MARSHALL ISLANDS SOCIAL SECURITY ADMINISTRATION

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

YEAR ENDED SEPTEMBER 30, 2003

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Marshall Islands Social Security Administration:

We have audited the accompanying statement of net assets of the Marshall Islands Social Security Administration (MISSA), a component unit of the Republic of the Marshall Islands, as of September 30, 2003, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the management of MISSA. 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 *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 MISSA as of September 30, 2003, and the changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in note 2 to the accompanying financial statements, MISSA adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus,* and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*.

The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by GASB. This information is the responsibility of MISSA's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required 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 February 13, 2004 on our consideration of MISSA'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.

Deloitte + Touche LLP

February 13, 2004

MARSHALL ISLANDS SOCIAL SECURITY ADMINISTRATION
Management's Discussion and Analysis

The following Management's Discussion and Analysis of the Marshall Islands Social Security Administration's (MISSA) financial performance provides an overview to the financial statements of MISSA for the year ended September 30, 2003. Since the MD&A is designed to focus on current activities, resulting changes and current known facts, we encourage the readers to consider it in conjunction with the audited financial statements, which follow this section.

REQUIRED FINANCIAL STATEMENTS

MISSA, a component unit of the Republic of the Marshall Islands (RepMar), prepares its financial statements on an accrual basis in accordance with generally accepted accounting principles promulgated by the Governmental Accounting Standards Board (GASB). The Statement of Net Assets reflects all of MISSA's assets and liabilities and provides information on the nature and amount of investments available to ensure payment of retirement, survivors and disability benefits.

FINANCIAL ANALYSIS OF MISSA

The Statement of Net Assets on page 7 and the Statement of Changes in Net Assets on page 8 provide an indication of MISSA's financial condition. MISSA's net assets reflect the difference between assets and liabilities. An increase in net assets over time typically indicates an improvement in financial condition. While these statements measure the value of MISSA's net assets and the changes to them, another important factor to consider in determining the financial health of MISSA is its funded status.

In fiscal year 2003, additions to net assets significantly exceeded total deductions to net assets. Specifically, total contributions of $13,035,585, investment income of $6,758,873 and other income of $985 exceeded total deductions of $12,787,542 by $7,007,901. This net increase in assets of $7,007,901 has brought MISSA's net asset base to $41,548,753. For actuarial purposes, MISSA's actuary uses the current value of assets in conjunction with the actuarial valuation of the MISSA's accrued liabilities to determine MISSA's funded status. As of October 1, 2001, MISSA had an accrued actuarial liability (AAL) of approximately $218 million. Assets held by MISSA covered approximately $35 million or 16% of the AAL. The unfunded AAL was therefore $183 million. A more recent valuation of MISSA's liabilities as of October 1, 2003 is being prepared and its findings will be disclosed in fiscal year 2004.

A summary of MISSA's Statement of Net Assets is presented below. We opted not to include the previous year's financial performance for comparative purposes in this year's discussion due to the fact that this is the first year for MISSA to implement GASB Statement No. 34 Governmental Reporting Requirements. Additionally, you will notice that MISSA's financial statements for fiscal year 2003 contain information pertaining only to the assets and liabilities of the Retirement Fund. In fiscal year 2002, the administration and control of the Basic Health Benefits Plan and the Supplemental Health Benefits Plan (collectively, the "Health Fund") and the Health Care Revenue Fund were transferred to RepMar's Ministry of Health and Environment (MOHE). As part of an agreement with MOHE, MISSA will continue to collect Health Fund contributions on behalf of MOHE.

ASSETS		
Cash and cash equivalents		$ 1,796,098
Time certificates of deposit		3,537,759
Receivables, net:		
Contributions	1,764,186	
Other	723,957	
		2,488,143
Due from affiliates, net		1,300,300
Investments:		
Common stocks	7,551,878	
Mutual funds	25,300,386	
		32,852,264
Fixed assets, net		355,390
Total assets		42,329,954
LIABILITIES		
Accounts payable		238,500
Other liabilities and accruals		154,913
Due to Ministry of Health		387,788
Total liabilities		781,201
NET ASSETS		
Held in trust for retirement benefits and other purposes		$ 41,548,753

Statement of Changes in Net Assets

Summarized below is the Statement of Changes in Net Assets for the year ended September 30, 2003.

