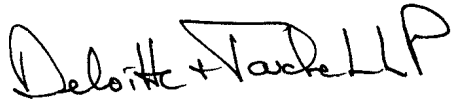
Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Administration's basic financial statements. The Other Supplementary Information listed in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Other Supplementary Information is the responsibility of the Administration's management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standard generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 26, 2014, on our consideration of the Administration's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Administration's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is written in a cursive, stylized font.

May 26, 2014

**FEDERATED STATES OF MICRONESIA SOCIAL SECURITY ADMINISTRATION
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Management's Discussion and Analysis
Years Ended December 31, 2013 and 2012

The following discussion and analysis provides an understanding of the FSM Social Security Administration's (FSMSSA) financial performance for fiscal year ended December 31, 2013. This section has been prepared by the management and should be read in conjunction with the FSMSSA's financial statements and accompanying notes.

Administration

The FSMSSA is a successor System of the former Trust Territory Social Security System. It was established by the Federated States of Micronesia Public Law 2-74 and began its full operation on January 1, 1988. The FSMSSA provides retirement, disability and survivor benefits to the citizens of the Federated States of Micronesia.

Under Title 53 of the FSM Code, the authority to administer the FSMSSA is vested to a six-member Board of Trustees, five of whom are nominated by the President and confirmed by the Congress of the FSM. The nominations to the Board take into account the need to have adequate geographical representation and to have representatives from public and private sector employers and employees. The members and officers of the Board of Trustees are as follows:

Gillian Doone	National Government	Chairman of the Board
Kalwin Kephas	State of Kosrae	Member
Rose Nakanaga	State of Pohnpei	Member
Nakama Sana	State of Chuuk	Member
Vincent Tafileluw	State of Yap	Vice Chairman
Alexander R. Narruhn	Administrator	Member, Ex officio

The Administrator, who is selected by the Board, is responsible for daily operation as well as supervision of branch managers from each of the four States of the FSM.

Funding

The FSM Social Security System is financed by employer/employee contributions at a rate of 7.5% each, or a combined tax rate of 15% paid to the system every quarter. The National and State governments as well as all private employers incorporated or doing business in the FSM are subject to social security tax. Beginning January 01, 2013, the maximum quarterly taxable wage of \$6,000 is subject to an increment of \$1,000 and every 5 years thereafter for a maximum of \$10,000 until January 1, 2028. Effective January 01, 2013, both the tax rate and the maximum quarterly taxable wage have been increased from 7% to 7.5% (employee 7.5%, employer 7.5%) and from \$6,000 to \$7,000, respectively.

Additional revenues are derived from interest and penalties charged to delinquent taxpayers, and other miscellaneous fees.

Budget

The FSM Public Law 5-120 mandates the FSMSSA to present an annual budget not exceeding 11% of its projected income for the ensuing fiscal year. The budget ceiling for fiscal year 2013 based on projected income of \$16.50 million was \$1.82 million. However, as part of management's cost cutting measures, the budget was streamlined at \$1.26 million which is 7.6% of the projected income. The actual administrative costs incurred for FY2013 was \$1.16 million, or 8% surplus compared to the approved budget. The remaining administrative costs for FY 2013 of \$0.04 million pertained to the Prior Service Fund.

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Management's Discussion and Analysis
Years Ended December 31, 2013 and 2012

Highlights

- Contributions collected increased by 5.33% from \$16.37 million in 2012 to \$17.24 million in 2013.
- Total benefit payments to members or their beneficiaries increased by 3.74% from \$17.98 million in 2012 to \$18.66 million in 2013.
- 6,377 beneficiaries received social security benefits as of the end of fiscal year 2013.
- 849 retirement, survivor and disability claims were received and processed in fiscal year 2013.
- The investment portfolio, including marketable securities, increased by 17.55% from \$37.21 million in 2012 to \$43.74 million in 2013.
- A drawdown of \$1.0 million was made from the investment portfolio to supplement benefit payments.
- Received \$1.0 million in funding from the FSM National Government, which was used to supplement benefit payments.
- Net position totaled \$49.13 million in December 31, 2013, compared to \$42.84 million in December 31, 2012, an increase of 14.69%.
- \$952,959 of delinquent accounts were collected in fiscal year 2013.
- Close monitoring of expenses led to a budget surplus of 8% in fiscal year 2013.
- Received \$360,100 from Prior Service Trust Fund Administration (PSTFA). Prior Service benefits paid in 2013 totaled \$223,247.
- Effective January 01, 2013, the tax rate and maximum taxable wages have been increased from 7% to 7.5% (employee 7.5%, employer 7.5%) and from \$6,000 to \$7,000, respectively.

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Management's Discussion and Analysis
Years Ended December 31, 2013 and 2012

RESULTS OF OPERATIONS / CHANGES IN FIDUCIARY NET POSITION

FSMSSA follows the calendar year as its fiscal year. The following table presents information about FSMSSA Retirement Fund's results of operations for CY2013, 2012 and 2011.

