

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(AN EXPENDABLE TRUST FUND)**

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT**

NINE MONTHS ENDED DECEMBER 31, 2000

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(AN EXPENDABLE TRUST FUND)**

Nine Months Ended December 31, 2000
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INDEPENDENT AUDITORS' REPORT

Board of Directors
FSM Social Security Administration:

We have audited the accompanying balance sheet of the Federated States of Micronesia (FSM) Social Security Administration (an Expendable Trust Fund), a component unit of the FSM National Government, as of December 31, 2000, and the related statement of revenues, expenditures, and changes in fund balance for the nine months then ended. These financial statements are the responsibility of the FSM Social Security Administration's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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 *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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the FSM Social Security Administration as of December 31, 2000, and the results of its operations for the nine months then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 13, 2001, on our consideration of FSM Social Security Administration's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is stylized and appears to be written in a cursive or semi-cursive font.

April 13, 2001

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(AN EXPENDABLE TRUST FUND)**

Balance Sheet
December 31, 2000

	<u>Retirement Fund (An Expendable Trust Fund)</u>	<u>General Fixed Assets Account Group</u>	<u>Total</u>
<u>ASSETS</u>			
Cash and equivalents	\$ 1,619,368	\$ -	\$ 1,619,368
General receivables, net of an allowance for doubtful accounts of \$44,375	4,566	-	4,566
Advances	35,629	-	35,629
Prepaid expenses	4,460	-	4,460
Investment in fixed assets	-	155,294	155,294
Investments, at market value	<u>38,194,814</u>	<u>-</u>	<u>38,194,814</u>
Total assets	<u>\$ 39,858,837</u>	<u>\$ 155,294</u>	<u>\$ 40,014,131</u>
<u>LIABILITIES AND FUND BALANCES</u>			
Liabilities:			
Accounts payable - beneficiaries	\$ 41,071	\$ -	\$ 41,071
Accounts payable - general	44,594	-	44,594
Taxes/personnel benefits payable	<u>13,737</u>	<u>-</u>	<u>13,737</u>
Total liabilities	<u>99,402</u>	<u>-</u>	<u>99,402</u>
Fund balances:			
Reserved for investment in fixed assets	-	155,294	155,294
Fund balance reserved for retirement, disability and survivors benefits (note 3)	<u>39,759,435</u>	<u>-</u>	<u>39,759,435</u>
Total fund balances	<u>39,759,435</u>	<u>155,294</u>	<u>39,914,729</u>
Commitments and contingencies (note 4)			
Total liabilities and fund balances	<u>\$ 39,858,837</u>	<u>\$ 155,294</u>	<u>\$ 40,014,131</u>

See accompanying notes to financial statements.

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(AN EXPENDABLE TRUST FUND)**

Statement of Revenues, Expenditures and Changes in Fund Balance
Nine Months Ended December 31, 2000

Revenues:	
Contributions	\$ 6,914,414
Net investment loss	<u>(1,527,557)</u>
	5,386,857
Other income:	
Miscellaneous income	<u>5,441</u>
Total revenues	<u>5,392,298</u>
Expenditures:	
Benefit payments	6,893,415
Refund contributions	43,781
Administrative expenses, net (note 6)	<u>623,172</u>
Total expenditures	<u>7,560,368</u>
Excess of expenditures over revenues	(2,168,070)
Fund balance at beginning of period	<u>41,927,505</u>
Fund balance at end of period	<u>\$ 39,759,435</u>

See accompanying notes to financial statements.

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
(AN EXPENDABLE TRUST FUND)**

Notes to Financial Statements
December 31, 2000

(1) Summary of Significant Accounting Policies

A. Basis of Accounting

The Federated States of Micronesia (FSM) Social Security Administration (the Administration) is accounted for as an Expendable Trust Fund and is a component unit of the FSM National Government. As an Expendable Trust Fund, the Administration's principal and income may be expended in the course of its designated operations, and accordingly, the Administration is accounted for in essentially the same manner as a governmental fund type. The financial statements of the Administration are presented under the modified accrual basis of accounting. Under the modified accrual basis, revenues are recognized when they become both measurable and available to finance expenditures of the current period and expenditures are generally recognized when the related liability is incurred.

Previously, the fiscal year end of the FSM Social Security Administration was March 31. Effective April 1, 2000, the FSM Social Security Administration changed its fiscal year end to December 31.

B. Budget

Within the confines provided by the Social Security Act, the FSM Social Security Administration does not require FSM Congress approval of its budget; as such, a statement of revenues, expenditures, and changes in fund balance - budget and actual is not presented.

C. Future Liabilities and Contributions

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

D. Cash and Equivalents

For the purposes of the balance sheet, cash and equivalents is defined as cash on hand, in bank checking and savings accounts, time certificates of deposit with initial maturities of ninety days or less and funds held by Pacific Century Trust, the trustee, in an automated cash management fund.

