FSMSSA 2007 Annual Report

SOCIAL SECURITY ADMINISTRATION
OFFICIAL SEAL
FEDERATED STATES OF MICRONESIA

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Letter from the Chairman

This report covers calendar year 2007, the 21st fiscal year of operation of Social Security as an independent program under the Federated States of Micronesia.

I have been a member of the Board since 2002 and am in my second year as the Chairman. I am proud to serve along side the other dedicated Board members and to work with the fine people who make up the Administration. I look forward to working hand-in-hand with the Executive and Legislative branches of the National Government to ensure that any and all legislation that affects Social Security will guarantee the future health of the program and benefit payments to all beneficiaries.

In April of 2006, the Social Security Administration assumed the responsibility of paying Prior Service Benefits to citizens of the Federated States of Micronesia. The Prior Service Trust Fund Board of Trustees is responsible for providing the Administration funds to pay these benefits from the United States. It is important to note that unless otherwise indicated, this Annual Report does not reflect the assets or liability of the Prior Service program and that Prior Service Benefits are not paid from the general revenues of the Social Security System, but rather are separately funded and accounted for.

During 2007, the trust realized total net investment income of $3,723,433, an 8.4% return which extended the trend of a positive return to five years in a row. Also during 2007, Social Security received $12,783,551 in contributions, paid $969,030 in administrative expenses and disbursed $13,663,880 in benefit payments and refunds of contributions. Benefit payments increased by 8.6% in 2007 compared to 2006. It is also important to note that after a decrease in contributions from 2005 to 2006 there was an increase of 6.1% in the amount of contributions collected from 2006 to 2007.

Public Law 14-86 was enacted in 2006. This law increases the funded status of the system and helps insure the future of social security in Micronesia. However, additional legislation is necessary. The Board and the Administration have proposed additional legislation which is necessary to further guarantee future financial security.

I would like to thank the Board members whose terms expired in 2007: Bernes Reselap, who served from 2000 to 2006, and Nena Ned, who served from 1997 to 2006, for their service on the Board. Their commitment to the people of Micronesia through their service on the Board is evident in the progress that Social Security has made over the years.

And finally, I would like to thank the other members of the Board and the Administration for their hard work and dedication that continue to ensure old age, disability, and survivor benefits to the people of Micronesia.

Sincerely,

Jack Yakana
Chairman
Board of Trustees

Administrator's Report

The Board of Trustees is the governing body of the Federated States of Micronesia Social Security System. Members are nominated by the President, confirmed by the Congress and serve three-year terms.

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 Social Security Administrator is an ex officio member of the Board.

Board Members		Terms
Pohnpei State Jack Yakana *Chairman*		10/10/02 to 10/9/05 10/10/05 to 10/10/08
FSM National Government *Nahoy G. Selifis* *Vice-Chairman*		10/10/02 to 10/9/05 10/10/05 to 10/9/08
Yap State Charles L. Chieng		5/26/89 to 5/26/92 6/5/92 to 6/5/95 5/13/96 to 5/13/99 5/26/99 to 5/26/02 11/5/02 to 11/4/05 11/15/05 to 11/14/08
Kosrae State Yosiwo George *FSM Ambassador to United States*		11/23/07 to 11/23/10
Chuuk State Garrison Irons		3/29/07 to 3/29/10
Administrator Alexander R. Narruhn *Ex-Officio Member*		7/1/00 to 6/30/02 7/1/02 to 6/30/05 7/1/05 to 6/30/08 7/1/08 to 6/30/11

I submit this Annual Report of the Federated States of Micronesia Social Security System (FSMSSA, or the "System") covering the period January 1, 2007 to December 31, 2007, the 2007 fiscal year, for the review of all interested parties.

As management of the FSMSSA, the Administration is responsible for the accuracy of the data presented in this report. We believe that this data is accurate in all material aspects and is reported in such a manner as to accurately represent the financial condition of the FSMSSA operations.

In 2007, Social Security celebrated its 39th year of operation. Progress is being made to further increase the financial stability of the fund. A significant amount of education was provided by the Administration to the Board of Trustees, the Legislatures and the participants of the fund as to the importance to make sure money is available in the future to pay promised benefits. As part of this education, a proposed public law has been presented as a step in the right direction. C.B. 15-52 proposes the following changes:

1. Clarification of the definition of "employer". The main purpose of the amendment is to improve tax collections by clearly outlining employer tax responsibilities so as to prevent employers from failing to pay taxes.

2. Require at least 50 quarters of coverage and at least $2,500 in contributions to the Social Security System to be fully insured for death or old age benefits.

3. Require at least 45 quarters of coverage and at least $1,500 in contributions to the Social Security System to be fully insured for disability benefits.

4. Require that individuals who become disabled on or after January 1, 2008 meet the definition of currently insured to qualify for a disability benefit. To be currently insured, one must have at least 20 quarters of coverage within the 25-quarter period ending with the quarter in which a person retires, dies or becomes disabled.

5. Impose criminal penalties on an employer for intentional failure to pay taxes and to identify the chief financial officer of municipal organizations, states of the FSM, or any agencies of any of the above as the individual liable to the program.

6. Allow for a lien on unpaid taxes, including penalties and interest accrued thereon

7. Limit surviving child's benefit to age 20 for students.

8. Reduce retirement benefits that begin on or after January 1, 2008 by 50% if started between the ages 60 to 64. At age 65 the benefit increases to the original unreduced amount. Reduced payments are not subject to the earnings test.

9. Allow fully insured individuals who are also citizens of the Federated States of Micronesia to elect a lump sum payment equal to all amounts contributed by him or her at the time of application for this lump sum, which will be paid when the individual attains age 60.