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Contributions	\$ 17,244,974	\$ 16,371,874	\$ 16,593,155
Benefit payments	(18,431,758)	(17,745,448)	(17,366,480)
Administrative expenses	(1,156,701)	(1,035,997)	(1,032,036)
Other income	<u>1,041,065</u>	<u>1,044,444</u>	<u>1,247,807</u>
Operating deficit	(1,302,420)	(1,365,127)	(557,554)
Investment income (loss), net	<u>7,502,456</u>	<u>3,669,947</u>	<u>(1,421,047)</u>
Change in net position	6,200,036	2,304,820	(1,978,601)
Net position at beginning of year	<u>42,687,289</u>	<u>40,382,469</u>	<u>42,361,070</u>
Net position at end of year	\$ <u>48,887,325</u>	\$ <u>42,687,289</u>	\$ <u>40,382,469</u>

Contributions

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Government	\$ 8,521,408	\$ 7,901,969	\$ 7,495,281
Private	8,523,577	8,266,665	8,772,936
Judgment	12,617	18,854	82,192
Penalties and interests	<u>187,372</u>	<u>184,386</u>	<u>242,746</u>
Total	\$ <u>17,244,974</u>	\$ <u>16,371,874</u>	\$ <u>16,593,155</u>

The total amount of contributions collected was \$17.24 million, averaging a collection of \$4.31 million per quarter. This amount constitutes an increase of 5.33% compared to 2012 at \$16.37 million. The higher collection was attributed to the recent increase in tax rate from 7% to 7.5% (15% employer & employer combined) and increase in maximum taxable wages from \$6,000 to \$7,000. The increase was effective January 01, 2013.

Total delinquent taxes collected in 2013 amounted to \$952,959. Of this amount, 47.4% or \$451,545 pertains to the prior years.

Benefit Payments

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Retirement	\$ 11,457,404	\$ 11,038,569	\$ 10,870,989
Survivors	5,189,255	5,068,023	4,881,958
Disability	1,523,375	1,456,825	1,395,552
Lump Sum	<u>261,724</u>	<u>182,031</u>	<u>217,981</u>
Total	\$ <u>18,431,758</u>	\$ <u>17,745,448</u>	\$ <u>17,366,480</u>

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Years Ended December 31, 2013 and 2012

Benefit payments increased by 3.87% from \$17.75 million in 2012 to \$18.43 million in 2013. The increase was attributed mainly to new claims received processed and approved during the year. Also, part of the reason for a higher rate of increase this year was the eligibility survey held in 2012. Benefits were put on hold for those individuals who did not complete the survey during the period. As of December 31, 2013, there were six thousand three hundred seventy-seven (6,377) members or their beneficiaries who received benefits in fiscal year 2013.

Administrative Expense

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Budget	\$ 1,255,695	\$ 1,115,902	\$ 1,063,046
Actual	\$ 1,156,701	\$ 1,035,997	\$ 1,032,036
Surplus	\$ 98,994	\$ 79,905	\$ 31,010
% of Budget	8%	7%	3%

Administrative expense increased by 11.65%. The higher administrative expense this year was attributed to the computer upgrade including servers for Pohnpei branch and Chuuk branch offices. Also, a new vehicle was purchased for Kosrae branch. Despite the higher administrative cost, a budget surplus of 8% was attained this year as a result of management continuous monitoring of its operating expenses.

Investment Income / (Loss)

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Investment	\$ 43,736,351	\$ 37,206,732	\$ 35,220,871
Income /(Loss)	\$ 7,502,456	\$ 3,669,947	\$ (1,421,047)
Drawdowns	\$ 1,000,000	\$ 1,000,000	\$ 500,000

Investment income increased by 104% from \$3.67 million net gain in 2012 to \$7.50 million net gain in 2013. The net gain is attributed mainly to the good performance of the equity investment accounts. As a result, the market value of the investment portfolio as of the end of FY2013 rose to \$43.74 million from \$37.21 million in 2012. This end of year market value is net of \$1.0 million drawdown during the year to supplement benefit payments in addition to the \$1.0 million funding received from the FSM National Government.

Other Income

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Approp. from FSM Govt.	\$ 1,000,000	\$ 1,000,000	\$ 1,200,000
Prior Service Reimbursement	44,649	47,334	35,359
Miscellaneous Receipts	26,438	31,661	43,078
Tax Refunds	<u>(30,022)</u>	<u>(34,551)</u>	<u>(30,630)</u>
Total	\$ <u>1,041,065</u>	\$ <u>1,044,444</u>	\$ <u>1,247,807</u>

Other Income decreased by 0.32% or \$3,379. The total income received from Prior Service reimbursement which is equivalent to 20% of benefits paid has decreased this year due to lower benefit payments as a result of decreasing number of Prior Service beneficiaries.

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NET POSITION

FSMSSA Retirement Fund's Statement of Fiduciary Net Position as of December 31, 2013, 2012 and 2011 follows:

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Assets			
Cash and equivalents	\$ 1,931,021	\$ 2,244,250	\$ 1,209,552
Investments	43,736,351	37,206,732	35,220,871
Other current assets	3,293,007	3,424,074	4,059,782
Fixed assets, net	<u>107,152</u>	<u>102,841</u>	<u>109,787</u>
Total	<u>49,067,531</u>	<u>42,977,897</u>	<u>40,599,992</u>
Liabilities	<u>180,206</u>	<u>290,608</u>	<u>217,523</u>
Net Position			
Held in trust for retirement, Disability and survivors; benefit	\$ <u>48,887,325</u>	\$ <u>42,687,289</u>	\$ <u>40,382,469</u>

Net position for the retirement fund (excluding the Prior Service Fund) increased by 14.5% from \$42.69 million in 2012 to \$48.89 million in 2013. The increase was attributed mainly to the net investment gain as a result of a higher market value of the portfolio as of the end of the year 2013.

