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, 2011 AND 2010

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

Years Ended December 31, 2011 and 2010
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INDEPENDENT AUDITORS' REPORT

Board of Trustees
FSM Social Security Administration:

We have audited the accompanying statements of net assets of the Federated States of Micronesia (FSM) Social Security Administration (the Administration), a component unit of the FSM National Government, as of December 31, 2011 and 2010, and the related statements of changes in net assets for the years then ended. These financial statements are the responsibility of the Administration's management. 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 *Governmental 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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Administration's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial status of the Administration as of December 31, 2011 and 2010, and the changes in financial status for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 9 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This information is the responsibility of the Administration's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 15, 2012, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental Combining Statement of Net Assets and Combining Statement of Changes in Net Assets on pages 23 and 24 are presented for the purpose of additional analysis and are not a required part of the financial statements. This supplementary information is the responsibility of the Administration's management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated in all material respects in relation to the financial statements as a whole.

Deloitte + Touche LLP

June 15, 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, 2011. 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 in 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 of Trustees was reorganized on February 01, 2011. The new members and officers of the Board of Trustees are as follows:

Rose N. Nakanaga	State of Pohnpei	Chairwoman of the Board
VACANT	State of Kosrae	Member
Gillian Doone	National Government	Member
Innocente Oneisom	State of Chuuk	Vice-Chairman
VACANT	State of Yap	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 7% each, or a combined tax rate of 14% 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. Effective January 01, 2013, both the tax rate and the maximum quarterly taxable wage will increase 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 2011, based on projected income of $13.80 million, was $1.52 million. However, as part of management's cost cutting measures, the budget was streamlined at $1.06 million which is 7.7% of the projected income. The actual administrative costs incurred for FY2011 was $1.03 million, or a 3% surplus compared to the approved budget.

HIGHLIGHTS

- Contributions collected increased by 14.17% from $14.53 million the previous year to $16.59 million in 2011.

- Total benefit payments to members or their beneficiaries increased by 5.34% from $16.49 million in 2010 to $17.37 million in 2011.

- 6.49 thousand FSM citizens received Social Security benefits in fiscal year 2011.

- 7.54 hundred retirement, survivor and disability claims were received, processed, and approved in fiscal year 2011.

- In FY2011, we processed and posted more than $108.28 million in reports of earnings to individual records.

- Investment portfolio decreased by 4.58% from $36.91 million to $35.22 million.

- Collected $0.3 million in funding from the FSM National Government, which was used to supplement benefit payments.

- Net assets totaled $40.38 million on December 31, 2011, compared to $42.36 million in FY2010; a decrease of 4.67%.

- Social Security tax rates increased from 6% to 7% (both employee and employer) effective October 01, 2010 as mandated by PL15-73

- New retirement eligibility became effective January 01, 2011 as mandated by PL15-73 whereby individuals receive 50% of their calculated benefit from age 60 to 64 and 100% from age 65.

- $1.24 million from delinquent accounts were collected in fiscal year 2011.

- Close monitoring of expenses led to a budget surplus of 3% in fiscal year 2011.

RESULTS OF OPERATIONS / CHANGES IN NET ASSETS

FSMSSA follows the calendar year as its fiscal year. The following table presents information about FSMSSA results of operations for CY2011, 2010 and 2009.

	2011	2010	2009
Contributions	$ 16,593,155	$ 14,525,608	$ 12,955,409
Benefit Payments	(17,366,480)	(16,488,738)	(15,304,704)
Admin Expenses	(1,032,036)	(946,951)	(961,778)
Other Income	1,247,807	1,543,882	1,190,244
Operating Deficit	(557,554)	(1,366,199)	(2,120,829)
Investment Income/(Loss), net	(1,421,047)	2,981,703	6,149,139
Change in Net Assets	(1,978,601)	1,615,504	4,028,310
Net Assets at beginning of year	42,361,070	40,745,566	36,717,256
Net Assets at end of year	$ 40,382,469	$ 42,361,070	$ 40,745,566

CONTRIBUTIONS

	2011	2010	2009
Government	$ 7,495,281	$ 6,690,931	$ 6,827,298
Private	8,772,936	7,566,503	5,967,099
Judgment	82,192	44,201	14,887
Penalties & Interest	242,746	223,973	146,125
Total	$ 16,593,155	$ 14,525,608	$ 12,955,409

The total amount of contributions collected was $16.59 million, averaging a collection of $4.15 million per quarter. This is an increase of 14.17% from the previous year's collection of $14.53 million. The increase was attributed mainly to the increase tax rate of 2% (employee 1% and employer 1%) effective October 01, 2010 and to the collection of delinquent accounts from prior years.