10. Decrease retirement benefit payments that begin or continue after January 1, 2008 by 30% when a retiree's cumulative benefits exceed the retiree's total contributions into the system, including the employer's share.

11. Increase the tax rate paid by both employees and employers to 7% on October 1, 2009, and to 7.5% five years later.

12. Allow the FSMSSA to invest in BBB grade bonds.

13. Allow for investments in the international market if their currency is in American Depository Receipts.

14. Change the percentage of the market value of the fund that can be invested in the stock of any one corporation from five to ten percent; and to change the percentage of the market value of the fund that can be invested in any one industry group from ten to twenty-five percent; and to insert a security measure so as to ensure that the portfolio is being invested only on a recognized national or regional stock exchange, physical or electronic.

15. Establishes an FSM Social Security Credit Union, which could then invest locally by making loans and taking deposits.

Public Law 14-86 was enacted in 2006 and added a fourth tier of 1.0% of total cumulative covered earnings in excess of $302,500 to the calculation of retirement and disability benefits that begin on or after January 1, 2007, scheduled regular increases in the maximum quarterly covered wages in $1,000 increments from $5,000 to $10,000 on January 1, 2028, and increased the minimum monthly benefit from $50 to $75 and then $100 on January 1, 2012. It also changed the definition of currently insured to require that an individual must have earned at least 20 quarters of coverage during the 25 quarter period ending with the earlier of the quarter in which he died, became entitled to old age benefits at age 60, or became disabled in order to qualify as currently insured. And finally, after December 31, 2006, a worker must have no more than 50 quarters of coverage and have contributed at least $2,500 to the Social Security System to be fully insured for an old age or death benefit and no more than 45 quarters and have contributed at least $1,500 to the Social Security System to be fully insured for a disability benefit.

Board Meetings

The Board of Trustees held three regular meetings during 2007.

The first regular meeting of the Board of Trustees was held on Pohnpei on March 5-6, 2007. Board members that were present included Chairman and Representative of Pohnpei, Lt. Gov. Jack E. Yakana, Vice-Chairman and at-large member, Nahoy G. Selifis, Representative of Yap, Charles L. Chieng. Social Security Administrator Alexander R. Narruhn, serving as ex-officio member, was also present.

The main agenda item of the meeting was the budget for calendar year 2007. The approved budget for calendar year 2007 is $1,039,581 which is 8.7% of the projected income. The maximum ceiling for administrative expenses is 11% of projected revenue. The administrator also presented financial statements for the year 2006. $957,805.83 in delinquent taxes were collected for the duration of 2006.

Total tax collections amounted to $11.9 million while benefit payments came in at $12.6 million. Mr. Narruhn brought the board's attention to the fact that payments now outpaced collections. Since the nature of the social security program required collections to be greater than payments in order to survive, the situation was not a feasible one.

The board also met with its investment portfolio's money managers through a teleconference held in the Telecommunications office building with investment consultant, Smith Barney, represented by Daniel Roland. Investments for the year 2006 turned out better than expected. By December 31, 2006, the portfolio had seen a gain of $4.18 million bringing its total value to $42.6 million.

The board's final agenda item was to extend the Deputy Administrator's contract for another two years. The Deputy Administrator, Dernista I. Capelle, has served diligently, and the board was confident in its decision to extend her contract.

The second regular meeting of the Board of Trustees took place on July 3-4, 2007, in Chuuk. Attending the meeting were Chairman and Pohnpei State representative, Jack E. Yakana; Vice Chairman and National Government Representative, Nahoy G. Selifis; newly-appointed Chuuk State representative, Garrison Irons. Ex-officio member, Social Security Administrator Alexander R. Narruhn was also present.

The board elected to have its meeting in Chuuk to coincide with the public education efforts at the Branch Office for this year's Annual Social Security Week and to entertain appeal cases from the state.

The Administrator reported on financial status of the System and revealed that from January 1 to March 31 of 2007 a total of $3.146 million had been collected. Total benefits paid during the same period were $3.339 million. As of March 31, 2007, administrative expenses totaled $211,062, representing 20.3% of the approved budget for calendar year 2007. Investments increased by $498,000 in the first quarter.

Moving on to new business, the Board entertained two appeal cases. As is mandated by law, a person whose claim is denied by the Administration has the right to make an appeal to the board within 60 days of the denial.

The Board then listened to a presentation by their actuary, Michael Spaid. He presented a study that concerned a number of amendments the Administration was planning. In his study, it was revealed that the tentative amendments would increase the FSMSSA's funded ratio from the current 16% to 24%.

The third regular meeting of the Board of Trustees took place on December 11-12, 2007, on the island of Kosrae. For the first time since February 2006, the board gathered with a full quorum. Gathered for the meeting were Chairman and Pohnpei State Representative, Lt. Gov. Jack E. Yakana; Vice Chairman and National Government Representative, Nahoy G. Selifis; Representative of Yap, Charles L. Chieng; Representative of Chuuk, Garrison Irons; and filling in vacant Kosrae Representative Seat, was Yosiwo George. FSMSS Administrator Alexander R. Narruhn was also present as ex-officio member.

Chairman Yakana opened the meeting with the roll call after which each member of the board took the time to cast their opening remarks. George officially welcomed the board to the State of Kosrae as its new representative and revealed that he was quite pleased to be representing his state. Each of the members echoed each other in their pleasure for finally attaining a full quorum. In his opening remarks, Chieng expressed similar sentiments and said he hoped the board would finally move forward with all the challenges the system currently faced

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The first item on the agenda was a presentation by Daniel Roland of Smith Barney's Consulting Group. The FSMSSA's portfolio is managed by three money managers: Atalanta Sosnoff, Payden & Rygel, and Missouri Valley Partners. The total value of the fund as of September 30, 2007, was $44.479 million. 59.2% of that was invested in large cap core, 32.3% was in fixed income, and the remaining 8.6% was invested in small cap. The growth of the portfolio was largely attributed to the constant over performance of Atalanta Sosnoff, which had constantly beat its benchmarks and outperformed other managers.