The FSMSSA continues to manage the Prior Service Benefits Program for FSM citizens, which is funded by the U.S. Department of Interior, Office of the Insular Affairs. For FY 2013, total funds received from the Prior Service Trust Fund Administration (PSTFA) amounted to \$360,100 while benefits paid and administrative expenses totaled \$223,247 and \$44,670, respectively.

No significant capital additions have occurred. For additional information, please refer to the notes to the financial statements.

As of December 31, 2013, the Prior Service Fund had net position of \$246,215. Contributions decreased by 11.93% while benefit payments also decreased by 5.66%.

Following are the Statement of Fiduciary Net Position as of December 31, 2013, 2012 and 2011 and Statement of Changes in Fiduciary Net Position for the years ended December 31, 2013, 2012 and 2011 of PSTFA.

Statement of Fiduciary Net Position
(Prior Service fund)

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Assets	\$ 299,712	\$ 196,297	\$ 70,650
Liabilities	<u>(53,497)</u>	<u>(44,050)</u>	<u>(43,750)</u>
Net position	\$ <u>246,215</u>	\$ <u>152,247</u>	\$ <u>26,900</u>

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Statement of Changes in Fiduciary Net Position
(Prior Service Fund)

	<u>2013</u>	<u>2012</u>	<u>2011</u>
PSTFA contributions	\$ 361,324	\$ 408,879	\$ 272,797
Benefit payments	(223,247)	(236,645)	(253,765)
Administrative expenses	(44,670)	(47,373)	(35,398)
Other	<u>561</u>	<u>486</u>	<u>231</u>
Change in net position	93,968	125,347	(16,135)
Net position at beginning of year	<u>152,247</u>	<u>26,900</u>	<u>43,035</u>
Net position at end of year	\$ <u>246,215</u>	\$ <u>152,247</u>	\$ <u>26,900</u>

Management's Discussion and Analysis for the year ended December 31, 2012 is set forth in the Administration's report on the audit of financial statements, which is dated May 27, 2013. That Discussion and Analysis explains the major factors impacting the 2012 financial statements and can be viewed at the Office of the Public Auditor's website at www.fsmopa.fm.

Conclusion:

The FSMSSA retirement fund net position in fiscal year 2013 grew by 14.5% or \$6.20 million compared to fiscal year 2012. The increase was attributed mainly to the increase in market value of the investment portfolio, particularly from the good performance of the equity investment accounts. However, the year 2013 saw another operating deficit due to imbalances between collection and benefit payments including administrative expenses. Total contributions collected were \$17.24 million while benefits paid and administrative expenses totaled \$18.43 million and \$1.16 million, respectively resulting in an operating deficit of \$2.3 million. To cover the deficit, \$1.0 million was withdrawn from the investment portfolio. The FSM National Government also appropriated \$1.0 million to supplement the benefit payments.

One of the major challenges the system is currently facing is to enforce the recovery and collection of outstanding social security taxes from delinquent employers. For fiscal year 2013, we have managed to recover over \$952,959 in delinquent taxes, which is an achievement considering the slow economic growth in the FSM.

With increased benefit payments of 3.87% and 2.18% in fiscal years 2013 and 2012 respectively, and unfunded accrued liability of \$245.4M (as of Jan 1, 2011), management endeavors to improve its operation through the following:

1. Collection of delinquent taxes;
2. Spot audits;
3. Conduct periodic eligibility survey of current beneficiaries;
4. Monitor investment performance; and
5. Control administrative expenses.

We would also request supplemental funding from the FSM National Government to help with the weak cash flow as experienced during the past several years due to imbalances between collected contributions and benefit payments including administrative expenses.

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2014 Outlook

Collection for 2014 is projected to increase at a lower rate compared to 2013 which attained a 5% increase due to the higher tax rate and taxable wages that took effect during the year. As there won't be any increase in tax rate and taxable wages until 2018, collections for 2014 is projected to increase 1% or to be at approximately same level as in 2013. Management will continue to remain focused on increasing collections from delinquent accounts and to make employers pay their current quarterly tax dues by ongoing spot audits that will include most of the employers in all of the FSM States. Having said this, collections from contributions are estimated to be approximately \$17.45 million including collection from delinquent accounts.

Benefit payments will continue to increase in 2014 because of new claims that will be received, processed and approved during the year. Based on the yearly average increase of benefit payments during the past years, it is projected that benefits in 2014 will be around \$18.83 million or an increase of 3% compared to 2013.

Administrative cost is projected to be lower if not approximately equal compared to 2013. Management will continue to implement the cost cutting measures being practiced during the past several years.