Cash and equivalents as of December 31, 2000, is comprised of the following:

Petty cash	\$ 1,200
Cash in bank - operations	4,778
Cash in bank - payroll	3,567
Cash in bank - benefits 3	(13,905)
Cash in bank - benefits 4	34,762
Savings accounts	280,455
Pacific Century Trust - automated cash management fund	<u>1,308,511</u>
	\$ <u>1,619,368</u>

**FEDERATED STATES OF MICRONESIA
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Notes to Financial Statements
December 31, 2000

(1) Summary of Significant Accounting Policies, Continued

D. Cash and Equivalents, Continued

Of the cash and equivalents, \$300,000 is subject to coverage by the Federal Deposit Insurance Corp. (FDIC) as of December 31, 2000. The remaining balance is uninsured. The Administration does not require collateralization of its deposits. Therefore, amounts exceeding FDIC insurable limitations are characterized as uncollateralized.

E. Investments

Investment in securities are carried at market value.

Generally, the FSM Social Security Administration can invest in bonds and other evidence of indebtedness of the FSM or U.S.; or of any State of the FSM and U.S.; in bonds, debentures, notes and other evidence of indebtedness issued or assumed by FSM or U.S. institutions; and in preferred or common stock of any corporation created or existing under the laws of the FSM or under the laws of the U.S., or any state, territory, or commonwealth.

Investments as of December 31, 2000, are comprised of the following:

Common stock	\$ 14,745,679
Investment in Sabre Partners, L.P.	6,529,954
U.S. government obligations	3,526,695
Government agencies	6,522,329
Corporate bonds and others	<u>6,870,157</u>
	\$ <u>38,194,814</u>

The investment in Sabre Partners L.P. of \$6,529,954 includes principal of \$5,000,000 and investment income of \$1,529,954. The Administration's legal counsel, in an opinion dated February 4, 2000, asserts that this transaction is not authorized under FSM statutes governing the FSM Social Security Retirement Fund. Additionally, the Administration's counsel asserts that the transfer of funds for the above investment was not performed in accordance with governing FSM statutes. This investment was liquidated on February 28, 2001.

Net investment loss as of December 31, 2000, is comprised of the following:

Equity share in undistributed net income	\$ 701,040
Income-interest and dividends	727,767
Realized gains on sale	1,769,944
Unrealized gains	3,473,887
Actual loss on sale	(759,908)
Unrealized losses	(7,196,826)
Investment fees	(261,281)
Interest income, net	<u>17,820</u>
Net investment loss	\$ <u>(1,527,557)</u>

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
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Notes to Financial Statements
December 31, 2000

(1) Summary of Significant Accounting Policies, Continued

E. Investments, Continued

GASB Statement No. 3 requires government entities to categorize investments in the following categories to give an indication of the level of risk assumed by the entity.

Category 1 - Insured or registered, or securities held by the Administration or its agent in the Administration's name.

Category 2 - Uninsured and unregistered, or securities held by a party other than the Administration or its agent, in the Administration's name.

Category 3 - Uninsured and unregistered, securities held by a party other than the Administration and not in the Administration's name.

The Administration's demand and time deposits are non-categorized investments in accordance with Governmental Accounting Standards Board (GASB) Statement No. 3. All other investments held by the Administration have been classified as category 1 investments in accordance with GASB No. 3 as all investments are held in the name of the FSM Social Security Administration by the Pacific Century Trust, the trustee.

F. Fixed Assets

The accounting and reporting treatment applied to fixed assets and long-term liabilities associated with a fund are determined by its measurement focus. All governmental funds and expendable trust funds are accounted for on a spending or "financial flow" measurement focus. This means that only current assets and current liabilities are generally included on their balance sheets. Their reported fund balance (net current assets) is considered a measure of "available spending resources." Governmental fund operating statements present increases (revenues and other financing uses) in net current assets. Accordingly, they are said to present a summary of sources and uses of "available resources" during a period.

Fixed assets used in governmental fund type operations (general fixed assets), are accounted for in the General Fixed Assets Account Group rather than in governmental funds. Fixed assets consist of furniture, fixtures and equipment and are recorded at cost. Depreciation is provided over the estimated useful lives of the assets by the straight-line method.

This account group is not a "fund." It is concerned only with the measurement of financial position and is not involved with measurement of results of operations.

Fixed assets accounted for in the General Fixed Assets Account Group as of December 31, 2000, are as follows:

**FEDERATED STATES OF MICRONESIA
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Notes to Financial Statements
December 31, 2000

(1) Summary of Significant Accounting Policies, Continued

F. Fixed Assets, Continued

<u>Asset Categories</u>	<u>Estimated Useful lives</u>	
Computer software and hardware	5 years	\$ 115,709
Office furniture, fixtures and equipment	5 years	109,978
Home furnishings	5 years	7,103
Vehicles	5 years	<u>113,168</u>
		345,958
Less accumulated depreciation		<u>190,664</u>
		<u>\$ 155,294</u>

G. Contributions

Contributions to the 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 five percent of wages received.

Maximum quarterly taxable wages are currently \$3,000. Every employer is required to contribute an amount equal to that contributed by employees.