ADDITIONS:	
Contributions	$ 13,035,585
Investment income	6,758,873
Other	985
Total additions	19,795,443
DEDUCTIONS:	
Benefit payments	9,276,506
Bad debts	2,631,257
Other	879,779
Total deductions	12,787,542
Change in Net Assets	7,007,901
Net Assets at Beginning of Year	34,540,852
Net Assets at End of Year	$ 41,548,753

Additions:

Of the total $19,795,443 in additional assets for fiscal year 2003, 65% or $13,035,585 was generated from contributions and the other 35% or $6,758,873 was generated from investments. MISSA's focus on implementing stricter controls on tax collections and enforcing penalties and interest on delinquent employers have been paramount in the increase in total revenues from contributions as more employers have voluntarily settled old accounts. Promissory notes executed and signed during the year amounted to $1,764,186, net of allowances. Investment income totaled $6,758,873, which reflects a 27.1% return on investments for the year. In light of the previous two years' negative investment performance, the income gained from investments this fiscal year alone was remarkable.

The following table presents MISSA's investment allocations as of September 30, 2003 by weight %, target %, market value and target value:

Investment Type	Weight %	Target %	Market Value	Target Value
Small Cap	6.9%	6.0%	$ 1,964,062	$ 1,712,509
Small Cap Value	10.1%	9.0%	2,881,836	2,568,763
Large Cap	5.3%	6.0%	1,511,587	1,712,509
Large Cap Value	8.7%	9.0%	2,472,114	2,568,763
Int'l Small Cap	7.2%	6.0%	2,058,584	1,712,509
Int'l Small Cap Value	9.4%	7.5%	2,696,109	2,140,636
Int'l Large Cap	5.7%	6.0%	1,634,139	1,712,509
Int'l Large Cap Value	7.8%	7.5%	2,239,032	2,140,636
Emerging Markets	3.4%	3.0%	969,093	856,255
Bonds/Fixed Income	35.1%	39.5%	10,019,556	11,274,017
Cash & Equivalents	0.4%	0.5%	95,703	142,709
	100.0%	100.0%	$ 28,541,815	$ 28,541,815

On November 11, 2002, MISSA formally acquired the services of a new Investment Advisor, Investor Solutions, Inc. and a new Custodian, Fidelity Investments Institutional Brokerage Group (FIIBG). Consequently, MISSA's policy on investments was modified and adopted by MISSA's Board of Directors on October 21, 2002. The above target allocations were established with total allocations limited to 60% for equities and 40% for bonds. With the exception of MISSA's investment in the Bank of the Marshall Islands (BOMI)*, all investments are limited to no-load mutual funds, unit investment trusts, Exchange Trade Funds, close-end mutual funds and other diversified marketable securities.

For the year ended September 30, 2003, the fair market value of MISSA's investments in the U.S. and International markets increased by $5,120,371. In addition, a total of $894,148 in dividends and interest payments were made and subsequently reinvested.

* MISSA presently holds a 32% interest in the Bank of the Marshall Islands. For the year ended September 30, 2003, MISSA's 64,485 shares at BOMI increased in value by $647,627. An annual dividend payment of $96,727 was received from BOMI in April 2003. As of September 2003, the shares at BOMI were valued at $4,406,152.

Deductions:

Deductions represent benefit payments, investment management fees, administrative expenses and a provision for doubtful accounts, which totaled to \$12,787,542. This amount was fully covered by the amount of contributions generated during 2003. Benefit payments have been steadily increasing by an average of 6% per annum with fiscal year 2003 paying out \$9,276,506 in total benefits. Administrative expenses and investment fees, on the other hand, have been kept to a minimum of \$783,436 or 3.95% of total income and \$96,343 respectively. Please note that MISSA's allowable ceiling in any given year for administrative expenditures as specified by the Social Security Act of 1990, as amended, is 20% of total contributions and investment income for that year.