Foregoing, benefit payments will increase faster than collection. It is projected that at least \$2.0 million will be needed in additional funding to supplement benefit payments and administrative expenses in 2014. The deficit is anticipated to be funded with cash withdrawals from investments and/or funding from the FSM National Government.

This MD&A is designed to provide our citizens, taxpayers, creditors and other interested parties with a general overview of the FSMSSA's finances and to demonstrate its accountability to funding agencies. Questions concerning any of the information provided in this discussion or requests for information should be addressed to the Administrator, FSM Social Security Administration at P.O. Box L, Kolonia, Pohnpei, FSM 96941.

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Statements of Fiduciary Net Position
December 31, 2013 and 2012

<u>ASSETS</u>	<u>2013</u>	<u>2012</u>
Cash and cash equivalents	\$ 2,229,804	\$ 2,440,547
Receivables:		
Contributions	2,679,938	2,842,350
Due from FSM National Government	500,000	500,000
Accrued interest	92,317	63,599
Other	18,081	14,525
Total receivables	<u>3,290,336</u>	<u>3,420,474</u>
Prepayments	<u>3,600</u>	<u>3,600</u>
Investments:		
Fixed income	13,657,716	13,033,746
Stocks	30,078,635	24,172,986
Total investments	<u>43,736,351</u>	<u>37,206,732</u>
Depreciable fixed assets, net	<u>107,152</u>	<u>102,841</u>
Total assets	<u>49,367,243</u>	<u>43,174,194</u>

LIABILITIES

Accounts payable	199,212	305,286
Other liabilities and accruals	25,638	24,865
Accrued management fees	8,853	4,507
Total liabilities	<u>233,703</u>	<u>334,658</u>

Contingencies

NET POSITION

Held in trust for retirement, disability and survivors' benefits	<u>\$ 49,133,540</u>	<u>\$ 42,839,536</u>
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See accompanying notes to financial statements.

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Statements of Changes in Fiduciary Net Position
Years Ended December 31, 2013 and 2012

	<u>2013</u>	<u>2012</u>
Additions:		
Contributions	\$ 17,244,974	\$ 16,371,874
Investment income:		
Net change in the fair value of investments	6,922,493	3,102,803
Interest and dividends	833,310	736,904
Total investment income	7,755,803	3,839,707
Less investment expense:		
Investment management and custodial fees	(252,786)	(169,274)
Net investment income	7,503,017	3,670,433
Other additions:		
Contributions from FSM National Government	1,000,000	1,000,000
Other	432,411	487,874
	<u>1,432,411</u>	<u>1,487,874</u>
Total additions	<u>26,180,402</u>	<u>21,530,181</u>
Deductions:		
Benefit payments:		
Retirement	11,544,359	11,133,092
Survivors	5,325,547	5,210,145
Disability	1,523,375	1,456,825
Lump sum	261,724	182,031
Total benefit payments	18,655,005	17,982,093
Refunds	30,022	34,551
Administrative	1,201,371	1,083,370
Total deductions	<u>19,886,398</u>	<u>19,100,014</u>
Change in net position	6,294,004	2,430,167
Net position at beginning of year	<u>42,839,536</u>	<u>40,409,369</u>
Net position at end of year	<u>\$ 49,133,540</u>	<u>\$ 42,839,536</u>

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA SOCIAL SECURITY ADMINISTRATION
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Notes to Financial Statements
December 31, 2013 and 2012

(1) Organization

The Social Security Administration of the Federated States of Micronesia (FSM) National Government was established by Public Law 2-74, passed on February 8, 1983, and began operations on October 1, 1987, for the purpose of administering the FSM Social Security Retirement Fund (the Retirement Fund) through the provision of retirement, disability and death benefits to qualified individuals and their survivors. The Administration is administered under the authority of a six-member Board of Trustees, five of whom are appointed by the President of the Federated States of Micronesia. The Administrator, who is selected by the Board, serves as an ex-officio member. Additionally, the Administrator is responsible for processing, monitoring and distributing benefit claims under the Prior Service Benefits Program (see note 7). Accordingly, the Administrator established the Prior Service Fund to account for activities under this program.

(2) Summary of Significant Accounting Policies

A. Basis of Accounting

The FSM Social Security Administration (the Administration) is accounted for as a Fiduciary Fund Type - Private Purpose Trust Fund and is a component unit of the FSM National Government. The Administration prepares its financial statements using the accrual basis of accounting. It recognizes employee and employer contributions as revenues in the quarter employee earnings are paid. Retirement benefits are recognized as expenses when payable. Expenses are recorded when the corresponding liabilities are incurred regardless of when payment is made.

Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus* and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*, establish financial reporting standards for governmental entities, which includes the requirement for the Administration to present Management's Discussion and Analysis (MD&A). The MD&A is considered to be required supplementary information and precedes the financial statements. In addition, these statements require that resources be classified for accounting and reporting purposes as held in trust for retirement, disability and survivors' benefits. Management of the Administration has determined that per its enabling legislation, net position of the Administration is all held in trust for retirement, disability and survivors' benefits.

B. Future Liabilities and Contributions

No recognition is given in the accompanying financial statements to the present value of the liabilities of prospective benefit payments or the present value of future contributions required from employees or employers.