Contributions as of December 31, 2000, are comprised of the following:

Government employment	\$ 3,881,144
Private employment	2,980,683
Penalties and interest	<u>52,587</u>
	<u>\$ 6,914,414</u>

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 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.

**FEDERATED STATES OF MICRONESIA
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Notes to Financial Statements
December 31, 2000

(1) Summary of Significant Accounting Policies, Continued

H. Benefit Obligations, Continued

Benefits are paid monthly and are computed upon an annual basis of 16.5% of the first \$10,000 of cumulative covered earnings, plus 3.0% of the next \$30,000, and 2.0% of any earnings in excess of \$40,000. The minimum benefit payment is \$50 per month.

Benefit payments as of December 31, 2000, are comprised of the following:

Retirement pension	\$ 4,033,876
Survivor pension	2,449,599
Disability pension	368,627
Lump sum pension	<u>41,313</u>
	\$ <u>6,893,415</u>

I. Totals - Memorandum Only

The "Totals - Memorandum Only" column represents an aggregate of the individual financial statements. The total column is presented for overview information purposes and does not represent consolidated financial information.

J. Management Estimates

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

(2) Establishment of the Social Security Administration

The Social Security Administration of the Federated States of Micronesia 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 providing retirement, disability and death benefits to qualified individuals and their survivors. The Administration is administered under the authority of a six-member board, five of which 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.

(3) Reservation of Fund Balance

The reservation of fund balance has been established 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.

**FEDERATED STATES OF MICRONESIA
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Notes to Financial Statements
December 31, 2000

(4) Commitments and 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 above mentioned liabilities at this time; however management is of the opinion that the amount is not material to the financial statements taken as a whole.

The FSM Social Security Administration undergoes periodic actuarial evaluations. The latest is as of April 1, 2000. The report indicates that although there is sufficient uncertainty concerning future economic developments to recommend against any benefit improvements at the current time, and while such future developments may make future adjustments in benefits and contributions necessary, there is not yet sufficient indication to show a need for immediate adjustment.

(5) Contributions Receivable

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

(6) Prior Service Claims

Under the terms of the Prior Service Claim Adjudication Service Agreement between the Prior Service Trust Fund Administration and the Social Security Administration of the Federated States of Micronesia, the FSM Social Security 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 will reimburse the Social Security Administrator \$8,000 per annum plus an amount equal to 8% of the total amount of automated and manual benefit payments.

The compensation based on the above agreement aggregating \$43,797 is netted against administrative expenses in the accompanying financial statements for the nine months ended December 31, 2000.



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED UPON THE AUDIT PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

The Board of Directors
FSM Social Security Administration:

We have audited the financial statements of the FSM Social Security Administration (an Expendable Trust Fund), as of and for the nine months ended December 31, 2000, and have issued our report thereon dated April 13, 2001. 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.

Compliance

As part of obtaining reasonable assurance about whether FSM Social Security Administration's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 instances of noncompliance that are required to be reported under *Government Auditing Standards*.

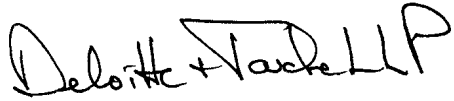
As explained in finding No. 2000-1 on page 11, the FSM Social Security Administration made a certain investment during the year ended March 31, 2000. The Administration's legal counsel is of the opinion that this investment was not authorized under statutes governing the FSM Social Security Retirement Fund. Additionally, counsel is of the opinion that the transfer of funds for the Administration's investment was also not performed in accordance with governing FSM statutes. This investment was subsequently liquidated on February 28, 2001.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered FSM Social Security Administration's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operations that we consider to be material weaknesses.

We noted other matters involving the internal control over financial reporting that we have reported to management of the FSM Social Security Administration in a separate letter dated April 13, 2001.

This report is intended for the information of the Board of Directors and management of FSM Social Security Administration, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

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

April 13, 2001

**FEDERATED STATES OF MICRONESIA
SOCIAL SECURITY ADMINISTRATION
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Schedule of Findings and Questioned Costs
Nine Months Ended December 31, 2000

Investments

Finding No. 2000-1

Criteria: All transactions of the FSM Social Security Administration should comply with FSM statutes governing the FSM Social Security Retirement Fund.

Condition: The FSM Social Security Administration invested \$5,000,000 in Sabre Partners, L.P. The Administration's legal counsel, in an opinion dated February 4, 2000, asserts that the above transaction is not authorized under FSM statutes governing the FSM Social Security Retirement Fund. Additionally, the Administration's counsel asserts that the transfer of funds for the above investment was not performed in accordance with governing FSM statutes.

Cause: The cause of the above condition is not known.

Effect: Material noncompliance with FSM statutes could be the result of this condition.

Recommendation: We recommend the Board and management review the above and resolve this issue with its legal counsel and the FSM attorney general.

Auditee Response: This investment was subsequently liquidated on February 28, 2001 and is no longer part of our investment portfolio.