The board paid a courtesy visit to the Governor of the State of Kosrae, Robert J. Weilbacher, and offered its willingness to participate in any state-arranged meeting or hearing in which the board would be glad to hear the people's concerns and questions. Chairman Yakana revealed that the board had conducted open public forums in the past and would be willing to schedule another for the State of Kosrae if requested to do so. The Governor thanked the board for the visit and assured them that if the need for a forum were to arise, he would inform the board of it.

The board reconvened in the conference room for a presentation from Donald H. Clark, vice president of Administrative Services Corporation. In his presentation, Clark walked the board through the viability of retirement plans.

Administrator Narruhn then made his report to the board concerning the FSMSSA's current status. While benefit payments were constantly increasing, collections seemed to have reached a stagnant point and as a result, both 2005 and 2006 came in with deficits. Operations and benefit payments were greater than collections by $817,000 in 2005 and by $1.814 million in 2006. As of September 30, 2007, benefit payments came in at a total of $10.217 million while contributions amounted to $8.688 million. Narruhn revealed that Public Law 14-86 had been passed in 2006, with the bulk of its amendments coming into effect on January 1, 2007. The intention of the law had been to decrease this gap between benefit payments and collections. Going on further, the administration had submitted a bill to the president which is currently with congress and this bill aims to rectify this issue by introducing key changes to help the system's unfunded liability and to bring a balance between collections and payments.

The administrator revealed that as of September 30, 2007, $4.082 million was reported delinquent. Out of this, the FSMSSA had been able to collect $1.704 million as of September 30, 2007, through audits and resulting payment agreements.

The administrator walked the board through the pending amendment which if passed into law, would help the administration's collections and decrease the system's unfunded liability by a total of $84.9 million and raise its funded status from the current 16% to 24%.

After entertaining an appeal case, the board had the administrator continue with his report. The administrator went on to present to the board the 2008 Proposed Budget for the FSMSSA. The proposed budget was at $1,104,132, which was 9.2% of the total projected income of the year, well below the maximum of 11%. The administrator reminded the board that the FSMSSA had never exhausted the total budget for any one year. The board approved the calendar year 2008 proposed budget as it was well under the ceiling.

The board also approved a resolution to make two separate drawdowns from the investment portfolio to cover benefit payments for the upcoming year. $500,000 would be the initial drawdown while $900,000 would be taken out sometime during the middle of the year.

After the board paid a courtesy visit to the Speaker of the Kosrae State Legislature, Lyndon Jackson, they reviewed a recommendation from its investment consultant concerning one of its money managers, Missouri Valley Partners. Due to its unsatisfactory performance since being hired in 2003, the board decided to begin a manager search and have its consultant come up with 3 potential managers for the board to review in its next meeting.

Funding Status

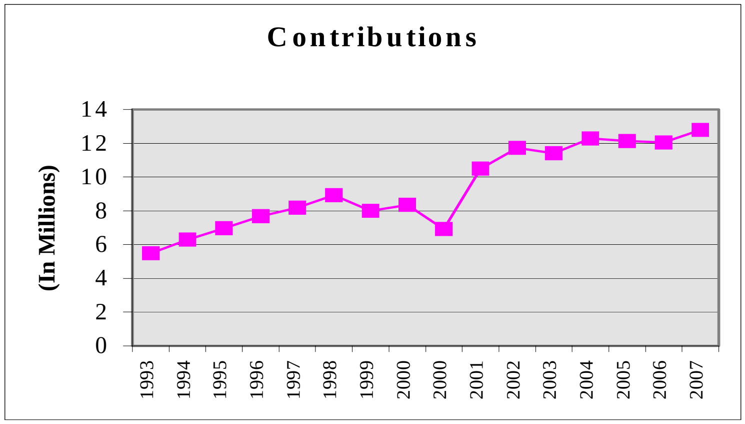
The Administration continues its efforts to ensure that collected contributions and investment income are sufficient to pay current benefits, meet administrative expenses, and reduce the unfunded accrued liability. The long term goal of the Administration is for the System to accumulate assets sufficient to guarantee that future benefit obligations will always be met.

The following graphs illustrate current and historical levels of contributions received as well as benefit payments and administrative expenses paid. The graphs also track the overall historical value of the investment and realized past investment performance.

Administrator's Report

Contributions

The Administration continues to initiate further tax audits of public and private sector employers in compliance with the Social Security Act.



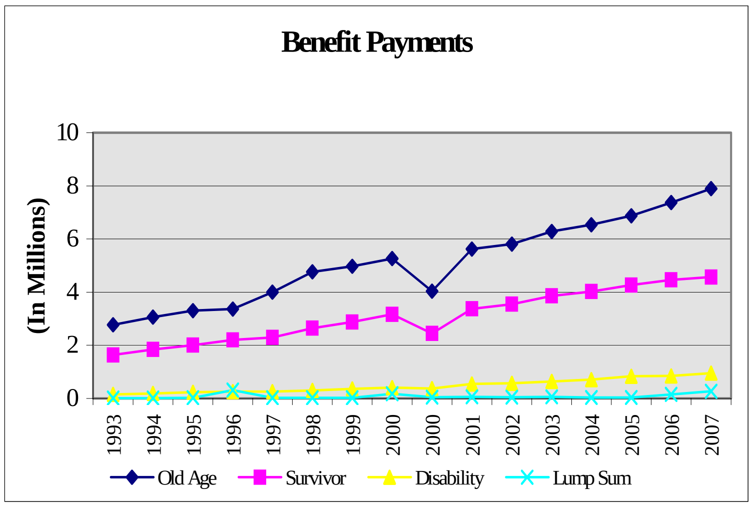
Contributions collected during fiscal year 2007 totaled $12,783,551, which is $733,563 higher than what was collected in the prior fiscal year.