C. Cash and Cash Equivalents

For the purposes of the statements of fiduciary net position, cash and cash equivalents include cash on hand, and cash in checking and savings accounts as well as short-term investments in money market funds with a maturity date within three months of the date acquired.

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Notes to Financial Statements
December 31, 2013 and 2012

(2) Summary of Significant Accounting Policies, Continued

D. Investments

Investments and related investment earnings are recorded at fair value. Fair value is the amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

E. Deposits and Investments

The deposit and investment policies of the Administration are governed by its enabling legislation. The Board is required to engage one or more fund custodians to assume responsibility for the physical possession of the Administration's investments. Legally authorized investments are as follows:

- (i) Government obligations - Obligations issued or guaranteed as to principal and interest by the FSM National Government and/or State governments of the Federated States of Micronesia or by the Government of the United States, provided that the principal and interest on each obligation are payable in the currency of the United States.
- (ii) Corporate obligations and mortgage-backed securities - Obligations of any public or private entity or corporation created or existing under the laws of the Federated States of Micronesia or of the United States or any state, territory or commonwealth thereof, or obligations of any other government or economic community which are payable in United States dollars, or pass through and other mortgage-backed securities provided that the obligation is issued by an agency of the United States Government, the FSM National Government, or is rated in one of the three highest categories by two nationally recognized rating agencies. No investment under this heading shall exceed ten percent of the market value of the Fund or ten percent of the outstanding value of the issue at the time of purchase.
- (iii) Preferred and common stocks - Shares of preferred or common stocks of any corporation created or existing under the laws of the Federated States of Micronesia or under the laws of the United States or any state, territory or commonwealth thereof provided that the purchase of such shares shall be considered reasonable and prudent by the Administration's investment advisor at the time of purchase, that not more than five percent of the market value of the Retirement Fund shall be invested in the stock of any one corporation, and that not more than ten percent of the market value of the Retirement Fund shall be invested in any one industry group.
- (iv) Insurance company obligations - Contracts and agreements supplemental thereto providing for participation in one or more accounts of a life insurance company authorized to do business in the Federated States of Micronesia or in any state, territory or commonwealth of the United States provided that the total market value of these investments at no time shall exceed ten percent of all investments of the Retirement Fund.

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(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Deposits:

Custodial credit risk is the risk that in the event of a bank failure, the Administration's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Administration does not have a deposit policy for custodial credit risk.

As of December 31, 2013 and 2012, the carrying amount of the Administration's total cash and cash equivalents was \$2,229,804 and \$2,440,547, respectively, and the corresponding bank balances were \$2,569,851 and \$2,798,604, respectively. As of December 31, 2013 and 2012, bank deposits in the amount of \$1,201,127 and \$1,369,663, respectively, were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2013 and 2012, bank deposits in the amount of \$500,000 and \$678,505, respectively, were FDIC insured. The Administration does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. The remaining amounts of \$1,368,724 and \$1,428,941, respectively, represent short-term investments held and administered by the Administration's trustees in accordance with various trust agreements. Based on negotiated trust and custody contracts, all of these investments were held in the Administration's name by the Administration's custodial financial institutions at December 31, 2013 and 2012.

Investments:

As of December 31, 2013 and 2012, investments at fair value are as follows:

	<u>2013</u>	<u>2012</u>
Fixed income securities:		
Domestic fixed income	\$ 13,657,716	\$ 13,033,746
Other investments:		
Domestic equities	22,725,474	18,357,176
International equities	<u>7,353,161</u>	<u>5,815,810</u>
	<u>\$ 43,736,351</u>	<u>\$ 37,206,732</u>

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Administrator does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

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(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Investments, Continued

As of December 31, 2013, the Administration's investments in debt securities were as follows:

	<u>Investment Maturities (In Years)</u>				Fair Value
	Less <u>Than 1</u>	<u>1 to 5</u>	<u>6 to 10</u>	Greater <u>Than 10</u>	
U.S. Treasury obligations	\$ 1,354,756	\$ 1,002,134	\$ 936,283	\$ -	\$ 3,293,173
Mortgage and asset-backed securities	-	1,795,352	194,743	2,715,849	4,705,944
Municipal bonds	-	63,609	-	-	63,609
Corporate notes and bonds	<u>-</u>	<u>1,510,572</u>	<u>2,802,937</u>	<u>1,281,481</u>	<u>5,594,990</u>
	<u>\$ 1,354,756</u>	<u>\$ 4,371,667</u>	<u>\$ 3,933,963</u>	<u>\$ 3,997,330</u>	<u>\$ 13,657,716</u>

As of December 31, 2012, the Administration's investments in debt securities were as follows:

	<u>Investment Maturities (In Years)</u>				Fair Value
	Less <u>Than 1</u>	<u>1 to 5</u>	<u>6 to 10</u>	Greater <u>Than 10</u>	
U.S. Treasury obligations	\$ 1,999,980	\$ 1,660,123	\$ -	\$ 423,914	\$ 4,084,017
Mortgage and asset-backed securities	-	-	-	3,740,030	3,740,030
Corporate notes and bonds	<u>374,450</u>	<u>1,346,992</u>	<u>2,430,375</u>	<u>1,057,882</u>	<u>5,209,699</u>
	<u>\$ 2,374,430</u>	<u>\$ 3,007,115</u>	<u>\$ 2,430,375</u>	<u>\$ 5,221,826</u>	<u>\$ 13,033,746</u>