FUTURE ECONOMIC OUTLOOK

Fiscal year 2003 ended with high optimism of improved voluntary tax compliance in the coming years, as more employers came forward willingly to pay their contributions. Delinquencies were reduced, as enforcement actions by MISSA became known. An increase in tax collection is expected, particularly in 2004, as Tax Auditors are sent out in the field to examine prior years' payroll records and past quarterly returns filed.

MISSA's investments have begun to recover from the period of recession. Hopefully, this trend will continue, thereby increasing MISSA's total assets and decreasing the unfunded Actuarial Accrued Liabilities (AAL). The effect of the newly extended Compact of Free Association, and its related funding and grants, on local businesses is uncertain, but looks promising.

These factors, directly or in some ways, should help MISSA reach its targeted revenues and sustain its retirement benefit programs and the healthcare services of the Ministry of Health and Environment in 2004 and for some years to follow.

MARSHALL ISLANDS SOCIAL SECURITY ADMINISTRATION

Statement of Net Assets
September 30, 2003

ASSETS	
Cash and cash equivalents	$ 1,796,098
Time certificate of deposit	3,537,759
Receivables, net:	
Contributions	1,764,186
Other	723,957
Total receivables, net	2,488,143
Due from affiliates, net	1,300,300
Investments:	
Stocks	7,551,878
Mutual funds	25,300,386
Total investments	32,852,264
Fixed assets, net	355,390
Total assets	42,329,954
LIABILITIES	
Accounts payable	238,500
Other liabilities and accruals	154,913
Due to Ministry of Health and Environment	387,788
Total liabilities	781,201
Contingencies	
NET ASSETS	
Held in trust for retirement benefits and other purposes	$ 41,548,753

See accompanying notes to financial statements.

MARSHALL ISLANDS SOCIAL SECURITY ADMINISTRATION

Statement of Changes in Net Assets
Year Ended September 30, 2003

Additions:	
Contributions:	
Private employees	$ 9,526,060
Government employees	2,628,409
Penalties and interest	881,116
Total contributions	13,035,585
Investment income:	
Net increase in the fair value of investments	5,864,725
Dividends	509,744
Interest	384,404
Total investment income	6,758,873
Other	985
Total additions	19,795,443
Deductions:	
Benefit payments:	
Retirement	4,927,656
Survivors	3,147,516
Disability	1,094,131
Reduction-in-force	55,052
Lump sum	52,151
Total benefit payments	9,276,506
Bad debts	2,631,257
Administrative	783,436
Investment management and custodial fees	96,343
Total deductions	12,787,542
Change in net assets	7,007,901
Net assets at beginning of year	34,540,852
Net assets at end of year	$ 41,548,753

See accompanying notes to financial statements.

(1) Organization

The Marshall Islands Social Security Administration (MISSA), a component unit of the Republic of the Marshall Islands (RepMar), was established pursuant to RepMar Public Law 1990-75 (the Social Security Act of 1990), as amended. The law repealed the Social Security Act of 1987 and established MISSA to administer the Marshall Islands Social Security Retirement Fund (the Retirement Fund). The Retirement Fund was established to provide a financially sound social security system with pension benefits and early retirement, whereby workers would be ensured a measure of security in their old age and during disability, and whereby surviving spouses and surviving children of deceased workers would be ensured support after the loss of the family's income.

Contributions to the Retirement Fund are governed by the Social Security Act of 1990, as amended, which imposes a tax on the quarterly income of every employee not currently subject to the United States Social Security System or any other recognized Social Security System equal to seven percent of wages received.

Maximum quarterly taxable wages are $5,000. Every employer is required to contribute an amount equal to that contributed by employees.

Retirement benefits are paid to every person who is a service insured or a fully insured individual as defined by the Social Security Act of 1990, as amended, has attained an age of sixty years 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 and are not working may also receive benefits until age eighteen (18) or up until age twenty-two (22), if in school. Eligible children who become disabled before age twenty-two 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.

Effective October 1, 1990, benefits are paid monthly and are computed as follows:

a) Pension element - two percent of index covered earnings, plus;

b) Social element - 14.5% of the first $11,000 of cumulative covered earnings plus 0.7% of cumulative covered earnings in excess of $11,000 but not in excess of $44,000. The $11,000 and $44,000 bend points may be increased from time to time by wage index adjustments granted by the Board of MISSA.