The contributions were comprised of the following:

	Amount
Government	$6,992,581
Private	5,575,799
Judgment	16,226
Penalties and interest	198,945

Benefit Payments

A total of $13,663,880 was disbursed in benefit payments during fiscal year 2007. In addition, $20,088 was disbursed as refunds of contributions.

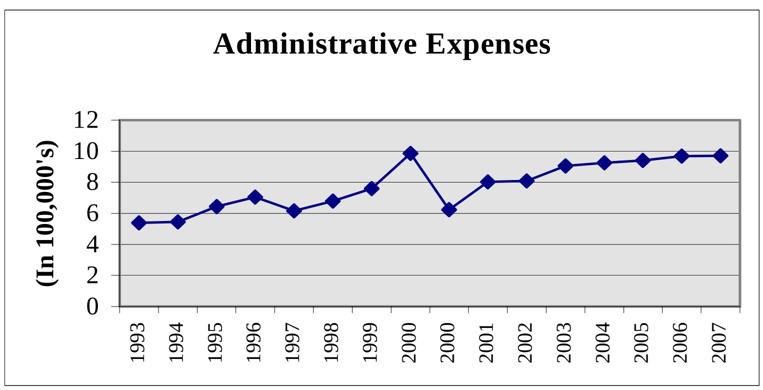


The following benefits were paid during fiscal year 2007:

Type	Amount
Old Age	$ 7,885,913
Survivor	$ 4,563,095
Disability	$ 947,870
Lump Sum	$ 267,002

Administrative Expenses

Net administrative expenses of $969,030 include a slight increase of 0.10% from the previous year.



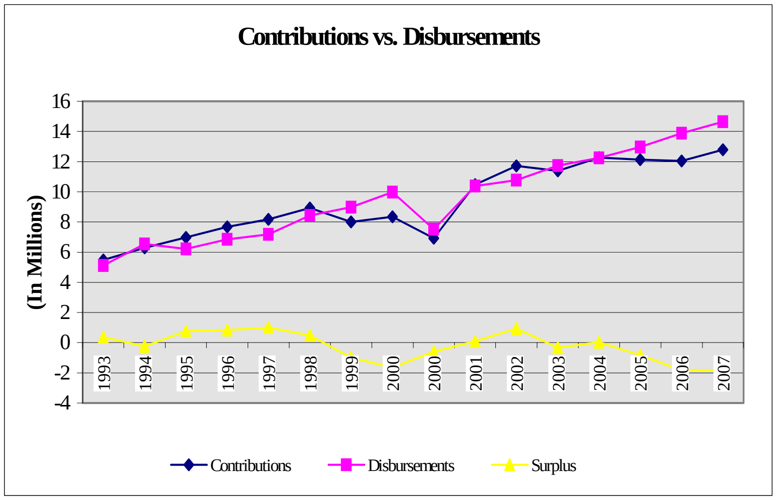
The administrative expenses were as follows:

Salaries and benefits	$550,562
Travel and training	110,839
Professional services	66,619
Other	241,010

Contributions and Disbursements

Contributions were deposited in a savings account at the Bank of FSM, which then funded the Bank of Guam checking accounts for benefit payments, payroll and operations.

For fiscal year 2007, disbursements exceeded contributions by 1,869,447 or 15%. For this comparison, disbursements represent payments to beneficiaries and payments for administrative expenses.

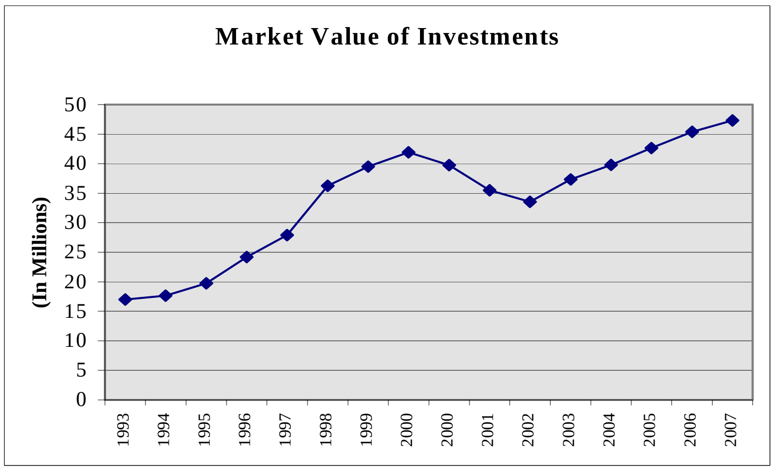


Investments

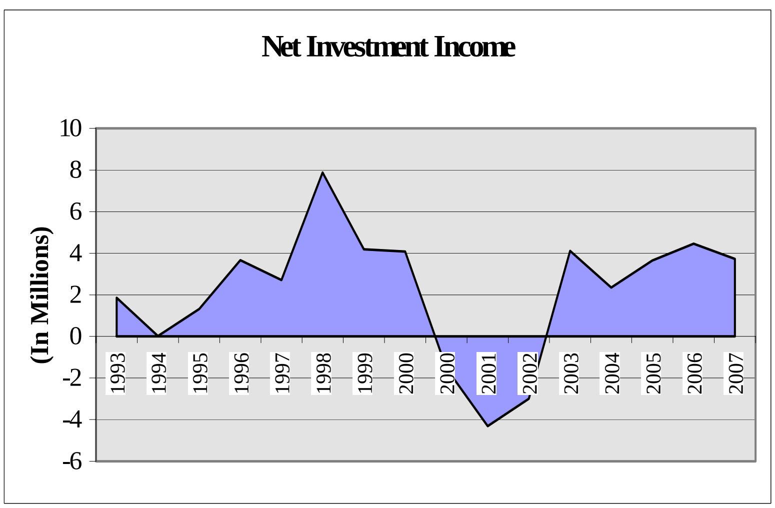
The Administration retained Smith Barney as its investment advisor, Atlanta Sosnoff Capital Corporation, Missouri Valley Partners, and Payden & Rygel as money managers and as custodial trustee.