Total delinquent taxes collected in 2011 totaled $1.24 million. Of this amount, 65% or $814 thousand pertains to the prior years.

BENEFIT PAYMENTS

	2011	2010	2009
Retirement	$ 10,870,989	$ 10,137,489	$ 9,188,597
Survivors	4,881,958	4,738,969	4,646,298
Disability	1,395,552	1,356,728	1,264,648
Lump Sum	217,981	255,552	205,161
Total	$ 17,366,480	$ 16,488,738	$ 15,304,704

Benefit payments increased by 5.34% from $16.49 million in 2010 to $17.37 million in 2011. The increase was attributed mainly to the increased number of beneficiaries. Six thousand four hundred ninety two (6,492) members or their beneficiaries received benefits in fiscal year 2011. Of this number, seven hundred fifty four new claims were received, processed and approved during the year.

ADMINISTRATIVE EXPENSE

	2011	2010	2009
Budget	$ 1,063,046	$ 1,069,053	$ 1,149,058
Actual	$ 1,032,036	$ 946,951	$ 961,778
Surplus	$ 31,010	$ 122,102	$ 187,280
% of Budget	3%	11%	16%

Administrative expense increased by 8.2% from $946.95 thousand in 2010 to $1.032 million in 2011. The increase was attributed mainly to two items namely, the cost to upgrade HQ's main server and computer hardware and also the cost of an actuarial valuation which is scheduled every two years. For additional information concerning capital assets, please see note 2F to the financial statements. Aside from these two expense accounts, there were no items individually material in comparison to the previous year. Management enforced several approaches to reduce the System's operating costs. Continuous monitoring of fuel, telephone and communication, utilities, and supplies and materials were in place to reduce costs. As a result, a budget surplus of 3% or $31 thousand was attained this year.

INVESTMENT INCOME/(LOSS)

	2011	2010	2009
Investments	$35,220,871	$36,910,189	$36,409,513
Income/(Loss)	$(1,421,047)	$ 2,981,702	$ 6,149,533
Drawdowns	$ 500,000	$ 2,000,000	$ 3,000,000

Investment income decreased by 147.65% from $2.98 million net gain in 2010 to a $1.42 million net loss in 2011. The loss was attributed to underperformance of the equity investment. A total of $0.5 million was withdrawn from the investment portfolio in fiscal year 2011 to supplement benefit payments in addition to the $0.3 million of cash funding received from the FSM National Government.

OTHER INCOME

	2011	2010	2009
Approp. from FSM Govt.	$ 1,200,000	$ 1,495,000	$ 1,150,000
Prior Service reimbursement	35,359	33,834	24,140
Miscellaneous receipts	43,356	35,112	33,514
Total	$ 1,278,715	$ 1,563,946	$ 1,207,654

Other Income decreased by 18.1% from $1.56 million in 2010 to $1.278 million in 2011. The decrease was attributed mainly to appropriations received from the FSM National Government. Out of $1.2 million appropriation for 2012, only $0.3 million was collected by end of year 2011. The remaining $0.9 million is to be released on a quarterly basis at $0.3 million each quarter.