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

The Administration's exposure to credit risk at December 31, 2013, was as follows:

<u>Standard and Poors' Rating</u>	<u>Domestic</u>
AAA	\$ 3,293,173
AA+	4,878,596
AA	40,959
AA-	306,774
A+	140,872
A	740,799
A-	2,015,550
BBB+	599,072
BB+	26,713
BBB	1,085,080
BBB-	413,092
Not rated	<u>117,036</u>
	<u>\$ 13,657,716</u>

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(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Investments, Continued:

The Administration's exposure to credit risk at December 31, 2012, was as follows:

<u>Standard and Poors' Rating</u>	<u>Domestic</u>
AAA	\$ 8,078,722
AA+	338,040
AA	153,774
AA-	197,109
A+	294,588
A	669,096
A-	1,079,205
BBB+	641,672
BBB	1,429,141
BBB-	<u>152,399</u>
	<u>\$ 13,033,746</u>

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Administration will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Administration's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the Administration's name by the Administration's custodial financial institutions at December 31, 2013 and 2012. The Administration's agent is not affiliated with or related to investment brokers. Accordingly, these investments are not exposed to custodial credit risk.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the Administration. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. There was no concentration of credit risk for investments as of December 31, 2013 and 2012.

F. Depreciable Fixed Assets

The cost of fixed assets, if greater than \$250, is capitalized at the time of acquisition. Depreciation is provided using the straight-line basis over the estimated useful lives of the respective assets.

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(2) Summary of Significant Accounting Policies, Continued

F. Depreciable Fixed Assets, Continued

Capital asset activity for the years ended December 31, 2013 and 2012, was as follows:

	<u>Estimated Useful Lives</u>	<u>January 1, 2013</u>	<u>Additions</u>	<u>Retirements</u>	<u>December 31, 2013</u>
Motor vehicles	5 years	\$ 107,880	\$ 7,025	\$ (3,879)	\$ 111,026
Computer software and hardware	5 years	158,262	17,003	(13,850)	161,415
Office furniture, fixtures and equipment	5 years	68,157	12,707	(5,203)	75,661
Home furnishings	5 years	<u>6,738</u>	<u>2,047</u>	-	<u>8,785</u>
		341,037	38,782	(22,932)	356,887
Less accumulated depreciation		<u>(238,196)</u>	<u>(34,471)</u>	<u>22,932</u>	<u>(249,735)</u>
		<u>\$ 102,841</u>	<u>\$ 4,311</u>	<u>\$ -</u>	<u>\$ 107,152</u>

	<u>Estimated Useful Lives</u>	<u>January 1, 2012</u>	<u>Additions</u>	<u>Retirements</u>	<u>December 31, 2012</u>
Motor vehicles	5 years	\$ 105,913	\$ 11,438	\$ (9,471)	\$ 107,880
Computer software and hardware	5 years	168,408	6,383	(16,529)	158,262
Office furniture, fixtures and equipment	5 years	64,571	12,243	(8,657)	68,157
Home furnishings	5 years	<u>6,738</u>	-	-	<u>6,738</u>
		345,630	30,064	(34,657)	341,037
Less accumulated depreciation		<u>(235,843)</u>	<u>(37,009)</u>	<u>34,657</u>	<u>(238,196)</u>
		<u>\$ 109,787</u>	<u>\$ (6,945)</u>	<u>\$ -</u>	<u>\$ 102,841</u>

G. Deferred Outflows of Resources

In addition to assets, the statements of fiduciary net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. The Administration has no items that qualify for reporting in this category.

H. Deferred Inflows of Resources

In addition to liabilities, the statements of fiduciary net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. The Administration has no items that qualify for reporting in this category.

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(2) Summary of Significant Accounting Policies, Continued

I. Contributions

Contributions to the Retirement Fund are governed by the Federated States of Micronesia Social Security Act of 1983, which imposes a tax on the quarterly income of every employee not currently subject to the United States Social Security Administration or any other recognized social security system. There is imposed on the income of every applicable employee a tax equal to seven percent of wages commencing October 1, 2010. The tax rate increased to 7.5% effective January 1, 2013.

Maximum quarterly taxable wages are currently \$6,000 which increased to \$7,000 effective January 1, 2013. Every employer is required to contribute an amount equal to that contributed by employees.

Contribution revenues received during the years ended December 31, 2013 and 2012 are comprised of the following:

	<u>2013</u>	<u>2012</u>
Government employment	\$ 8,521,408	\$ 7,901,969
Private employment	8,523,577	8,266,665
Judgments	12,617	18,854
Penalties and interest	<u>187,372</u>	<u>184,386</u>
	<u>\$ 17,244,974</u>	<u>\$ 16,371,874</u>

J. Benefit Obligations

Retirement benefits are paid to every person who is a fully insured individual as defined by the Federated States of Micronesia Social Security Act, has attained sixty years of age, and has filed an application for old age insurance benefits. Benefits are also paid to surviving spouses of deceased workers, subject to eligibility requirements, as long as they do not remarry or work. Eligible children who are not married or are not working may also receive benefits until age eighteen (18) or up to age twenty-two (22) if in school.