The investment portfolio that included money market was valued at $43,356,178 at the end of year. The amount was $734,088 higher from the previous year's total of $42,622,090.

The FSMSSA does not own any time deposits at the local banks.



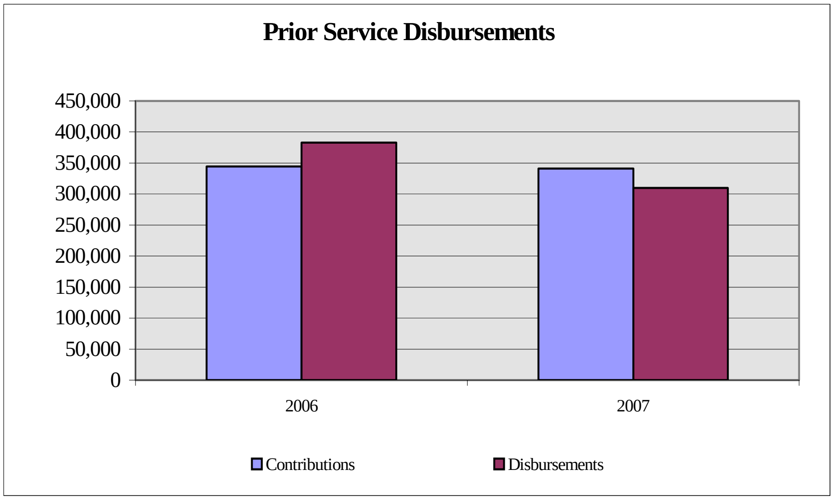
Compared from last year, net investment income decreased by 10% due to global volatile market and drawdown of $2.9 million to fund benefit payments and administrative expenses.



Administrator’s Report

Prior Service

For fiscal year 2007, reimbursements to FSMSSA from the Prior Service Benefits Trust Fund totaled $344,514. Disbursements exceeded reimbursements by $38,439. In fiscal year 2006 disbursements totaled $309,937 and reimbursements equaled $341,017.



Professional Service Providers

Actuary

Pacific Actuarial Services
205 W. Kansas Street
Liberty, MO 64068

Investment Advisor

Smith Barney
Citibank Building
402 East Marine Drive,
Suite 100
Agana, Guam 96910

Money Managers

Atlanta Sosnoff Capital Corporation
101 Park Avenue
New York, NY 10178

Missouri Valley Partners
P.O. Box 16901
135 N. Meramec, Suite 500
St. Louis, MO 63105

Payden & Rygel
333 South Grand Avenue
Los Angeles, CA 90071

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System Legislation

Effective January 1, 2007, the provisions of Public Law 14-86 were fully implemented. The principal provisions of this law are

- Added a fourth tier of 1.0% of total cumulative covered earnings in excess of $302,500 to the calculation of retirement and disability benefits that begin on or after January 1, 2007,
- Scheduled regular increases in the maximum quarterly covered wages in $1,000 increments from $5,000 to $10,000 on January 1, 2028,
- Increased the minimum monthly benefit from $50 to $75 and then $100 on January 1, 2012,
- Provides a new definition of "currently insured",
- Provided a new definition of "fully insured" which requires a minimum number of quarters and a minimum amount of contributions,
- Provides the Administration discretion when recognizing an adopted child,
- Allows for Voluntary contributions of 12% of $5,000.00 wages per year from citizens working abroad which will allow them to participate in the System on a voluntary basis, and
- Provides a lump sum payment to certain non-citizens equal to 100% of their contributions should they leave the FSM permanently.

Prior Service Benefits

The Prior Service Benefits Trust Fund (PSBTF) is a supplemental retirement, disability and survivors' plan established pursuant to Section 105(m) of U.S Public Law 99-239. It was established to continue to provide benefits to those who worked for the U.S. Navy Administration or the Government of the Trust Territory of the Pacific Islands for at least 5 years prior to July 1, 1968.

In 1987 the United States Congress provided $8 million for initial capitalization of the PSBTF. Pursuant to U.S. Public Law 99-239, future funding would be provided if warranted based on the results of actuarial valuations.

In the past six years there have been four appropriations used to pay benefits, the most recent coming from the United States Department of the Interior for $1.5 million which was received in March of 2005. These appropriations are used to reimburse beneficiaries for payments that were missed in the past due to insufficient funds, pay current benefit payments, and to cover administrative expenses.

Effective April 1, 2006, the Federated States of Micronesia Social Security Administration assumed responsibility for benefit payments made to citizens of the Federated States of Micronesia. During 2007 the Administration paid a total of $382,952 in Prior Service benefits and expenses and received $344,513 to pay these benefits and to meet associated administrative costs.

Administrator’s Report

Conclusion

The Administration continues to aggressively pursue its policy of collecting all contributions due and the newly acquired ability to waive interest penalties will help achieve this goal. The provisions of Public Law 14-86, especially the change to the benefit structure and the lump sum payments made to non-citizens who leave FSM, will help to stabalizestabilize and /or reduce the System liability and increase the funded status and aid in the future financial health of the system.