The minimum benefit is $129 per month, effective October 1, 1995.

The Reduction-in-Force (RIF) benefits are paid to those laid-off civil service employees during the downsizing process of RepMar through the Public Sector Reform Program. The monthly benefit payments are paid out on the basis of the current benefit rules of MISSA, as if the employee were aged fifty-five and "service insured", for a maximum period of three years, or for as long as the funds are available. Pursuant to the RIF program, MISSA expended RIF benefit payments amounting to $55,052 for the year ended September 30, 2003.

MISSA operates under the authority of a seven-member Board of Directors appointed by the Cabinet of RepMar.

(2) Summary of Significant Accounting Policies

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. In June 2001, GASB issued Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus* and Statement No. 38, *Certain Financial Statement Note Disclosures*, which amended certain provisions of GASB Statement No. 34. MISSA is required to adopt GASB Statement No. 34, as amended by GASB Statement No. 37, and certain provisions of GASB Statement No. 38 in fiscal year 2003. These statements establish financial reporting standards for governmental entities, which include the requirement for MISSA 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 into the following net asset categories:

- Invested in capital assets, net of related debt:

  Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

  Nonexpendable - net assets subject to externally imposed stipulations that require MISSA to maintain them permanently. For the year ended September 30, 2003, MISSA does not have nonexpendable net assets.

  Expendable - net assets whose use by MISSA is subject to externally imposed stipulations that can be fulfilled by actions of MISSA pursuant to those stipulations or that expire by the passage of time.

- Unrestricted:

  Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

Management of MISSA has determined that per its enabling legislation, all net assets of MISSA are restricted for retirement, disability and survivors' benefits.

A. Basis of Accounting

MISSA 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.

B. Future Liabilities and Contributions

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

(2) Summary of Significant Accounting Policies, Continued

C. Cash and Cash Equivalents and Time Certificates of Deposit

For the purposes of the statement of net assets, cash and cash equivalents include cash in checking and savings accounts as well as short-term investments with original maturities of three months or less from the date acquired. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified. As of September 30, 2003, the carrying amount of MISSA's cash and cash equivalents and time certificates of deposit was $5,333,857, and the corresponding bank balance was $5,904,115, which is maintained in financial institutions not subject to Federal Deposit Insurance Corporation (FDIC) insurance.

D. Investments

Investments are stated at fair value as of September 30, 2003. Fair value is the amount at which an investment could be exchanged in a current transaction between willing parties.

An investment of 20% or more of the voting stock of an investee is presumed to give the investor significant influence. Under the equity method, the investor records, as earnings or loss, its proportionate share of the investee's earnings or loss.

E. Receivables and the Allowance for Doubtful Accounts

Contributions receivable are due from employers located within the Republic of the Marshall Islands. Premiums receivable are due from members located within the Republic of the Marshall Islands and the United States of America. These receivables are not collateralized and are non-interest bearing.

The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts. The allowance is established through a provision for bad debts charged to expense.

F. Fixed Assets

Fixed assets are capitalized at their cost at the time of acquisition. Depreciation is provided using the straight-line basis over the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

Building and improvements	20 years
Motor vehicles	3 years
Computer equipment	4 years
Office equipment	5 years
Furniture	3 - 10 years

(2) Summary of Significant Accounting Policies, Continued

G. Compensated Absences

Vested or accumulated vacation leave that is expected to be liquidated with expendable available financial resources is reported as an expenditure and a fund liability of the expendable trust fund. The liability as of September 30, 2003, is $20,640 and is included in the statement of net assets within other liabilities and accruals. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits. The accumulated estimated amount of unused sick leave as of September 30, 2003, is $9,660.

Annual leave accumulates at the rate of one working day per bi-weekly pay period.

H. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires 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, expenditures and expenses during the reporting period. Actual results could differ from those estimates.

I. New Accounting Standards

For fiscal year 2004, MISSA will be implementing GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units* and GASB Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3)*. For fiscal year 2005, MISSA will be implementing GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. As of the date of the opinion, MISSA has not evaluated the financial statement impact of GASB Statement Nos. 39, 40 and 42.