NET ASSETS

FSMSSA Statements of Net Assets as of December 31, 2011, 2010 and 2009 follows:

	2011	2010	2009
Assets			
Cash and equivalents	$ 1,209,552	$ 2,780,258	$ 1,600,034
Investments	35,220,871	36,910,189	36,409,513
Other current assets	4,059,782	2,770,894	2,831,584
Fixed assets, net	109,787	77,190	66,491
Total	40,599,992	42,538,531	40,907,622
Liabilities	217,523	177,461	162,056
Net Assets			
Held in trust for retirement,			
Disability and survivors; benefit	$ 40,382,469	$ 42,361,070	$ 40,745,566

Net assets for the retirement fund (excluding the Prior Service Fund) decreased 4.90% from $42.36 million in 2010 to $40.38 million in 2011. The decrease was attributed to investment losses as well as an operating deficit as a result of higher benefit payments as compared to collected contributions.

The FSMSSA continues to manage the Prior Service Benefits Program for FSM citizens, which is funded by the U.S. Department of the Interior, Office of Insular Affairs. For FY 2011, total funds received from the Prior Service Trust Fund Administration (PSTFA) amounted to $272.80 thousand while benefits paid and administrative expenses totaled $253.76 thousand and $35.40 thousand, respectively.

As of December 31, 2011, the Prior Service Fund had net assets of $26.90 thousand. Contributions increased by 205.50% while benefit payments decreased by 6.50%.

Following are the Statements of Net Assets as of December 31, 2011, 2010, and 2009 and Statements of Changes in Net Assets for the years ended December 31, 2011, 2010, and 2009 of PSTFA.

Statements of Net Assets
(Prior Service fund)

	2011	2010	2009
Assets	$ 70,650	$ 86,139	$ 295,261
Liabilities	(43,750)	(43,104)	(37,382)
Net assets	$ 26,900	$ 43,035	$ 257,879

Statements of Changes in Net Assets
(Prior Service Fund)

	2011	2010	2009
PSTFA contributions	$ 272,797	$ 89,593	$ 445,052
Benefit Payments	(253,765)	(271,407)	(282,835)
Admin expenses	(35,398)	(33,844)	(24,171)
Other	231	814	694
Change in net assets	(16,135)	(214,843)	138,740
Net assets at beginning of year	43,035	257,879	119,139
Net assets at end of year	$ 26,900	$ 43,035	$ 257,879

CONCLUSION:

Fiscal Year 2011 saw a decrease in retirement fund net assets. The investment portfolio decreased 4.58% due to the underperformance of the equity investment. $500,000 has to be withdrawn also from the investment funds to supplement benefits payment, which grew 5.32% during the fiscal year. In addition to the investment funds withdrawal, a total amount of $300,000 was received from the FSM National Government in December as part of the $1.2 million total appropriation for CY2012 and this amount was also used to pay benefits for that month.

While contributions increased, disbursements also increased resulting in an operating deficit during the year. Contributions increased 14.17% as a result of the 2% tax rate increase and collections of delinquent accounts. However, increased collections were not enough to cover benefit payments and administrative expenses.

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 2011, we have managed to recover over $1.24 million in delinquent taxes, which is an achievement considering the slow economic growth in the FSM.

With increased benefit payments of 5.34% and 7.73% respectively for fiscal years 2011 and 2010, and an 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.

Management's Discussion and Analysis for the year ended December 31, 2010 is set forth in the report on the audit of FSMSSA's financial statements, which is dated April 27, 2011. That Discussion and Analysis explains the major factors impacting the 2010 financial statements and may be obtained from the contact information below.

2012 OUTLOOK

Collections are again expected to increase in 2012 with $17.4 million of total projected collections by the end of year including collections of delinquent accounts. However, the expected increase could be partially offset by non-compliance with contribution payments from some employers, which was experienced in 2011 despite new criminal penalties for employer offenders of FSM Social Security Act as recently mandated by PL15-73.

Benefit payments are also expected to increase by 5% for a total of $18.2 million of benefits paid by the end of the year. The projected increase is largely due to additional beneficiaries who will become eligible for benefits in 2012.

Administrative cost is projected to be lower if not approximately equal compared to 2011. Management will continue to implement cost cutting measures practiced during the past several years.

Foregoing, benefit payments will increase faster than collections. It is projected that at least $1.8 million will be needed in additional funding to supplement benefit payments and administrative expenses in 2012. 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.

FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
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Statements of Net Assets
December 31, 2011 and 2010

ASSETS	2011	2010
Cash and cash equivalents	$ 1,280,202	$ 2,866,397
Receivables:		
Contributions	3,051,613	2,642,239
Due from FSM National Government	900,000	-
Accrued interest	91,721	112,357
Other	11,668	12,698
Total receivables	4,055,002	2,767,294
Prepayments	4,780	3,600
Investments:		
Fixed income	13,384,226	13,676,610
Stocks	21,836,645	23,233,579
Total investments	35,220,871	36,910,189
Fixed assets, net	109,787	77,190
Total assets	40,670,642	42,624,670
LIABILITIES		
Accounts payable	230,235	187,536
Other liabilities and accruals	22,598	24,079
Accrued management fees	8,440	8,950
Total liabilities	261,273	220,565
Contingencies		
NET ASSETS		
Held in trust for retirement, disability and survivors' benefits	$ 40,409,369	$ 42,404,105

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
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Statements of Changes in Net Assets
Years Ended December 31, 2011 and 2010

	2011	2010
Additions:		
Contributions	$ 16,593,155	$ 14,525,608
Investment income (loss):		
Net change in the fair value of investments	(2,181,438)	2,314,631
Interest and dividends	969,271	866,970
Total investment income (loss)	(1,212,167)	3,181,601
Less investment expense:		
Investment management and custodial fees	(208,649)	(199,085)
Net investment income (loss)	(1,420,816)	2,982,516
Other additions:		
Contributions from FSM National Government	1,200,000	1,495,000
Other	351,234	158,539
	1,551,234	1,653,539
Total additions	16,723,573	19,161,663
Deductions:		
Benefit payments:		
Retirement	10,973,220	10,250,648
Survivors	5,033,492	4,897,217
Disability	1,395,552	1,356,728
Lump sum	217,981	255,552
Total benefit payments	17,620,245	16,760,145
Refunds	30,630	20,064
Administrative	1,067,434	980,794
Total deductions	18,718,309	17,761,003
Change in net assets	(1,994,736)	1,400,660
Net assets at beginning of year	42,404,105	41,003,445
Net assets at end of year	$ 40,409,369	$ 42,404,105

See accompanying notes to financial statements.

(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, all net assets of the Administration are 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 net assets, 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.

(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

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

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.

(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Deposits:

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1	Deposits that are federally insured or collateralized with securities held by the Administration or its agent in the Administration's name;
Category 2	Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the Administration's name; or
Category 3	Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the Administration's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. 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, 2011 and 2010, the carrying amount of the Administration's total cash and cash equivalents was $1,280,202 and $2,866,397, respectively, and the corresponding bank balances were $1,539,638 and $3,025,893, respectively. As of December 31, 2011 and 2010, bank deposits in the amount of $831,696 and $2,076,254, respectively, were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2011 and 2010, bank deposits in the amount of $500,000 and $527,093, 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 $728,000 and $949,579, 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, 2011 and 2010.

(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Investments:

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 Investments that are insured or registered, or securities held by the Administration or its agent in the Administration's name;

Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the Administration's name; or

Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the Administration's name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

As of December 31, 2011 and 2010, investments at fair value are as follows:

	2011	2010
Fixed income securities:		
Domestic fixed income	$ 13,384,226	$ 13,676,610
	13,384,226	13,676,610
Other investments:		
Domestic equities	16,403,466	19,354,905
International equities	5,433,179	3,878,674
	$ 35,220,871	$ 36,910,189

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.

(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Investments, Continued:

As of December 31, 2011, the Administration's investments in debt securities were as follows:

	Investment Maturities (In Years)				
	Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	$ 599,976	$ 626,392	$ 121,369	$ 643,337	$ 1,991,075
Mortgage and asset-backed securities	-	100,912	483,225	4,882,302	5,466,439
Corporate notes and bonds	204,263	2,163,290	2,110,852	1,448,308	5,926,712
	$ 804,239	$ 2,890,594	$ 2,715,446	$ 6,973,947	$ 13,384,226

As of December 31, 2010, the Administration's investments in debt securities were as follows:

	Investment Maturities (In Years)				
	Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	$ 1,328,904	$ 284,792	$ 1,112,006	$ 726,160	$ 3,451,862
Mortgage and asset-backed securities	-	407,856	-	-	407,856
U.S. Government agencies	-	-	524,031	3,230,033	3,754,064
Corporate notes and bonds	205,320	2,264,456	2,843,668	749,384	6,062,828
	$ 1,534,224	$ 2,957,104	$ 4,479,705	$ 4,705,577	$ 13,676,610

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, 2011, was as follows:

Standard and Poors' Rating	Domestic
AAA	$ 7,326,042
AA+	355,619
AA	387,237
AA-	58,464
A+	621,433
A	981,869
A-	1,361,560
BBB+	756,140
BBB	1,243,834
BBB-	292,028
	$ 13,384,226

(2) Summary of Significant Accounting Policies, Continued

E. Deposits and Investments, Continued

Investments, Continued:

The Administration's exposure to credit risk at December 31, 2010, was as follows:

Standard and Poors' Rating	Domestic
AAA	$ 7,754,437
AA+	436,986
AA	462,100
AA-	138,734
A+	297,546
A	1,503,804
A-	737,228
BBB+	971,204
BBB	782,073
BBB-	592,498
	$ 13,676,610

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, 2011 and 2010. 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, 2011 and 2010.

F. 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.

(2) Summary of Significant Accounting Policies, Continued

F. Fixed Assets, Continued

Capital asset activity for the years ended December 31, 2011 and 2010, was as follows:

	Estimated Useful Lives	January 1, 2011	Additions	Retirements	December 31, 2011
Motor vehicles	5 years	$ 105,193	$ 720	$ -	$ 105,913
Computer software and hardware	5 years	123,873	55,603	(11,068)	168,408
Office furniture, fixtures and equipment	5 years	88,963	4,875	(29,267)	64,571
Home furnishings	5 years	7,308	-	(570)	6,738
		325,337	61,198	(40,905)	345,630
Less accumulated depreciation		(248,147)	(28,601)	40,905	(235,843)
		$ 77,190	$ 32,597	$ -	$ 109,787

	Estimated Useful Lives	January 1, 2010	Additions	Retirements	December 31, 2010
Motor vehicles	5 years	$ 128,158	$ 22,800	$ (45,765)	$ 105,193
Computer software and hardware	5 years	119,183	4,690	-	123,873
Office furniture, fixtures and equipment	5 years	82,513	6,450	-	88,963
Home furnishings	5 years	3,791	3,517	-	7,308
		333,645	37,457	(45,765)	325,337
Less accumulated depreciation		(267,154)	(26,275)	45,282	(248,147)
		$ 66,491	$ 11,182	$ (483)	$ 77,190

G. 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.

Maximum quarterly taxable wages are currently $6,000. Every employer is required to contribute an amount equal to that contributed by employees.

Contribution revenues received during the years ended December 31, 2011 and 2010 are comprised of the following:

	2011	2010
Government employment	$ 7,495,281	$ 6,690,931
Private employment	8,772,936	7,566,503
Judgment	82,192	44,201
Penalties and interest	242,746	223,973
	$ 16,593,155	$ 14,525,608

(2) Summary of Significant Accounting Policies, Continued

H. 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, 2011 and 2010, the minimum monthly benefit payment is $75.

I. New Accounting Standards

During fiscal year 2011, the Administration implemented the following pronouncements:

- GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions.

- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools.

- The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

- In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to measurement of OPEB obligations by certain employers participating in agent multiple-employer OPEB plans. The provisions of Statement 57 related to the use and reporting of the alternative measurement method are effective immediately. The provisions related to the frequency and timing of measurements are effective for actuarial valuations first used to report funded status information in OPEB plan financial statements for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

(2) Summary of Significant Accounting Policies, Continued

I. New Accounting Standards, Continued

- In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

- In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus,* which is designed to improve 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 provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

- In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements,* which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

- In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

- In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions (an amendment of GASB Statement No. 53)*, which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The provisions of this statement are effective for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Administration.

(2) Summary of Significant Accounting Policies, Continued

K. Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America require management to make estimates and assumptions that affect the reported amounts of net assets 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.