The FSMSSA continued to realize a positive return on invested assets for the fifth fiscal year in a row with total net investment income of $3,723,433 during 2007 which represented an 8.4% return for the year.

The Administration continued to pay more in benefits, refunds, and expenses than it collected in contributions during 2007 (now a three year trend), and as a result, the Administration was forced to liquidate trust assets to meet the deficit. Even though Public Law 14-86 was just recently passed, additional changes must be made to ensure the ongoing health of Social Security.

Acknowledgements

I would like to thank everyone whose hard work and dedication make Social Security a reality for the people of Micronesia. Through the continued efforts of the Congress and President, the Board of Trustees, and the Administration staff Social Security continues to promise security to the retired, disabled, and surviving spouses and children of the hard working men and women of Micronesia who make our economy grow and flourish.

This report is intended to be a complete and succinct summary of the FSMSSA as a basis for making management decisions, responsible management of the assets contributed by the members and their employers and as a preliminary means of evaluating the effects of legislation pertaining to the System. This report will be submitted to the President and Congress of the Federated States of Micronesia as well as other interested parties.

Alexander R. Narruhn
Administrator

Management’s Discussion and Analysis

The following discussion and analysis provides an understanding of the FSM Social Security System Administration’s (FSMSSA) financial performance for fiscal year ended December 31, 2007. 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 Board is duly represented by the following individuals:

Jack E. Yakana	State of Pohnpei	Chairman of the Board
Nahoy G. Selifis	National Government	Vice Chairman
Charles L. Chieng	State of Yap	Member
Garrison Irons	State of Chuuk	Member
Yosiwo George	State of Kosrae	Member
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 6% each, or a combined tax rate of 12% 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 1, 2008, the maximum quarterly taxable wage of $5,000 is subject to an increment of $1,000 and every 5 years thereafter for a maximum of $10,000 until January 1, 2028.

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 2007 based on projected income of $12 million was $1.32 million. However, as part of management’s cost cutting measures, the budget was streamlined at $1.04 million, which is 8.7% of the projected income.

Significant Events

- Effective January 1, 2007, the provisions of Public Law No. 14-86 were fully implemented. These are:
  - Raise to 55 years of age the limit on wage earners adopting children so children adopted after December 1, 2006 by wage earners who are 55 years or more would not be eligible for survivor benefits;
  - To be eligible, the minimum contribution of $2,500 is required for a retiree or individual who dies after December 31, 2006 and the minimum contribution of $1,500 for an individual who becomes disabled after December 31, 2006;
  - Raise the minimum monthly benefit from $50 to $75;
  - FSM citizens working abroad may participate in the Program through voluntary contributions of 12% of $5,000 wages per year; and
  - Lump sum equal to employee's share shall be paid to non-citizens of the USA, Palau and Marshall Islands when they decide to leave the FSM permanently.

- On November 2007, the FSMSSA participated at the annual network of the Freely Associated Social Security Administrators from the Republic of Marshall Islands and the Republic of Palau. The conference/workshop focused on performance updates on investments, accounting, tax collections, claims and benefits, enhancements to the database software, and other challenges faced by the three Social Security Administrations.

- 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 2007, total funds received from the Prior Service Trust Fund Administration (PSTFA) amounted to $344,514 while benefits paid and administrative expenses totaled $313,995 and $68,957 respectively.

Management's Discussion and Analysis

Financial Highlights

- Net assets for the retirement fund (non-inclusive of the Prior Service Fund) increased by $1.95 million or 4% from fiscal year 2006. The increase is mainly due to the positive performance of investments.

Statement of Net Assets (Retirement Fund)

	2007	2006	2005
ASSETS			
Cash and equivalents	$ 4,298,083	$ 1,417,209	$ 2,873,476
Investments	39,618,679	41,806,275	37,809,060
Other current assets	3,468,620	2,220,018	1,970,466
Fixed assets, net	85,352	71,988	79,944
Total	$ 47,470,734	$ 45,515,490	$ 42,732,946
LIABILITIES	$ 149,227	$ 140,269	$ 75,884
NET ASSETS			
Held in trust for retirement, disability and survivors' benefit	$ 47,321,507	$ 45,375,221	$ 42,657,062

- The investment income absorbed the impact of the 2007 operating deficit of $1.78 million as a result of lower contributions against benefit payments and administrative expenses.

Statement of Changes in Net Assets (Retirement Fund)

	2007	2006	2005
Contributions	$ 12,783,551	$ 12,049,988	$ 12,129,796
Benefit Payments	(13,663,880)	(12,586,560)	(12,006,929)
Admin Expenses	(969,029)	(968,012)	(940,444)
Other	72,212	80,518	43,804
Operating deficit	$ (1,777,147)	$ (1,424,066)	$ (773,773)
Investment Income	3,723,433	4,142,225	3,648,998
Change in Net Assets	$ 1,946,286	$ 2,718,159	$ 2,875,225
Net Assets, beginning	45,375,221	42,657,062	39,781,837
Net Assets, ending	$ 47,321,507	$ 45,375,221	$ 42,657,062

- The investment portfolio is up by $734,088 or 1.7% from the previous year's balance of $42,622,090. Net investment income decreased this year by 10% due to global volatile market and drawdown of $2.9 million to fund benefit payments and administrative expenses.

Retirement Fund	**2007**	**2006**	**2005**
Investment*	$ 43,356,178	$ 42,622,090	$ 39,675,318
Investment Income	$ 3,723,433	$ 4,142,225	$ 3,648,998
Investment Withdrawals	$ 2,900,000	$ 1,250,000	
*includes cash management fund			

- Total delinquent taxes collected for FY 2007, excluding $1.2 million from the Chuuk State Government, amounted to $1.9 million.