Eligible children who become disabled before age twenty-two (22) will continue to receive benefits for the duration of the disability. Disability benefits are paid to qualified workers for the duration of the disability or until retirement or death at which time retirement or survivor benefits become available.

Benefits are paid monthly and are computed on an annual basis of 16.5% of the first \$10,000 of cumulative covered earnings, plus 3.0% of the next \$30,000, 2.0% of any earnings in excess of \$40,000, and 1.0% of any earnings in excess of \$302,500. As of December 31, 2013 and 2012, the minimum monthly benefit payment is \$100.

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Notes to Financial Statements
December 31, 2013 and 2012

(2) Summary of Significant Accounting Policies, Continued

K. New Accounting Standards

During the year ended December 31, 2013, the Administration implemented the following pronouncements:

- GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, which improved financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB Statement No. 66, *Technical Corrections - 2012*, which enhanced the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial reports of most pension plans, and Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 67 are effective for financial statements for periods beginning after June 15, 2013. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of these statements on the financial statements of the Administration.

In January 2013, GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations*, which improves accounting and financial reporting for state and local governments' combinations and disposals of government operations. Government combinations include mergers, acquisitions, and transfers of operations. A disposal of government operations can occur through a transfer to another government or a sale. The provisions in Statement 69 are effective for fiscal years beginning after December 15, 2013. Management has not yet determined the effect of implementation of this statement on the financial statements of the Administration.

In April 2013, GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, which requires a state or local government guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement. The provisions in Statement 70 are effective for fiscal years beginning after June 15, 2013. Management has not yet determined the effect of implementation of this statement on the financial statements of the Administration.

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Notes to Financial Statements
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(2) Summary of Significant Accounting Policies, Continued

K. New Accounting Standards, Continued

In November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date, an amendment of GASB Statement No. 68*, which improves accounting and financial reporting by addressing an issue in Statement No. 68, Accounting and Financial Reporting for Pensions, concerning transition provisions related to certain pension contributions made to defined benefit pension plans prior to implementation of that Statement by employers and nonemployer contributing entities. The provisions in Statement 71 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of this statement on the financial statements of the Administration.

L. Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) require management to make estimates and assumptions that affect the reported amounts of net position and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

M. Risk Management

The Administration is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Administration has elected to purchase automobile and property and casualty insurance from independent third parties for the risks of loss to which it is exposed. The Administration is substantially self-insured for all other risks. Settled claims have not exceeded commercial coverage in any of the past three years.

(3) Net Position Held in Trust

Net position is held in trust to comply with the Social Security Act of 1983. All net position of the Administration is to be used for retirement, disability and survivors' benefits.

(4) Contingencies

The Administration is aware of liabilities of the fund related to retroactive benefit payments for wages not posted to the system due to an unmatched social security number or name provided by the employer, as well as a liability related to overpayment of contributions. Management is unable to determine a reasonable estimate of the abovementioned liabilities at this time; however, management is of the opinion that the amount is not material to the financial statements as a whole.

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(4) Contingencies, Continued

In January 2012, the Administration obtained an actuarial valuation of the Retirement Fund as of January 1, 2011. The valuation reported actuarial accrued liabilities for the Retirement Fund of \$287,771,000. As of December 31, 2013 and 2012, the Administration recorded total fund equity of \$48,887,325 and \$42,687,289, respectively, in the Retirement Fund, as funds available to fund future benefit obligations. These conditions indicate that the Administration should not increase future or current benefits until a long-term trend of decreasing the unfunded accrued liability is realized.

(5) Contributions from FSM National Government

The Administration receives periodic subsidies for its operations from appropriations received from the Congress of the FSM. During the years ended December 31, 2013 and 2012, contributions from the FSM National Government amounted to \$1,000,000, of which \$500,000 is recorded as receivable from the FSM National Government as of December 31, 2013 and 2012.

(6) Contributions Receivable

The Administration is of the opinion that there are outstanding contributions due to the Retirement Fund; however, a reasonable estimate of this amount cannot be made due primarily to noncompliance by employers.

(7) Prior Service Claims

Under the terms of a Prior Service Claim Adjudication Service Agreement between the Social Security Administration of the Federated States of Micronesia and the Trust Territory Prior Service Trust Fund, the Administration is to provide for the processing of benefit claims and to assist in the monitoring of continuing eligibility under the Prior Service Program. The Prior Service Trust Fund Administration (PSTFA) will reimburse the Administration \$8,000 per annum plus an amount equal to eight percent of the total amount of automated and manual benefit payments. Any cost for the Administration personnel who assist in searching and locating prior service documents in cooperation with the Prior Service Administration will be reimbursed on a dollar for dollar basis.