J. Restatement

Due to the implementation of GASB Statement Nos. 34, 35 and 37, the beginning net assets of the statement of net assets have been restated. Fund balance of the governmental funds at September 30, 2002 was increased by $277,812 for the cumulative effect of these changes on years prior to fiscal year 2003. The effect on those items is as follows:

Fund balances reported as of September 30, 2002	$ 34,263,040
Adjustments:	
Capital assets	537,154
Accumulated depreciation	(259,342)
	277,812
Beginning net assets as of September 30, 2002	$ 34,540,852

(3) Investments

GASB Statement No. 3 requires MISSA to categorize investments to give an indication of the level of credit risk assumed at year end. The three categories are described below:

Category 1	Insured or registered, or securities held by MISSA or its agent in MISSA's name;
Category 2	Uninsured and unregistered, with securities held by the broker's or dealer's trust department or agent in MISSA's name; or
Category 3	Uninsured and unregistered, with securities held by the broker or dealer, or by its trust department or agent but not in MISSA's name.

MISSA's investments as of September 30, 2003, are as follows:

	Categories			Fair
	1	2	3	Value
Common stocks	$ 4,406,152	$ 3,145,726	$ -	$ 7,551,878
Mutual funds	-	25,300,386	-	25,300,386
	$ 4,406,152	$ 28,446,112	$ -	$ 32,852,264

MISSA holds a 32% interest in Bank of Marshall Islands (BOMI), which engages in commercial banking services in the Republic of the Marshall Islands. As of September 30, 2003, MISSA maintained deposit accounts and a time certificate of deposit with BOMI of $5,808,413

A summary of unaudited financial information as of and for nine months ended September 30, 2003, for investees accounted for using the equity method of accounting for investments, is as follows:

Assets	$ 60,276,889
Liabilities	$ 46,197,383
Net earnings	$ 14,079,506

(4) Receivables

Receivables as of September 30, 2003, including applicable allowances for doubtful accounts, are as follows:

Contributions	$ 1,764,186
Other	4,453,085
	6,217,271
Less allowance for doubtful accounts	(3,729,128)
	$ 2,488,143

(5) Due from Affiliates

Receivables from affiliates as of September 30, 2003, including applicable allowances for doubtful accounts, are as follows:

Ministry of Health and Environment	$ 1,188,954
Other RepMar ministries	154,019
	1,342,973
Less allowance for doubtful accounts	(42,673)
	$ 1,300,300

On November 4, 2003, MISSA entered into a debt reduction agreement with the Ministry of Health and Environment (MOHE) for the repayment of certain receivables in the amount of $1,177,964. Under the terms of this agreement, MOHE is required to make interest-free quarterly payments of $60,000 commencing on January 1, 2004.

(6) Capital Assets

Capital asset activity for the year ended September 30, 2003, was as follows:

	October 1, 2002	Additions	Retirements	September 30, 2003
Buildings and improvements	$ 382,259	$ 80,038	$ -	$ 462,297
Motor vehicles	5,345	73,994	-	79,339
Computer equipment	56,532	19,681	-	76,213
Furniture	49,123	13,940	-	63,063
Office equipment	43,895	3,100	-	46,995
	537,154	190,753	-	727,907
Less accumulated depreciation and amortization	(259,342)	(113,175)	-	(372,517)
	$ 277,812	$ 77,578	$ -	$ 355,390

(8) Contingency

In October 2001, MISSA obtained an actuarial valuation of the Retirement Fund as of September 30, 2001. The valuation reported actuarial accrued liabilities for the Retirement Fund of $217,959,000. As of September 30, 2003, MISSA recorded total fund equity of $41,548,753 as funds available to fund future benefit obligations. These conditions indicate that MISSA may be unable to meet its future benefit obligations.

(9) Risk Management

MISSA 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. MISSA has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. MISSA is also exposed to investment risk. This risk is limited to diversification of the portfolio, establishment and monitoring of investment policies and guidelines, and monitoring of investment performance. In addition, investment consultants monitor MISSA's activities and advise the Board of Directors.