Contributions	**2007**	**2006**	**2005**
Government	$ 6,992,581	$ 6,388,593	$ 6,292,337
Private	5,575,798	5,398,825	5,662,080
Judgment	16,226	63,990	16,320
Penalties and interest	198,945	198,580	159,059
Total	$ 12,783,550	$ 12,049,988	$ 12,129,796

- Benefit payments were 9% higher due to increased number of beneficiaries that averaged 6,429 monthly compared to 6,363 for FY 2006.

Benefit Payments	**2007**	**2006**	**2005)**
Retirement	$ 7,885,913	$ 7,251,790	$ 6,870,291
Survivors	4,563,095	4,339,471	4,269,263
Disability	947,870	841,012	830,813
Lump Sum	267,002	154,287	36,562
Total	$ 13,663,880	$ 12,586,560	$ 12,006,929

- Actual administrative expenses were 7% lower than the approved budget and 27% less than the budget ceiling.

Budget	**Approved**	**Actual**	**Surplus**	**%**
2007	$ 1,039,581	$ 969,029	$ 70,552	7%
2006	$ 1,007,412	$ 968,012	$ 39,400	4%

- For additional information on FSMSSA's fixed assets, please refer to note 2F of the financial statements.

- As of FY 2007, the Prior Service Fund has net liabilities of $4,291. Reimbursements increased by 1% while benefit payments increased by 30%. The PS Fund commenced in April 2006, hence lower disbursements for FY 2006.

Statement of Net Assets
(Prior Service Fund)

	2007	2006	Inc(dec)	%
ASSETS	$ 30,378	$ 139,766	$ (109,388)	-78%
LIABILITIES	$ (34,669)	$ (107,350)	$ (72,681)	-68%
NET ASSETS	$ (4,291)	$ 32,416	$ (36,707)	-113%

Statement of Changes in Net Assets
((Prior Service Fund)

	2007	2006	Inc(dec)	%
PSTFA Reimbursements	$ 344,514	$ 341,017	$ 3,497	1%
Benefit Payments	(313,995)	(241,696)	72,299	30%
Admin Expenses	(68,957)	(68,241)	716	1%
Other	1,732	1,336		
Change in Net Assets	$ (36,707)	$ 32,416		
Net Assets, beginning of year	32,416	-		
Net Assets, end of year	$ (4,291)	$ 32,416	$ (36,707)	-113%

Management's Discussion and Analysis for the year ended December 31, 2006 is set forth in the report on the audit of the FSMSSA's financial statements, which is dated April 27, 2007. That Discussion and Analysis explains the major factors impacting the 2006 financial statements.

Conclusion:

The FSMSSA retirement fund posted net assets increase of $1.95 million and $2.7 million for fiscal years 2007 and 2006 respectively. However, management was prompted to redeem $2.9 million and $1.25 million from the investment portfolio for fiscal years 2007 and 2006 respectively, to sustain lower tax collections against increasing benefit payments and administrative expenses.

With increased benefit payments of 9% and 5% respectively for fiscal years 2007 and 2006, and unfunded accrued liability of $219.5 million (as of Jan 1, 2006), management endeavors to improve its operation through the following:

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

Significantly, management continues to lobby legislation for proposed amendments to the Social Security Act. Public hearings are ongoing for Congressional Bill No. 15-52 that propose the following:

1. Clarify the definition of "employer" whether it is an individual, a partnership, a corporation, a municipal or state organization or agency thereof, or any other type of business or non-business organization and its responsibilities as far as social security taxes are concerned.

2. Individuals who attain age 60 or die after December 31, 2007, must earn at least 50 quarters of coverage and have contributed at least $2,500 to the Social Security System to be fully insured for death or old age benefits.

3. Individuals who become disabled on or after January 1, 2008, must earn at least 45 quarters of coverage and have contributed at least $1,500 to the Social Security System to be fully insured for disability benefits.

4. Individuals who become disabled on or after January 1, 2008, must also meet the definition of currently insured to qualify for a disability benefit.

5. Violations, Penalties and interest, Attorney's fees and costs
   - Impose criminal penalties on an employer for failure to pay taxes.
   - Identify the chief financial officer of a state or municipal government or any agency thereof as the individual liable to the program.

6. Lien for taxes: All taxes, including penalties and interest accrued thereon, imposed or authorized under this subtitle and owed by a state or municipal government, or any agency thereof, shall be subject to a writ of garnishment of all moneys owed by the FSM National Government to any state or municipal government or any agency thereof, and such writ of garnishment shall have priority over any claim for such moneys in any manner by the particular state or municipal government or agency thereof.

7. Limit surviving child's benefit to age 20 for students.

8. Retirement benefits that begin on or after January 1, 2008, that are paid to individuals aged 60 to 64 are reduced by 50% until the retiree attains age 65, at which time the benefit will automatically be adjusted to what it would have been prior to the 50% reduction. Reduced payments are not subject to the earnings test. In other words, a retiree

aged 60 to 64 will receive 50% of his/her calculated retirement benefit while still working full-time.

9. Fully insured individuals who are also citizens of the Federated States of Micronesia may elect to receive a lump sum payment equal to all amounts contributed by him or her at the time of application for this lump sum, which will be paid when the individual attains age 60. Upon election of the lump sum the individual shall forfeit credit for all quarters of coverage earned up to the date of application. If the lump sum is greater than $5,000, the payment will be divided into 6 month payments. If the lump sum is greater than $10,000, the lump sum payment will be divided into 12 month payments.