L. 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 Assets Held in Trust

Net assets are held in trust to comply with the Social Security Act of 1983. All net assets of the Administration are 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.

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, 2011 and 2010, the Administration recorded total fund equity of $40,409,369 and $42,404,105, 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) Contribution from the 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, 2011 and 2010, contributions from the FSM National Government amounted to $1,200,000 and $1,495,000, respectively, of which $900,000 and $0 is receivable from the FSM National Government as of December 31, 2011 and 2010, respectively.

(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, 2011 and 2010, had received an allocation of $272,797 and $89,593, respectively, from PSTFA of which $253,765 and $271,407 were paid as benefits during the years ended December 31, 2011 and 2010, 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, 2011 and 2010, the amount available for future benefit payments under the Prior Service Benefits Program amounted to $26,900 and $43,035, respectively.

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

Combining Statement of Net Assets
December 31, 2011

	Retirement Fund	Prior Service Fund	Total
ASSETS			
Cash and cash equivalents	$ 1,209,552	$ 70,650	$ 1,280,202
Receivables:			
Contributions	3,051,613	-	3,051,613
Accrued interest	91,721	-	91,721
Other	911,668	-	911,668
Total receivables	4,055,002	-	4,055,002
Prepayments	4,780	-	4,780
Investments:			
Fixed income	13,384,226	-	13,384,226
Stocks	21,836,645	-	21,836,645
Total investments	35,220,871	-	35,220,871
Fixed assets, net	109,787	-	109,787
Total assets	40,599,992	70,650	40,670,642
LIABILITIES			
Accounts payable	186,485	43,750	230,235
Other liabilities and accruals	22,598	-	22,598
Accrued management fees	8,440	-	8,440
Total liabilities	217,523	43,750	261,273
NET ASSETS			
Held in trust for retirement, disability and survivors' benefits	$ 40,382,469	$ 26,900	$ 40,409,369

See Accompanying Independent Auditors' Report.

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

Combining Statement of Changes in Net Assets
Year Ended December 31, 2011

	Retirement Fund	Prior Service Fund	Total
Additions:			
Contributions	$ 16,593,155	$ -	$ 16,593,155
Investment income (loss):			
Net change in the fair value of investments	(2,181,438)	-	(2,181,438)
Interest and dividends	969,040	231	969,271
Total investment income (loss)	(1,212,398)	231	(1,212,167)
Less investment expense:			
Investment management and custodial fees	(208,649)	-	(208,649)
Net investment income (loss)	(1,421,047)	231	(1,420,816)
Other additions:			
Contributions from FSM National Government	1,200,000	-	1,200,000
Other	78,437	272,797	351,234
	1,278,437	272,797	1,551,234
Total additions	16,450,545	273,028	16,723,573
Deductions:			
Benefit payments:			
Retirement	10,870,989	102,231	10,973,220
Survivors	4,881,958	151,534	5,033,492
Disability	1,395,552	-	1,395,552
Lump sum	217,981	-	217,981
Total benefit payments	17,366,480	253,765	17,620,245
Refunds	30,630	-	30,630
Administrative	1,032,036	35,398	1,067,434
Total deductions	18,429,146	289,163	18,718,309
Change in net assets	(1,978,601)	(16,135)	(1,994,736)
Net assets at beginning of year	42,361,070	43,035	42,404,105
Net assets at end of year	$ 40,382,469	$ 26,900	$ 40,409,369

See Accompanying Independent Auditors' Report.

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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 the financial statements of the Federated States of Micronesia Social Security Administration (the Administration) as of and for the year ended December 31, 2011, and have issued our report thereon dated June 15, 2012. We conducted our audit 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.

Internal Control Over Financial Reporting

Management of the Administration is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Administration's internal control over financial reporting as a basis for designing our auditing procedures 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 over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Administration's internal control over financial reporting.

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 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Administration's financial statements are free of 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*.

This report is intended for the information of the Board of Trustees, management, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLP

June 15, 2012

Summary Schedule of Prior Year Findings
Year Ended December 31, 2011

There are no prior year findings unresolved as of December 31, 2011.