On September 15, 2005, an agreement was entered into between the PSTFA Board and the U.S. Department of the Interior to delegate the Board's obligations and responsibility for the enrollees eligible for Prior Service Benefits Program to the Social Security Systems of the Republic of the Marshall Islands, the Republic of Palau, the Federated States of Micronesia and the Retirement Fund of the Commonwealth of the Northern Mariana Islands. Based on the agreement, the Social Security Administration (SSA) of each Government shall be entitled to an administrative fee not to exceed 20% of the share of allocated funds.

The Administration assumed administrative functions and as of December 31, 2013 and 2012, had received an allocation of \$361,324 and \$408,879, respectively, from PSTFA of which \$223,247 and \$236,645 were paid as benefits during the years ended December 31, 2013 and 2012, respectively. However, while the Administration accepts the liability for any amounts received, the Administration does not accept the obligation to pay future benefits unless additional funds are received from PSTFA. As of December 31, 2013 and 2012, the amount available for future benefit payments under the Prior Service Benefits Program amounted to \$246,215 and \$152,247, respectively.

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Combining Statement of Fiduciary Net Position
December 31, 2013

	<u>Retirement Fund</u>	<u>Prior Service Fund</u>	<u>Total</u>
<u>ASSETS</u>			
Cash and cash equivalents	\$ 1,931,021	\$ 298,783	\$ 2,229,804
Receivables:			
Contributions	2,679,938	-	2,679,938
Due from FSM National Government	500,000	-	500,000
Accrued interest	92,317	-	92,317
Other	17,152	929	18,081
Total receivables	<u>3,289,407</u>	<u>929</u>	<u>3,290,336</u>
Prepayments	<u>3,600</u>	<u>-</u>	<u>3,600</u>
Investments:			
Fixed income	13,657,716	-	13,657,716
Stocks	<u>30,078,635</u>	<u>-</u>	<u>30,078,635</u>
Total investments	<u>43,736,351</u>	<u>-</u>	<u>43,736,351</u>
Depreciable fixed assets, net	<u>107,152</u>	<u>-</u>	<u>107,152</u>
Total assets	<u>49,067,531</u>	<u>299,712</u>	<u>49,367,243</u>
<u>LIABILITIES</u>			
Accounts payable	145,715	53,497	199,212
Other liabilities and accruals	25,638	-	25,638
Accrued management fees	8,853	-	8,853
Total liabilities	<u>180,206</u>	<u>53,497</u>	<u>233,703</u>
<u>NET POSITION</u>			
Held in trust for retirement, disability and survivors' benefits	<u>\$ 48,887,325</u>	<u>\$ 246,215</u>	<u>\$ 49,133,540</u>

See Accompanying Independent Auditors' Report.

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Combining Statement of Changes in Fiduciary Net Position
Year Ended December 31, 2013

	<u>Retirement Fund</u>	<u>Prior Service Fund</u>	<u>Total</u>
Additions:			
Contributions	\$ 17,244,974	\$ -	\$ 17,244,974
Investment income:			
Net change in the fair value of investments	6,922,493	-	6,922,493
Interest and dividends	832,749	561	833,310
Total investment income	7,755,242	561	7,755,803
Less investment expense:			
Investment management and custodial fees	(252,786)	-	(252,786)
Net investment income	7,502,456	561	7,503,017
Other additions:			
Contributions from FSM National Government	1,000,000	-	1,000,000
Other	71,087	361,324	432,411
	<u>1,071,087</u>	<u>361,324</u>	<u>1,432,411</u>
Total additions	<u>25,818,517</u>	<u>361,885</u>	<u>26,180,402</u>
Deductions:			
Benefit payments:			
Retirement	11,457,404	86,955	11,544,359
Survivors	5,189,255	136,292	5,325,547
Disability	1,523,375	-	1,523,375
Lump sum	261,724	-	261,724
Total benefit payments	18,431,758	223,247	18,655,005
Refunds	30,022	-	30,022
Administrative	1,156,701	44,670	1,201,371
Total deductions	<u>19,618,481</u>	<u>267,917</u>	<u>19,886,398</u>
Change in net position	6,200,036	93,968	6,294,004
Net position at beginning of year	<u>42,687,289</u>	<u>152,247</u>	<u>42,839,536</u>
Net position at end of year	<u>\$ 48,887,325</u>	<u>\$ 246,215</u>	<u>\$ 49,133,540</u>

See Accompanying Independent Auditors' Report.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Board of Trustees
FSM Social Security Administration:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Federated States of Micronesia Social Security Administration (the Administration), which comprise the statement of fiduciary net position as of December 31, 2013, and the related statement of changes in fiduciary net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 26, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Administration's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Administration's internal control. Accordingly, we do not express an opinion on the effectiveness of the Administration's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

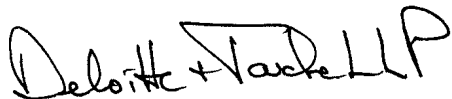
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Administration's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Deloitte + Tatchell LLP". The signature is written in a cursive, stylized font.

May 26, 2014

**FEDERATED STATES OF MICRONESIA SOCIAL SECURITY ADMINISTRATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA
NATIONAL GOVERNMENT)**

Summary Schedule of Prior Year Findings
Year Ended December 31, 2013

There are no prior year findings unresolved as of December 31, 2013.