10. For retirement benefit payments that begin or continue after January 1, 2008, the Administration will pay a retirement benefit as calculated in section 804 until the sum of retirement benefits paid to the retiree exceeds the total of amounts received by the Administration under sections 901 and 902 on behalf of the retiree. In the calendar year following this event, the retiree's monthly retirement benefit shall be reduced by 30%. This reduction will not apply to any disability benefits as calculated in section 804 and paid under section 803A nor will it apply to any survivor benefits paid under section 806.

11. Increase the tax rate paid by employees and employers to 7% each on October 1, 2008, and then to 7.5% each on October 1, 2012.

12. To enable the FSMSSA to invest in BBB investment grade bonds.

13. To allow for investments in the international market but only with those who exchange their currency in American Depository Receipts.

14. Concerning preferred and common stocks in the investment act:
    - To increase the market value of the fund that may be invested in the stock of any one corporation from five to ten percent.
    - To increase the market value of the fund that may be invested in any one industry group from ten to twenty-five percent.
    - To create a security measure so that shares are invested and actively traded only on a recognized national or regional stock exchange. (To be expanded to allow for investments in the local economy.)

15. To establish an FSM Social Security Credit Union which could then invest locally by making loans and taking deposits. The establishment of such a credit union can be accomplished by Board action and through the issuance of regulations.

Summary of Principal System Provisions

Applicable Laws

Public Law 2-74, as amended by Public Laws 5-120, 6-111, 7-118, 7-119,7-120, 9-56, 12-51, 12-76, 14-37, and 14-86

Workers and Employer's Contributions

Workers, self-employed workers and employers each pay 6% of earnings up to a maximum of $5,000 of earnings per quarter.

Self-employed with employees - remuneration shall be deemed to be twice the amount paid to the highest paid employee reported by the self-employed person in quarter, up to $5,000 taxable per quarter.

Self-employed with no employees- Remuneration is deemed to be 2.5% of the gross revenue of the business for the previous calendar year subject to $5,000 taxable per quarter.

Coverage

All employees employed by an employer incorporated or doing business in the Federated States of Micronesia are covered unless both the employer and employee are currently subject to another recognized social security system.

Eligibility for and Computation of Benefits is based on the following definitions:

Quarters of Coverage: A calendar quarter in which contributions were made for at least $50 of earnings.

Currently Insured: Credited with at least 20 quarters of coverage during the most recent previous 25 calendar quarters.

Fully Insured: Credited with at least one quarter of coverage for each year since the later of attainment of age 21 or June 30, 1968 and having not less than 12 quarters of coverage. No more than 50 quarters are required for Fully Insured status.

Maximum Covered Earnings: Earnings up to a maximum of $5,000 each quarter. Effective January 1, 2008, the maximum covered earnings increases to $6,000, January 1, 2013 - $7,000, January 1, 2018 - $8,000, January 1, 2023 - $9,000 and January 1, 2028 - $10,000.

Minimum Benefit: $75 per month. Effective January 1, 2012, the minimum benefit increases to $100.

Basic Benefit

A worker's Basic Benefit is calculated as 1/12 of:

1. 16.5% of the first $10,000 of total Maximum Covered Earnings for which contributions have been made, plus

2. 3.0% of the next $30,000 of total Maximum Covered Earnings for which contributions have been made, plus

3. 2.0% of the next $262,500 of total Maximum Covered Earnings for which contributions have been made, plus

4. 1.0% of total Maximum Covered Earnings in excess of $302,500 for which contributions have been made.

Old Age Insurance Benefit

Eligibility: Age 60 and Fully Insured

Amount: Greater of the Basic Benefit and the Minimum Benefit, subject to the earnings test.

Disability Insurance Benefit

Eligibility: Disabled for three months and Fully Insured at time of disability

Amount: Unreduced Basic Benefit earned at time of disability. Sum of disability benefit and workers compensation benefit may not exceed 80% of the highest covered compensation earned in the year of disability and the prior five years. The benefit ceases should the worker recover from the disability.

Surviving Spouse Benefit

Eligibility: Worker must have been Fully Insured at time of death.

Amount: 60% of the Basic Benefit earned at the time of death, subject to the earnings test. Paid until the earlier of the date the spouse remarries or dies. This benefit is reduced by any Old Age Insurance Benefit that the spouse may be entitled to based on his or her own earnings history.

Surviving Child Benefit

Eligibility: Worker must have been Fully or Currently Insured at time of death.

Amount: 15% of the Basic Benefit for each dependent child under the age of 18 or 22 if a student. The benefit ceases if the child marries or is adopted by a close relative.

The minimum total survivor benefit is $75 per month and is subject to the Earnings Test.

The sum of all survivors' benefits cannot exceed 100% of the Basic Benefit earned at the time of death.

Payment to Foreign Citizens residing outside the FSM

Payments to citizens and nationals of the Republic of Palau, the Republic of the Marshall Islands and the United States shall be made as if they were citizens or nationals of the Federated States of Micronesia as long as those nations give citizens and nationals of the Federated States of Micronesia reciprocal treatment. For citizens and nationals of other countries, a lump sum payment equal to total worker paid contributions as of the date the worker turned age 60, became disabled, or died. The lump sum payment is reduced by any payments already made to the employee, surviving spouse or child before the lump sum is paid.

Lump Sum Death Benefit

Eligibility: After the death of any covered worker and rights to all survivors' benefits have ceased.

Amount: Four percent of total Maximum Covered Earnings for which contributions have been paid, less the value of any benefits already paid.

Lump Sum Benefit (other than death)

Eligibility: Age 60 and not fully insured, native born citizen of the Federated States of Micronesia or resident for at least 10 years and must have lived in the Federated States of Micronesia for at least one year immediately preceding death.

Amount: Four percent of total Maximum Covered Earnings for which contributions have been paid.

Earnings Test

Benefits are reduced by $1 for every $2 of earnings in excess of $300 received each quarter.

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